

UPSC
NCERT Summary
Center-State Relation- 2

FINANCIAL RELATIONS

Generally, in typical federation along with the distribution of legislative and administrative powers, the financial resources of the country are also so distributed as to ensure financial independence of the units. However, the Indian Constitution does not make a clearcut distribution of the financial resources and leaves much to be decided by the Central Government from time to time.

The financial resources which have been placed at the disposal of the state are so meagre that they have to look up to the Union Government for subsidies and contributions. The distribution of financial resources in India has broadly been made as follows.

- **Taxes exclusively assigned to the Union:** Income from certain subjects like customs and export duties, income tax, excise duty on tobacco, jute, cotton etc., corporation tax, taxes on capital value of assets of individuals and companies; estate duty and succession duty in respect of property and other than agricultural land; and income from the earning departments like the railways and postal departments have been exclusively assigned to the Union Government by the Constitution.
- **Taxes exclusively assigned to States:** Income from land revenue, stamp duty except on documents included in the Union List; succession duty and estate duty in respect of agricultural land; income tax on agricultural lands; taxes on goods and passengers carried by road or in land water; taxes on vehicles used on roads, animals, boats, taxes on the consumption or sale of electricity, tolls, taxes on lands and buildings ; taxes on professions, traders, calling and employment; duties on alcoholic liquors for human consumption, opium, Indian hemp and other narcotic drugs, taxes on the entry of goods into local areas, taxes on luxuries, entertainments, amusements, betting and gambling, etc. has been assigned to the States.
- **Taxes leviable by Union but collected and appropriated by the State:** The taxes on the following items are levied by the Union Government but the actual revenue from them is collected and appropriated by the States;
(i) stamp duties on bills of exchange, cheques, promissory notes, bills of

landing, letters of credit, policies of insurance, transfer of shares etc. ;
(ii) Excise duties on medicinal toilet preparation containing alcohol or opium or Indian hemp or other narcotic drugs.

- **Taxes levied and collected by the Union but assigned to states:** The taxes in this category are levied and collected by the Union Government although they are subsequently handed over to the states where from they have been collected. Such taxes included duties in respect of succession to property other than agricultural land; state duty in respect of property other than agricultural land terminal taxes on goods or passengers carried by railways, sea or air, taxes on railway freights and fares; taxes other than stamp duties on transactions in stock exchanges and future markets; taxes on the sale or purchase of news papers and on advertisements published there in; taxes on purchase or sale of goods other than newspapers where such sale or purchases take place in the course of inter -state trade or commerce.
- **Taxes levied and collected by the Union but shared with the States:** Taxes on income other than agricultural income and excise duties other than those on medicinal and toilet preparations are levied and collected by the Union Government but shared with the states on an equitable basis. The basis of distribution is determined by the Parliament through a law.

CENTRE - STATE RELATIONS: CONFLICT ZONE

Arising out of the nature of Centre - State relations as well as difference in political ideology of the ruling parties at the Centre and States, following major areas of tensions have emerged in Indian federalism.

- Role of Governor as a representative of the central Government with regard to appointing and dismissing State ministers and dissolution of the State Assemblies.
- Misuse of powers of imposition of President's Rule under Article 356.
- Reservation of Bills for the consideration of the President under Article 201.
- Sharing of finances, and central approval of state projects.
- Demand for autonomy by the States

Within these five major areas, there are several other issues of administrative and political processes that cause tensions in Centre - State relations

(i) Role of Governor

Such interferences by Governors in State Government affairs and abuse of their powers for partisan reason has been giving rise to a feeling of insecurity among

State and demand for settling the issues of appointment and dismissal of Governors themselves, their compulsion to act on the advice of Council of Ministers, and definite code for the exercise of discretionary powers. Governors role in the government of particular state often based on ruling party of the centre, This is the reason the ruling party reshuffle the post whenever it forms new government.

(ii) Misuse of Article 356

- The provision for imposition of President's rule in States under Article 356 was made to deal with serious situations as a life saving device to be used as a sure of last resort. However, in practice this article has been so frequently used for purely partisan interests that it has become almost poisonous for Indian political system.
- The use of Article 356 rests on the subjective satisfaction of the President. President's rule can be imposed either on the recommendations of Governor or even without that, that is, on the satisfaction of President (Prime Minister) himself.
- In the same manner, the Prime Minister can also make use of Article 365 to ensure that the administration in State is carried on in accordance with the provisions of the Constitution, and if other wise, dissolve the State Government on the basis of his own assessment of the representative character or otherwise.
- The Sarkaria Commission drawing attention to the repeated abuse of Article 356 has pointed out that during the period from 1951 to 1987, of the 75 occasions when the President's rule was imposed, only in 26 cases was President's rule inevitable. In recent past Bihar government was dissolved in the use of article 356.

(iii) Article 200 & 201

- The power of the Governor to reserve all bill, passed by the legislature for the President's assent is another cause of tension between the Centre and the State.
- This has especially been so in case where the Governor has reserved a bill against the advice of the State Ministry, presumably under the direction of the Central Government. The main purpose of this provision is that the Centre wants to keep a watch on the activities of the States.

(iv) Revenue

- One of the most controversial areas between the Centre and the State in a federal system is that of financial relations and the Indian federal system is no exception to this.
- The demand of the states for greater fiscal autonomy has now become one of the most debated issues of the Indian federation. The tension between Centre and States with regard to fiscal relations arises because of:
 - (i) Comparative powers of taxation,
 - (ii) Statutory versus discretionary grants, and
 - (iii) Economic planning.

(v) Fiscal Matters

- Sources of revenue to the Centre are relatively elastic and expansive as against those of the states. The Centre also controls vast resources generated through deficit financing, loans from organized money market in the country as well as huge funds of foreign aid.
- The residuary powers of taxation are also vested with the Central Government. In addition to this, Constitution also authorizes the Centre to collect surcharges on taxes to raise additional funds in times of emerging.
- In practice surcharge has become a permanent feature of income tax structure. Another loop hole in taxation system, on account of which states suffers, is the cooperative tax, which keeps on expanding and is in the exclusive purview of the Centre. The states there fore have to be dependent on Central assistance.

(vi) Grants - in - Aid

- With regard to sharing of resources and assignment of certain resources entirely to the State, Articles 280 and 281. provide for the appointment of an independent Finance Commission every fifth year or earlier as the President of India desires.
- The provision of Finance Commission was to regulate, co-ordinate and integrate the finances of the Government of India and the State Government. Originally, the Finance Commission was intended to cover all the financial transfers from the Centre to States.
- However, slowly Planning Commission has also been brought in for the purpose and now it plays a rather important part in devolution of resources from the Centre to the States. Since the Planning Commission is a completely Central institution and the politically influenced States have a sense of discrimination in location of grants.

- States are sore not only because of the fact that the Planning Commission's authority to determine the scope and pattern of a major portion of Central assistance to States has relegated the role of Finance Commission to a subsidiary one but also because the Centre does not seem to be much serious even about the reduced role of the Finance Commission. In addition, provision for grants-in-aid by the Centre is purely a political and arbitrary means of devolution and centre has been making use of this more and more and that too in a controversial manner.
- Centre gives grant-in-aid to States under Article 281 on its discretion for undertaking welfare schemes, meet natural calamities or for removal of disparities etc. A close scrutiny of the Central relief to the States affected by natural calamities indicates that no well considered norms were followed in this regard. The Central teams preoccupied by political considerations have always assessed the damage done by droughts, flood, etc. in an adhoc perfunctory manner.
- The States therefore, have sharply questioned the need for the Centre to wield heavy financial clout in the shape of discretionary grants. There are about the inherent danger of their being used as a political weapon against a State that happens to be out of favour with the Centre.

(vii) Economic Planning

- It is generally agreed that the process of planning in India has tended to push the political system to greater centralisation due to both the central control over resources for development and the preponderance of the centralised planning machinery.
- The grave and most harmful consequence of the atrophy of the state's domain in the economic field is in regard to industries and economic planning.
- Similarly it is alleged that in the name of national planning, the centre for political considerations has been inordinately delaying viable and important state projects. On the contrary, Centre has been superimposing its schemes on the States which deemed by State governments to be irrelevant to the conditions prevailing in the States

(viii) Demand for Autonomy

- The constituent units of the Indian Union i.e. the States have been developing a feeling of deprivation on the ground that the Centre has denied them the autonomy that has been guaranteed under the

Constitution. Unfortunately despite changes in Government, the trend towards centralization has not been weakened.

- In this context the demand for a greater and more meaningful devolution of power has been assertively and more stridently articulated over the years. The Administrative Reforms Commission (appointed in 1967) recommended that powers should be delegated to the maximum extent to the States.
- It also expressed the opinion that centralized planning had tended towards excessive interference in the freedom of States to work out their policies and programmes.
- The Commission made some recommendations with regard to the office of Governor and also suggested the need to establish an Inter-State Council under Article 263 of the Constitution. The recommendations of the Commission however remained on paper and process of centralization continued.

(ix) Sarkaria Commission

- The decades of the eighties witnessed a struggle to get the federal issue on the nation's agenda. And when the political challenge assumed new dimensions and tensions between the Centre and the States grew in sharpness, it became necessary to ease the situation.
- It was in this context that the Government of India announced on March 24, 1983 the appointment of a Commission to examine and review the working of existing arrangements between the Union and the States in regard to powers, functions and responsibilities in all spheres and recommend appropriate changes and measures.
- The Commission came to be known as the Sarkaria Commission on Centre-State Relations after the name of its Chairman R.S. Sarkaria. The Commission was asked to keep in view the social and economic developments that have taken place over the years as also the scheme and the framework of the Constitution and the need for preserving the unity and integrity of the country.
- The Sarkaria Commission submitted its report on October 27, 1987. The Commission favoured a strong Centre as the only safe-guard to national integrity which was being threatened severely in the light of recent fissiparous tendencies in the body politics. But, the Commission did not equate strong Centre with centralisation of powers. In fact, it viewed centralisation as dangerous for national integration.

(x) Salient Recommendations of Sarkaria Commission are:

- More extensive and generous use of Article 258 which gives powers to Union government to confer powers, etc. to State governments should be made than as hitherto being done.
- Any move to disband the All India Service or to permit the State government to opt out the scheme must be regarded as retrograde and harmful to the larger interest of the country. The All India Services should be further strengthened and greater emphasis given on the role expected to be played by them.
- Amend Article 248 to provide the legislature of the state with exclusive power to make any law with respect to any matter listed in the Union List or Concurrent List. That is, the residuary power on the federation should lie with the states.
- Delete Article 249 that gives power to Parliament to legislate on the State List, by the concurrence of the Rajya Sabha on a matter deemed by it to be of national interest. This short circuits the amending process laid down in Article 368, and unilaterally transfers a subject from the State List to the Concurrent List. A better and more equitable alternative is any how available in Article 252(1) even if it be cumbersome and time consuming.
- Amend Article 280 (regarding the Finance Commission), and provide for the transfer of seventy five percent of the total revenue raised by the Centre from all sources, to the States.
- Delete Article 302 (regarding the power of Parliament to impose restrictions on trade and commerce with a State or between the States)
- Delete Articles 356 and 357 (Emergency provisions, giving right to the Centre to dissolve a State Assembly and impose Presidential rule).
- Delete Article 360 (Financial provision) that empowers the President to interfere in State administration, on ground of threat of financial instability.
- Delete Article 200 and 201 which empower the Governor to withhold assent to bills, and reserve them for Presidential approval.
- Amend Article 368, to ensure that no amendment of the constitution is possible without two thirds majority of the members of Parliament, present and voting.
- Amend Article 3, to ensure that the name and area of a State cannot be changed by Parliament without the consent of the state legislative concerned.
- When ever the Union proposes to undertake legislation with respect to a matter in the Concurrent List, there should be prior consultation not only with the State government, individually, but also collectively. There should be regular consultations on the management of All India Services between the Union and the State governments.

- The Planning Commission and the National Development Council are to be reformed assuring at the same time of full and effective consultation with the States at all stages of the planning process so that they feel that their role in it is not that of a supplicant, but of an equal participant.
- Before the Union government deploys its armed and other forces in a state in aid of the civil power otherwise than on request from the State government or declare an area within a State as disturbed, it is desirable that the State government should be consulted, wherever feasible, and its cooperation sought, even though prior consultation with the State government is not obligatory.
- Convention as to consultation with State governments in Concurrent List individually as well as collectively should be strictly adhered to except in extreme emergency.
- Article 356 (emergency provisions) should be used very sparingly in extreme cases as a measure of last resort when all available alternatives fail.
- An expert committee should be constituted to enquire into and revive from time to time in consultation with the States, the operational feasibility of the scope for levying taxes and duties under Article 269 and the complementary measures, the State governments would be required to (Taxes levied under this article are collected by the Union Government and assigned to the States).
- In order to ensure effective consultation with the State Chief Minister, in the selection of a person to be appointed as Governor, the procedure of consultation should be prescribed in the Constitution itself by suitably amending it.
- Residuary powers of legislation in regard to taxation matters should continue to remain exclusively in the competence of parliament while the residuary subjects other than that of taxation should be placed in the Concurrent List.
- Safeguards should be incorporated in Article 356 to enable Parliament to revive continuance in force of a proclamation.
- The Constitution should be suitably amended to add the subject of taxation of 'advertisement broadcast by radio or television to the present Entry 92, List (Union list) and Article 269 (1) relating to duties and taxes levied and collected by the Union assigned to States.
- Inter State River Water Disputes Act may be amended to make it mandatory on the Union government to constitute a tribunal within one year of receipt of an application from a State and should be amended to empower the Union government to appoint a tribunal when it is satisfied that a case exists, to require States to furnish necessary data to the tribunal, to make the award of the tribunal effective within 5 years

to give the award of the tribunal the same sanction and force as that of a decree of a Supreme Court.

- On top of this elaborate scheme of establishing cooperative Union State relations, was the recommendation relating to the setting up of a permanent Inter State Council under Article 263 of the Constitution to discuss many of the problems of common Union-State interest.
- Consisting of a General Body with Prime Minister as Chairman and all Union Cabinet Ministers and all Chief Ministers as members, and Standing Committee with the Prime Minister as chairman, Six Union Cabinet Ministers and Six chief Ministers one from each zone as members, such a Council is expected to provide a forum for discussion in an era among senior statesmen. The arrangement is expected to promote proper understanding and mutual confidence among the Chief Executive of the Union and the States.
- In the light the recommendations of the Sarkaria Commission, the Ministry of Home Affairs issued an order dated 28th May, 1990 by which an Inter-State Council was established under article 263 of the Constitution. A copy of the relevant notification is appended at the end of the chapter.
- The Inter-State Council consists of the Prime Ministers, Chief, Ministers of all States and Union territories with or without a Legislative Assembly and six Ministers of Cabinet rank in the Union Council of Ministers to be nominated by the Prime Ministers or Ministers of State having independent charge in the Union Government when any item under their charge comes up for discussion. The Prime Minister is the Chairman of the Council.