

Fiscal provisions in the Indian constitution:

Federal and counter tendencies-brief overview

R Mohan

The Honorary Fellow, GIFT

The fiscal provisions in Indian Constitution have been more or less adopted from the Government of India Act, 1935. Personal income tax collected by the Union was treated as the balancing factor to ameliorate vertical fiscal imbalances between the Union and the States. Consequent to the Government of India Act, 1935, the Otto Neimeyer Commission suggested sharing of 50 per cent personal income tax with the provinces. In the Constituent Assembly, the report of the Nalini Ranjan Sarkar committee was considered and ultimately, no fixed share of personal income tax was fixed in the constitutional provisions. Under Article 280 of the Constitution, Finance Commissions are to be constituted every five years or earlier, as per a Presidential notification and the Commission shall make recommendations to the President on the prescribed share of the taxes collected by the Union to the States and how this has to be distributed among the States. Till the 80th constitutional amendment, only personal income tax was mandatorily shareable and central excise duty was shareable through legislation as per Article 272 (which is not in existence after the 80th amendment). Based on the recommendations of the 10th Finance Commission, 80th constitutional amendment made all taxes collected by the Union (except surcharges and cesses) became shareable with the States. This has come into effect from 2000-2005 onwards. Through this, a long standing demand of the States was met. Till then, the grievance of the States was that more buoyant taxes like corporation tax and customs duties were kept outside the divisible pool of taxes. This is an important federal tendency in the fiscal area.

The provision for mandatory constitution of Finance Commission itself is an important federal feature of the Indian Constitution. The recommendations of the Finance Commission are submitted to the President, who shall cause it to be laid before each House of Parliament along with an explanatory memorandum as to the action taken thereon as required under Article 281 of the Constitution.

The share of taxes accepted by the President does not form part of Consolidated Fund of India and is not voted in the Parliament. The grants recommended by the Finance Commissions under Article 275 of the Constitution to the States in need of assistance are charged to the Consolidated Fund of India and hence not subject to vote in Parliament.

Under Article 74 of the Indian Constitution, President is bound to act in accordance with the aid and advice of the Council of Ministers headed by the Prime Minister. Though, President can ask the Council of Ministers to reconsider the advice, if the same advice is tendered again, President is bound to act in accordance with it, in short, the Union Cabinet can modify the recommendations of the Finance Commission submitted to the President. Finance Commission decides on the recommendations regarding distribution of taxes and disbursement of grants after hearing the sides of the Union and the States. The fact that one of the parties before the Commission, the Union can alter its recommendations is an unitary feature of Indian Constitution. But so far, the recommendation of the Finance Commission regarding share of taxes to be distributed to the States or the formula for distribution among the States have not been altered by the Union. This is a federal feature that has evolved through practise. But other recommendations like that of the Third Finance Commission on the Commission taking a holistic view of the revenue account of the States, including plan and non-plan, was not accepted by the Union Government. The Member Secretary to the Commission had written a dissent note that the Commission should confine to the non-plan side of the revenue account of the States and this was accepted by the Union. But later, the recommendation of the Ninth Finance Commission (for the period 1990-95) for considering the plan side also was accepted.

After five year plans have been done away with after 2015-16, the Fourteenth and Fifteenth Finance Commissions have considered revenue account as a whole for recommending grants under Article 275.

The Fourteenth Finance Commission did not recommend conditional grants to the States. This was an important step towards fiscal federalism. On subjects enumerated in the State List of the Seventh Schedule of the Constitution, the States will have freedom to spend according to their priorities. But the Fifteenth Finance Commission has given conditional grants.

The grants other than those given based on the recommendations of the Finance Commission, which is a constitutional body, are given under Article 282, which is under Miscellaneous Financial Provisions. But the discretionary grants given under Article 282, comprises four-fifths of the total central grants to the States. This includes central assistance to Centrally Sponsored Schemes (CSS). The criteria of CSS are fixed by the ministries of Government of India and States have very limited flexibility. The Ninth Finance Commission report constrains a discussion on whether grants under Article 282 can be disbursed as a matter of routine, ultimately, Supreme Court in *Bhim Singh Vs Union of India and others* (5 SCC 538, 2010) held that Article 282 is not subject to any other Article of the Constitution and its scope is not restricted and the only requirement is that it should be for a public purpose. The apex court upheld the validity of the Members of Parliament Local Area Development Scheme (MPLADS) in this case.

The general power to disburse discretionary grants not through the route of the Finance Commissions gives Union a wide latitude to disburse grants through State specific packages.

In the interests of cooperative federalism, grants should be disbursed on the basis of criteria and States should have the maximum flexibility to spend in the subjects enumerated in the State List.

We have already noted that the fiscal resource sharing arrangement is an important federal feature of our Constitution. But when emergency provisions are invoked (Article 352), Union can modify the provisions of Articles 270 to 279 (Article 354). It is in the provisions of these Articles that fiscal sharing arrangements with the States are mentioned, Even though, the Finance Commissions will have to be constituted every quinquennium, even when emergency provisions are invoked, the fiscal sharing arrangements can be modified. This is a very important unitary feature. But this provision has not so far been invoked.

Another power which the Union has is the proclamation of Financial Emergency (Article 360) in whole or part of India. When such an emergency is in force in part of India, President can issue directions all money bills and bills requiring Finance memorandum under Article 207, will have to be sent for Presidential assent. This power makes the fiscal provisions completely unitary when Financial Emergency is invoked. So far, this provision also has not been invoked.

By virtue of powers under Article 293 (3), States which have loans or guarantees from the Union are to get Union's approval before further borrowings, the pressure on the States to adhere to deficit targets in Fiscal Responsibility Legislations (FRAs) is more than that of the Union.

In the fiscal provisions, Indian Constitution has important federal features like constitution of Finance Commissions, there are substantial provisions with unitary nature, though these have so far not been invoked. In a meaningful cooperative set up, how these provisions are worked is most important.

References

Constituent Assembly Debates on Draft Articles 268 and 269

Reports of the 9, 10,14 and 15 Finance Commissions