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GRANTS-IN-AID DEVOLUTION IN INDIAN DEMOCRATIC FEDERATION: NEED OF SOME SUGGESTED REGULATORY REFORMS

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Abstract- The real challenge of any federation is to eliminate intra-regional vertical and horizontal fiscal inequalities. During the last decade disparity between Centre and the States and among the States increased, and became economically and politically important. This situation resulted due to globalization and privatization. Here in this context the role of government and other financial institutions increased and has to work according to changing phase. The Fiscal and Monetary Policies need to be modified and some major reforms are must to accelerate the path of economic development. In India the major normative concern of policy structuring is equality and efficiency. The aim of this paper is to focus on role of grants-in-aid (GIA) devolution from Finance Commission (FC) to States and to study the rationale, trend and prospects for balancing the fiscal imbalance through this mode. Secondary data has been used in this study. . In few FCS GIA transfers favor developed states which are issues of great concern. No single policy can be very effective for a very long period in vibrant large and variegated country like India. The paper recommends for increasing the share of GIA to all backward States to reduce vertical and horizontal fiscal imbalances for overall economic development and optimizing social welfare of the entire economy .The parameters to judge the needs of the states should be made mainly on population below poverty line (BPL) and the stage of development of the concerned state. The remedial measures are suggested for policy reforms
KeyWords: Finance Commission, Vertical Imbalance, Horizontal Imbalance, Grants-in- Aid, Fiscal imbalance, Indian Federation, Regulatory Reforms

INTRODUCTION

The key problem of Indian democratic federation is to reconcile with the desire to obtain the advantage of decentralization in terms of delivery of efficient program and responsiveness to users' need. The main objective behind this is to meet the national targets and important programs for redistribution. The role of Central Government in equalizing the ability of States to provide comparable level of public services is no different in principle than its general equalization role. The transfer of resources through different sources in different modes of resource transfer (taxes, loans and grants-in-aid) has different effects on the economy. Different States have different revenue raising abilities, thus they need different policies for development and poverty alleviation related expenditures. In order to provide comparable services at comparable state tax rates and fiscal equity and efficiency the existing fiscal imbalances should be balanced. This whole process for reconciliation involves two steps: (i) A reasonable assignment of functions between different levels of government, (ii) Establishment of a system of inter-governmental relations that facilitate the goals of national objectives. This is clear that assignment of functions and interovernmental transfers are the basic issues of a federation.

In Indian context there is need to address the institutional space provided by federal democratic structures to the operations of FC .Centre-State financial relations consist of a set of financial transfers from the Central Government to States and provisions are made for coordinating and sharing of tax revenues and allocating grants.

Federal government collects more tax revenues than its need for its own purpose, and then it transfers to State Governments either as grants or by sharing of tax revenues according to provisions made in the constitution. In a decentralized decent democratic federation, federal state transfer is necessary to fulfill its national efficiency and equity objectives for smooth fiscal relations. In order to balance the vertical and horizontal fiscal imbalances inter-governmental transfers are used as an instrument of fiscal adjustment by almost all federations. Besides, fiscal instruments, grants are used by spillover benefits and to achieve equalization of revenues and other basic services which is the essential requirement for a welfare state. Different FC work on different TOR and different priorities are made by successive Finance Commissions. In successive FC transfers, it is observed that redistributive factors are assigning greater weight to state transfers. The Twelfth FC has slightly changed this trend and increased the weight attached to income neutral factors and decreased the weight to redistributive factors. The Thirteenth FC has increased the weight of index of fiscal discipline and reduced an important indicator of fiscal discipline, i.e. the tax GSDP (Gross State Domestic Product) ratio. The weight of the share of GIA to GDT and GDP has been steadily increasing over the FCs but it reduced slightly during Thirteenth FC. The GIA transfers are not rational and scientific because the high income states got more share till Eleventh FC but the Twelfth FC has changed the trend slightly. The GIA transfers are crucial for improving the revenues of the States along with incentivizing them for better fiscal performance. Thirteenth FC has increased the heads of special needs and added a list of “special needs” to GIA transfers.

LITERATURE REVIEW

Different federations prefer different methods of resource transfers to solve the problem of fiscal imbalance as this is common to all federation and the objective behind is to provide maximum social advantage to all irrespective of place of residence. “Fiscal reforms at the State level are, thus, important from the view point of macro-economic stability and micro-economic allocation efficiency” Rao M G [1]The system of inter-governmental fiscal transfers, as it has evolved in India over the years, has come under attack on the ground that it has created perverse incentives by putting a premium on equity and neglect of efficiency led to a fiscal profligacy at lower levels of government, although sharp regional disparities persist and have grown sharper particularly in recent years Bagchi A [2], Chelliah RJ and associates [3] argues that the existence of increasing decentralization of expenditure and increasing centralization of revenues in India has led to the widening up of the fiscal imbalance. In Germany, social welfare expenditures are shared responsibility where the Central Government sets the broad outlines of policy (criteria and level of spending), while the local government makes the determination of social neediness and disburse grants Warner[4]. In United States, public welfare services involve all three levels of government Schroeder[5]. In Canada welfare is the social responsibility. Knopff and Sayer[6]. The leading federations of the world USA, Canada, Australia and Switzerland show the well functioning and suitable formula for the resource allocation, which is the prime determinant of promoting stability and prosperity. In most developing and transition economies there is a sense that regional inequalities of incomes and social indicators are on rise. Kanbur ,R and A J Venables,[7]

The imbalance between functional responsibilities and financial resources of different layers of Government is feature of all federations, particularly for dynamic decent federations. The mismatch in India, relating to revenue and expenditures are sought to be removed through vertical and horizontal devolutions from the Centre to the States through different mechanisms of Finance Commission, Planning Commission and Union Ministries. Finance Commission makes recommendations regarding devolution of taxes and duties collected by Centre under the provisions made in Article 246(1) list of seventh schedule and grants-in-aid under Article 275 of Indian Constitution ,Constitution of India[8].Buchanan [9] advanced horizontal equity grounds for equalization purposes of GIA transfers. Later Boadway , Robin and Flatters, Frankin[10] reformulated the concept of horizontal equity in a way that poor states are supported by central government for macroeconomic stability.

Several economists in India have studied and concluded that regional disparity as the main constraint for economic development .Chandrasekhar S [11] says that in India both vertical and horizontal fiscal imbalances exist. These imbalances are caused by the very structure of federation itself. The Administrative Reforms Commission [12] observed, “exact correspondence of resources and functions is not possible to secure in any federal situation but in India the balance is tilted rather heavily in favor of the Centre and the outstanding feature of the financial relationship between the Centre and the States, consequently the former is always the giver and the latter the receivers.” For backward states Lakadwala, D.T.[1967][13] argues that backward States may have abundant but untapped natural resources. These states remain poor because of the ‘absence of the initial spark’. Once this missing link is provided they will grow fast. Hicks UK, [14] opined that “As countries become more awake to the possibilities of development and especially of development from below, the extent of grants is likely to expand, so that a coherent grant policy becomes increasingly important.”

Pigou[15] has suggested that in case of external benefits the economic unit that generates spillover benefits should receive a unit subsidy or grant equal to the value of marginal benefits created. Coase, Ronald [16] criticized Pigou and argues that the potential inefficiencies of provision of public good can be resolved by mutual agreement and joint action but Oates WE [17] favors Pigou and by saying grants hold good even if there exists reciprocal externalities .

OBJECTIVE OF THE STUDY

The objective of this paper is to evaluate the role of Grants-in –aid as an effective tool for removing fiscal imbalances.

HYPOTHESIS

Grants-in –aid transfers through FC are made according to the economic structure of states i.e. Poor states receive more grants-in- aid as compared to richer states**.**

DATA COLLECTION and METHODOLOGY

The study is based on secondary data of reports of various FC and simple statistical analysis is done to obtain the results.

TRANSFER OF RESOURCES

For a developing economy the primary purpose of fiscal policy should be demarcation and realization of developmental goals and this depends on the economic political and social structure of the country .For economic development of developing country like ours the main developmental goals are accelerating the rate of economic growth through capital formation.

Maintaining economic stability, raising employment opportunities and reducing income and wealth inequalities within the country is the prime role of government. Thus all these reasons recommend resource transfer in federal structure. The revenue transfers are made through taxes and grants on the basis of different criteria such as fiscal capacity, fiscal need and other specific condition including transfers depending on the situation. This paper focuses on transfers through Grants-in-aid (GIA). Different types of transfers have different effects on the economy. In Indian context, the economy is growing with rising inter-personal and inter-state inequalities. This raises the questions for policy makers to respond. As the Indian economy is facing its developmental and transitional challenges reforms related policies become more important.

Transfers consist of tax sharing, grants and loans. Tax sharing and grants are used to correct vertical and horizontal fiscal imbalances and to give overall equalizing effect. Revenue transfer is needed because the own revenues of a lower level of government are generally insufficient to meet the expenditure required for providing services allotted to it. Central Government retains elastic sources of revenue such as income tax, excise levies and custom duties with it. The inelastic sources of revenue such as sales tax, excise or liquor and motor vehicle tax are allotted to State Governments. The gap between own revenues and expenditure needs to show the degree of dependence of State Government on the Central Government. Thus, inter-governmental theory is justified due to the correction of fiscal gap between the expenditure need and revenue means of a state. The fiscal capacity and fiscal need of the State differs because the fiscal capacity depends on natural, geographical and climatic conditions of a particular State while fiscal need depends on the developmental and Welfare policies of the government. The access of revenue base varies from region to region. Per unit cost of services varies depending on the nature (climatic and geographical) and the density of population. Fiscal gap also occurs due to inappropriate assignment of revenue resources and functional responsibilities. For this reason fiscal gap correction becomes necessary and just.

The other justification of resource transfer is for providing minimum standard of services across the regions. Transfer from Centre to States may be needed to upgrade the existing level of services to ensure a common minimum standard across the federation. The Central Government can provide grants to State to ensure a national standard for providing some basic public services. The transfers may be made for inter-jurisdictional spillover. Spillover occurs where the benefits of local public services spread to persons who are not legally required to contribute to 'costs of a service.' Inter-governmental grants are used as a major weapon for correcting spillover effects. Further, grants are the best way to correct the spillover effects and provide minimum standard of services across the region irrespective of what they are paying in form of tax. In order to implement certain schemes of national importance (disease control, preserving ecological balance, etc.) funds are provided to State Governments to perform such functions. But it does not provide a clear-cut policy for power and functions of State Government and Central Government. It creates a dual polity based division of powers and functions.

The favorable position given to the Centre in regard to financial resources reflects the strength of the focal theme running through the Constitution and many feel that this has been an important factor in keeping the country united. The Planning Commission makes recommendations for grants for the States under Article 282, which provides for government assistance for any public purpose. The Union Ministries also use Article 282 for assistance to States for various schemes known as the centrally sponsored schemes. To avoid overlapping of recommendations, the FC was restricted to non-plan revenue needs of the States. Presently, first a particular portion of revenue resources (net proceeds) levied and collected by the Union under a particular Article is earmarked for passing on to the States and then this portion is apportioned to different States according to different criteria or formula through assignment of weights.

The Indian Constitution recognizes the fact that the financial resources of the States will be inadequate for welfare, maintenance and developmental activities. To correct the disequilibrium between the functional responsibilities of the States and their resources provisions are made for mobilization of resources from the Centre to States in the Constitution itself. In India the Central transfers are channeled through:

(i) Finance Commission – Statutory transfers

(ii) Planning Commission – Plan transfers

(iii) Central Government Schemes – Discretionary transfer for centrally sponsored schemes, relief for natural calamities and rehabilitation of displaced persons.

These are the direct transfers from the Central Government to State Governments. Resources also flow to the States indirectly through different channels [18].

MOBILISATION OF RESOURCES

FC transfers resources through sharing of certain Central taxes and grants-in-aid. Though the powers allocated to the Centre and the States through taxation are mutually exclusive. But some taxes and duties levied by the Centre are not meant entirely for the Centre. In practice, some taxes and duties levied by the Centre is not used by the Centre. They are totally assigned to or shared with the State to supplement their revenue according to their needs. Even with a share in the proceeds of divisible taxes, some States still need financial assistance and provision is made in the Constitution itself. The architects of the Constitution have made provision for annual grants-in-aid of revenues under Article 275(1) to needy States according to their need and availability of resources. The Centre is also required to give grants-in-aid to the States for the welfare of Scheduled Tribes and to raise the level of administration especially for Assam. This feature of Indian Constitution shows the flexibility regarding distribution of financial resources between the Centre and States. Constitution provides provisions for Central transfers. It does not indicate the share of the States in the divisible taxes and it also does not prescribe any principle for the distribution of States' share among the States themselves. It seems that the architects of the Constitution knowingly avoided permanent formulae in this connection with a view of expected changes in the sphere of taxation and public expenditure. Thus, the taxes and the actual determination of grants are left on the FC appointed under Article 280 by the President and the President is guided by the advice of the Central Council of Ministries (Article 74). Sometimes it is observed that Centre itself becomes a party to the dispute between the Centre and the States regarding transfer of resources and the FC has to act like mediator or arbiter.

The FC consists of a Chairman and four other Members recommending the principle of distribution between the Centre and the States and the proceeds of the taxes, their allocation among the States. The FC recommends on the basis of detailed assessment of the financial position of the Central and State Governments. For this assessment the experts of public finance are concerned and studies are commissioned on specific topics. The Commissions visit the State capitals and hold discussions with officials and leaders. After this process the FC makes recommendations together with the Explanatory Memorandum on the action taken on them. Then it is laid on the table of the House by the Government under the Article 281 of the Constitution. The President is not bound to accept the recommendations of the FC but due to quasi-judicial nature of the FC it is generally accepted. The FCs is provided with Terms of References by the Finance Ministry for allocation of resources. The FC transfers are made differently for two categories, General Category States and Special Category States. These transfers are made on different norms. But till now once during 1984-85 the recommendations of the Eighth FC, the Centre did not accept the entire set of recommendations. Till now 13 FC have been formed and they have worked independently. Some of them have been quite assertive. The FC of India has a unique feature of the Indian Constitution, having no parallel in any federation.

The FC has the responsibility to recommend a scheme of transfer of resources in order to ensure financial equilibrium between states during that period and to design formulae to allocate transfer of resources between them. But practically FC cannot solve this problem alone. The actual working of the revenue sharing mechanism of FC is sharing of tax revenue and disbursal of grants-in-aid. The criteria of fiscal capacity and fiscal discipline used by Thirteenth FC, which are given a weight of about two-thirds in the formula, are inadequate, inconsistent and subjective. The allocation outcome based on such a formula along with the discretionary nature of grants neither reflects equalization nor efficiency and hence provides confusing signals to states for their future fiscal behavior and growth orientation is the view of Archana R. Dholakia[19].

To judge the total transfers through FC the percentage share of Grants-in-aid transfers and percentage share of taxes and duties transfers in total. The share of grants-in-aid transfers has remarkably increased after Eleventh FC. The Twelfth FC also showed an increase while during Thirteenth FC it was almost same or minor decrease [Table 1].

The bar diagram shows the increasing trend of Grants-in-aid transfers during successive FC and the share of Grants-in-aid and taxes in total transfers through FC (fig. 1).

But Table 1 clearly focus that the transfers through grants –in-aid is not uniform rather it changes with the policies and priorities of the existing government. The FC are not free to decide the resource transfers .FC are provided with terms of references by the centre government to work accordingly transfers by calculating the variance of FC transfers this is very clear.

The Variance in grants in-aid transfers during Seventh FC till the Thirteenth FC is 86.65 in nominal terms having a high value. This shows that the grants–in-aid transfers are not uniform during successive FCs. The disparity ratio of the Seventh to Thirteenth FC is 160.61

Variance (seventh FC - thirteenth FC) =86.65

Disparity Ratio =160.61

The most unfortunate development in the part of fiscal federalism during neo-liberal reforms period has been in the working of FC as constitutionally mandated body and centre using its discretionary powers. Centre also controls fiscal situation and public finance of Indian economy. Bagchi [20] said that, "the direct entry of the neo-liberal project into the arena of public finance, and in particular centre state financial relations, can be dated from the Ninth Finance Commission which reported on financial allocations from 1989-90to 1994-95.Until Ninth FC it regularly wrote off the debt of the central government to the state government ,so that the latter could start their financial programs in a relatively unburdened fashion ".The most remarkable fact shows that the centre is trying to impose the neo liberal policy on the states making FC as a medium of implementation. This was evident with the report of Eleventh FC "By knowing the wishes of the centre 15percent of the revenue deficit grants for fifteen states was given by Eleventh FC for the period of 2000-05which was conditional on the states**.** Patnaik[21] remarks that this step of eleventh FC was strongly criticized as an act that abridged the constitutional rights of the states and privileged the centre over the state governments (contrary to its own constitutional obligations)through which Eleventh FC exceeded its own jurisdiction ,along with putting forward a mechanism of double counting the state's failure on certain fiscal parameters ,which is not logical at all.

The grants-in-aid transfers in recent FC have improved .Till Ninth FC the trend of grants-in-aid transfers was almost same and there was no remarkable change. But after Ninth FC the grants-in-aid transfers changed which itself is clear from the growth rate .After tenth FC the growth rate of grants-in aid increased and they also focused on specific sectors of development. Among grants-in-aid transfers health and education are the two critical merit services .Table 2 shows the growth rate of grants-in-aid transfers in nominal terms.

Per capita grants to States are showing irregular pattern [Table 3] in high income states. Gujarat a high income state received a huge transfer during Tenth and Twelfth FC but it got a nominal share in the Eleventh FC .Maharashtra received the highest share during Tenth FC .Punjab was the highest recipient of per capita grants during Eleventh and Twelfth FC .Haryana a high income state also received a good share during Tenth Eleventh and Twelfth FC .During Thirteenth FC grants-in- aid transfers to Gujarat reduced while the share of Haryana and Maharashtra increased (Fig. 2,3).

The bar diagram also shows the irregular transfers in per capita grants in high income states during different Finance Commissions (Fig.4).

In case of low income states [Table 4] there was low per capita grants during Tenth FC .All the five low income states were losers during TC but during Eleventh FC only Rajasthan and Uttar Pradesh were the losers. During Twelfth FC all the low income states' share increased and Bihar received the largest share.

Figures of Madhya Pradesh, Uttar Pradesh and Bihar refer to undivided States. Grants-in-aid exclude grants to the local bodies as it is introduced after Tenth Finance Commission.[For uniformity of analysis.] (Fig.5).

Percentage increase in per capita grants indicates that all the High income states were gainers while the low income states were losers during Tenth FC while, Maharashtra got the largest share and Rajasthan got the least .During Eleventh FC the share of all high income states decreased and Gujarat got the least and in low income states, Rajasthan's share further decreased a lot while UP has a marginal loss of 7.42%. All other states gained during Twelfth FC and Punjab got the maximum share while the share of all high income states increased .In case of low income states the share of Bihar was maximum and all the states got a good share .The total amount transferred to all the states is almost same as Twelfth FC .A salient feature of Thirteenth FC is that it has increased specific needs transfers "Giving grants to the states for their "special needs" for example ,gives an appearance of being arbitrary and judgmental." Rao MG[1, 27]This an example of irrational Grants-in -Aid transfers through FC. Again Rao and Rakshit Mihir [22] criticized the "gap filling" approach adopted by FC and comments that GIA has "the expectation that the gaps will be covered and larger the gaps, more is the state likely to get."

Rao and Jena [23] [Table 4] have shown negative relationship between per capita transfers and per capita GSDP by measuring income elasticity of transfers. With the increase in per capita income there is a decline in per capita transfers is shown by negative sign of elasticity. The Twelfth FC transfers have deteriorated in comparison to Eleventh FC and the main cause behind was assignment of higher weight to 'population' factor at the cost of per capita GSDP. This analysis depicts that tax shares are more elastic than grants, and the same trend was followed by Thirteenth FC with a slight change in the devolution pattern. With a decline in per capita income the share of tax and grants decreases but as compared to Twelfth FC the share of grants declined slightly more than tax shares.

The share of grants-in-Aid transfers (Table 5) has increased during successive Finance Commissions .Grants-in-Aid transfers as percentage of GDT declined during Tenth Finance Commission but it increased during eleventh Finance Commission .Grants-in –aid as percentage of GDP of transfers has decreased during Eleventh and Twelfth FC was low as compared to Ninth and Twelfth FC. It has an increasing trend over the FC period and the loan component in Central transfers became less significant after Twelfth FC due to FRBM .During Thirteenth FC the grants-in –aid transfers reduced slightly in comparison to Twelfth FC and this resulted in slight reduction in the share in Gross devolution of transfers and Gross Domestic Product .Thus grants-in-aid transfers increased after Eleventh FC and there was a remarkable change after Ninth FC.

GDP: Gross Domestic Product
GDT: Gross Devolution of transfers
GIA: Grants-in-Aid

The share of grants-in-Aid transfers has increased during successive FC .Grants-in-Aid transfers as percentage of GDT declined during Tenth FC but it increased during Eleventh FC KurinNJ[24].Grants-in –Aid as percentage of GDP of transfers has decreased during Eleventh and Twelfth FC was low as compared to Ninth and Twelfth FC. It has an increasing trend over the FC period and the loan component in Central transfers became less significant after Twelfth FC. Report Of Twelfth Finance Commission[29].

REGULATORY REFORMS

Grants-in-aid devolution in India needs some major regulatory reforms. The design of fiscal transfers should be changed to ensure the efficiency and equity of local service provision and fiscal health of national governments.

Some simple considerations can be helpful in designing these transfers:

The objectives of Grants-in-aid should be clearly and precisely specified. When the objective of Grants-in-aid is clear the grant, received by the concerned State also becomes responsible and remain answerable to all defaults. It should not be designed with vaguely defined objectives. The State Governments should have complete independence and flexibility in setting priorities according to their need and prevailing circumstances. The categorical structure of programs and uncertainty associated with decision making at the Centre should not constrain the sub-national Governments. To Isaac Thomas and Pinaki Chakra borty[25]the States should get autonomy for fixing their priorities but it should not be used to finance State Governments deficit which leads to the tendency to create higher deficits in future . States should do effort to raise their revenue.

The Grants-in-aid should not be very rigid and fixed rather, should have flexibility to accommodate unforeseen changes in the fiscal situation of the grant receiving State. There should be provision in the structure of Grants-in-aid to meet the natural, social and political calamities. Through Grants-in-aid transfers State Governments should get adequate resources to discharge functions, objectives and responsibilities, no work should be stopped due to shortage of resources. In ability of the commissions to offset relative fiscal disabilities of the state makes necessary the commission to recommend large number of specific purpose grants Rao MG [26]. Adequate resources should be transferred through Grants-in-aid to achieve the objectives and the objectives should not be changed until it is fulfilled. The structure of Grants-in-aid mechanism should ensure predictability of State Government's share by projecting the availability of funds for five years and should be made public.

The Grants-in-aid should fairly be distributed among the States. It should vary directly with fiscal needs of the State and inversely with the tax capacity of each State. The distribution of resources among the States should be on the basis of equity. The Grants-in-aid transfers should avoid negotiations and political hindrances .Finally political influence on the transfer system has been increasing due to prevalence of coalition governments ruling at the centre typically the regional parties playing the pivotal role Rao and Nirvikar Singh [27]. The FCs provide a built in incentive to launch new programs which involve substantial expenditure on current account without the consequence for future Vithal and Shastry[28] Discretionary grants may create disunity and dissention in a federal system. There should be no partiality in resource distribution among the states. There are some unnecessary constraints in designing an efficient and suitable resource transfer methodology in Indian situation .Srivastava DK[30]. The fiscal capacity and fiscal distance components can potentially contradict each other which is true for all weighted formula Chakraborty [31]The resource distribution formula needs to be formulated according to the after affects of indicators used in order to minimize contradictions.

GIA transfers should not be multi-channeled. All the three granting authorities should be merged and channeled; the total transfers through grants should be single. A state should be given its total entitlement of grants and allowed to select its own mix of centrally sponsored schemes floated by different ministries, within the limit of total grant Narayan valluri[32] The award parameters should be updated. For example total population is taken for fiscal transfers but if population below poverty line is used in resource transfer formula, certainly it will give better result.

There should be more research programs based on intergovernmental fiscal federalism and the experiences of other federations should be shared .This will provide input to policy makers for future predictions and implications to coming FC .The time lag information of using 1971 population data and dated per capita GSDP data should not be used for resource transfers .Both the data should be updated and of the same time period. There is mismatch of Data published by different organizations. The data on share in Central taxes and Grants-in-aid of Union and State budgets do not match. The district level data should be made available on social and economic indicators that would help in better understanding and specification of disparities among the states

CONCLUSION

The imbalance between functional responsibilities and financial resources of different layers of Government is feature of all federations, particularly for Indian situation Grants-in-aid can be an efficient tool to balance the dynamic decent federations The Grants-in- Aid transfer should be based o n objective and need of the State not on the TOR given to FC and needs more freedom. The Grants-in-Aid should be simple and mostly focused on single objective. Multiple objectives have risk of failure in achieving any of them and thus reflect no perfections. It is desirable to have the grants distribution to be reviewed periodically. National minimum standard of basic services across the nation should be established in order to strengthen the economy and provide maximum social advantage to all irrespective of place of residence. Per capita fiscal capacity should be equalized in order to achieve fiscal equalization across the country. Government regulatory policies should be reformed and efforts should be made to transfer maximum amount through Grants-in-Aid with clear objectives. Percentage share of Grants-in Aid devolution to GDP and GDT has increased but the percentage share to GSDP during the same period did not show the desired result. States get FC grants as a matter of right it should be the matter of effort. The step taken by Thirteenth FC by giving performance grants to Assam, Sikkim and Uttarakhand is an example to all States. Population the most neutral variable represents the expenditure needs of the States but if populations below poverty line, SC, ST population are used as indicator of expenditure needs a very effective and progressive .The time period base of Finance Commission and Planning Commission should be the same .The role of Grants-in-aid transfers, needs to be reformed in order to balance the vertical and horizontal imbalances existing deeply in Indian federation by the coming FC.

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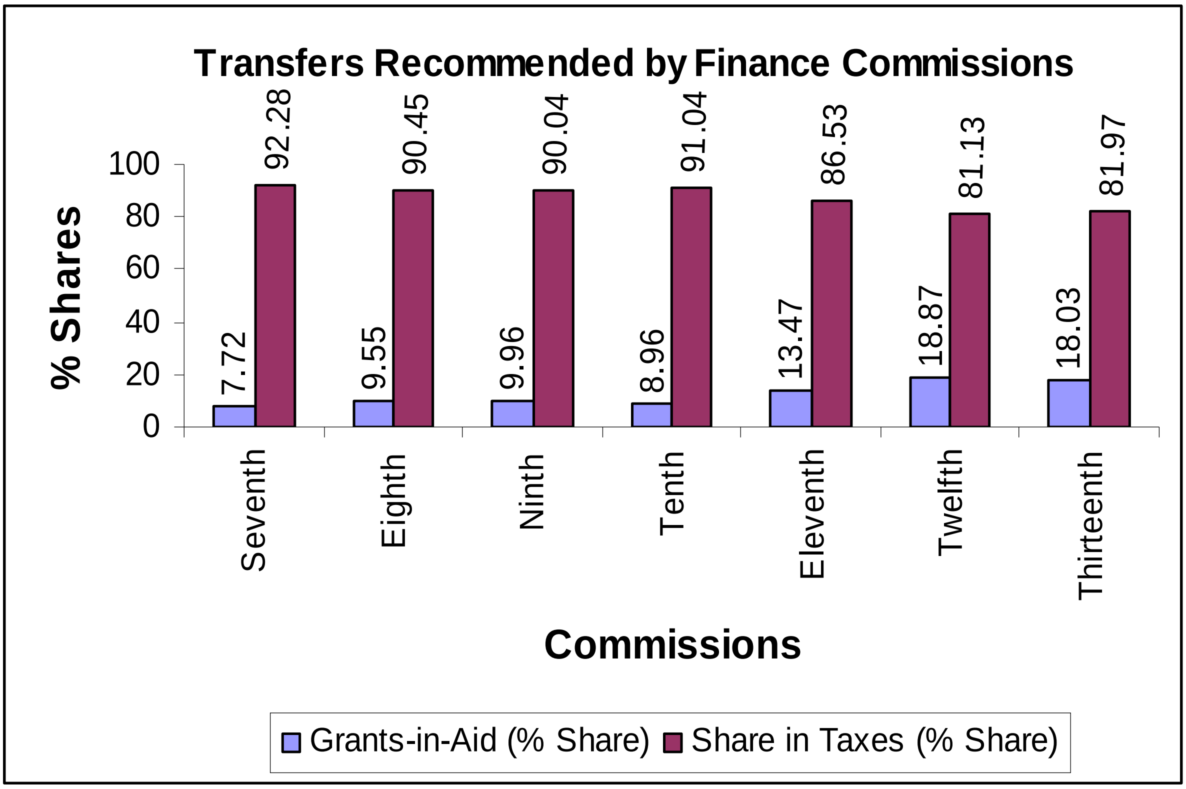

Fig. 1- figure of finance commission transfers and grants-in-aid

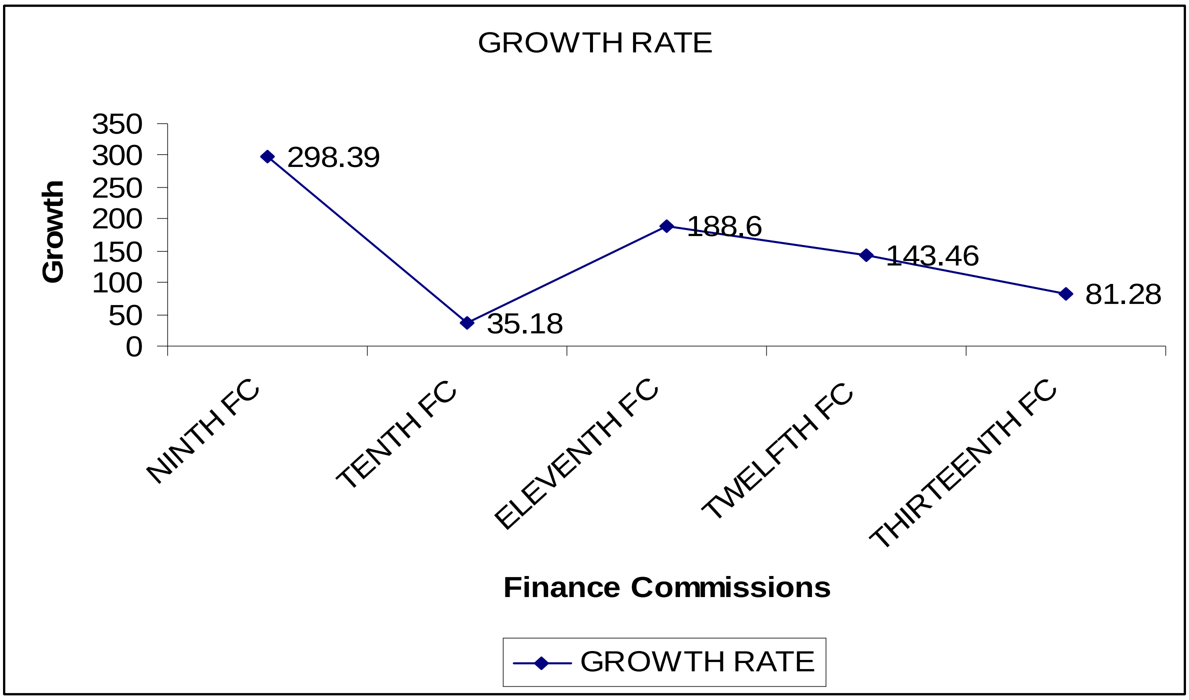

Fig. 2- grants-in-aid and its growth rate

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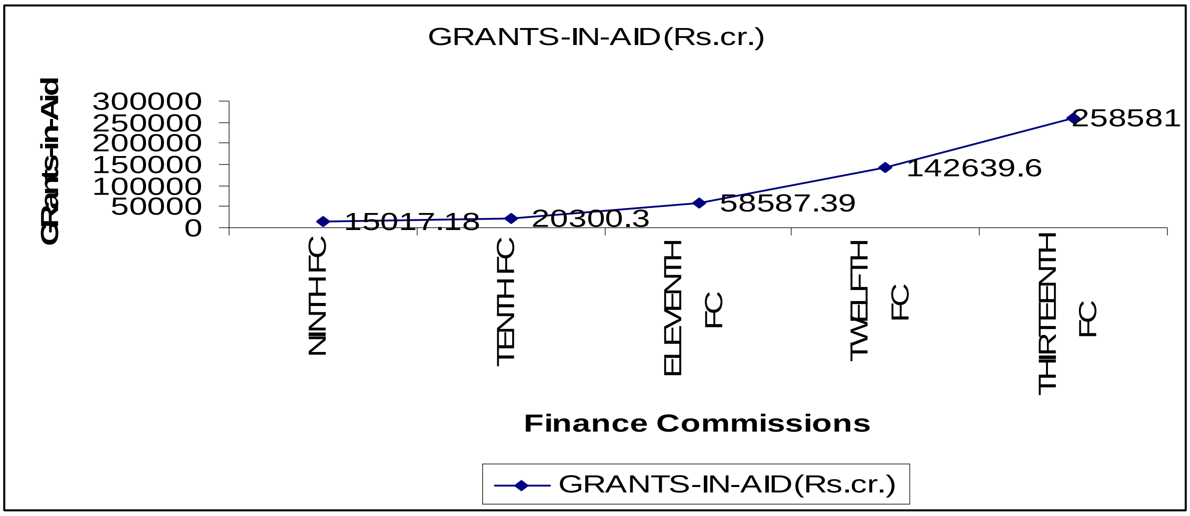

Fig. 3- grants-in-aid during successive finance commissions

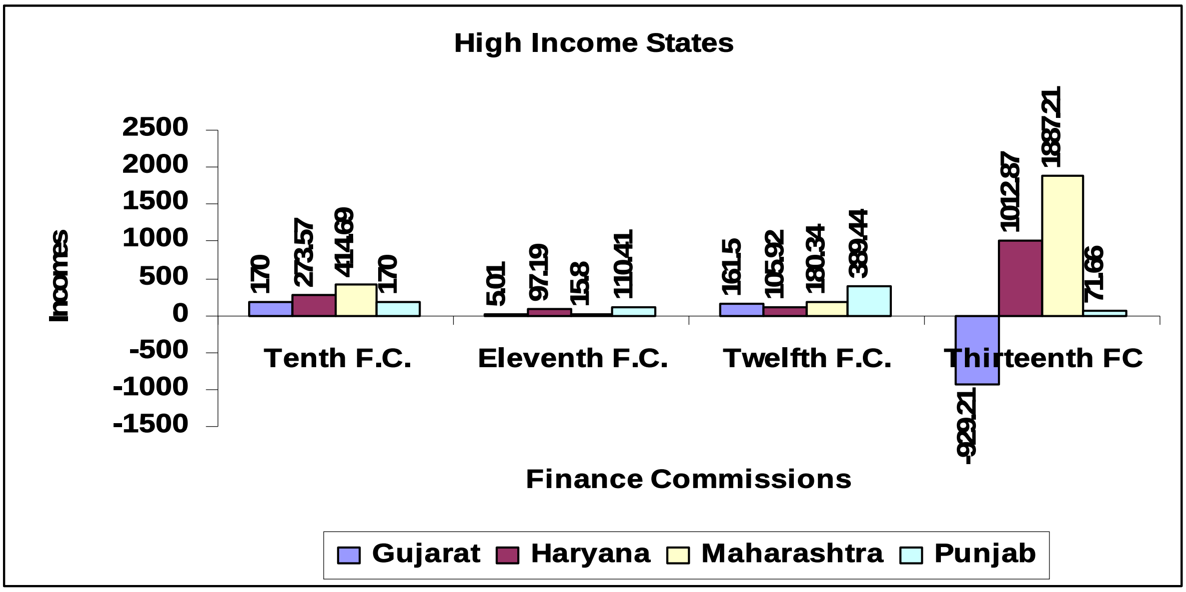

Fig. 4- finance commissions and high income states

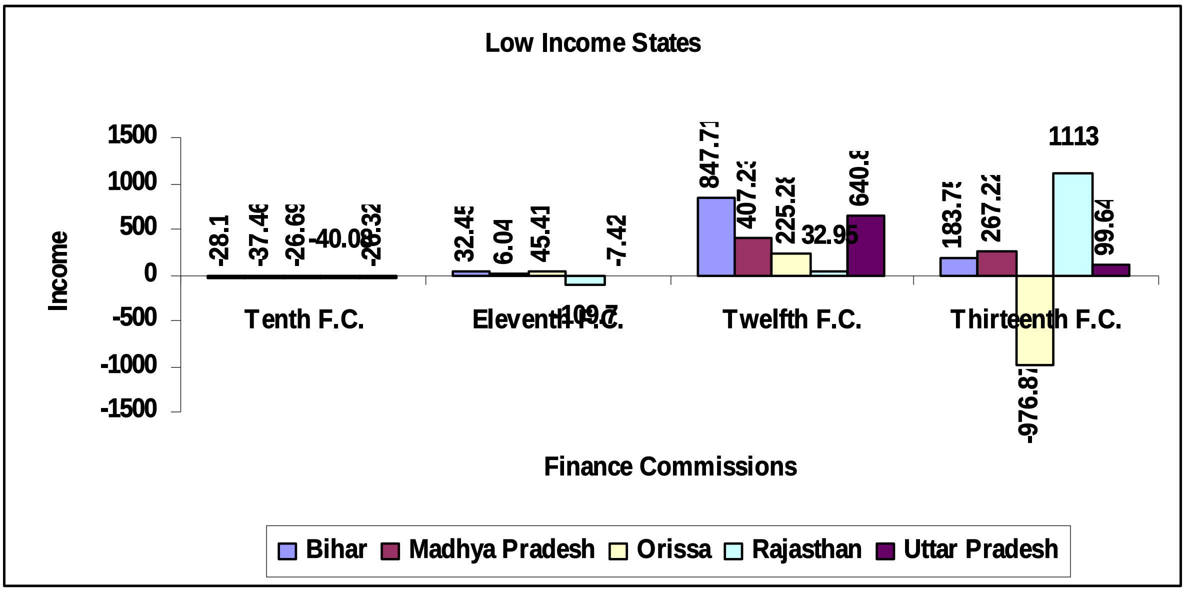

Fig. 6- finance commissions and low income states

Table 1: Transfers Recommended by Finance Commissions

Commissions	Period	Grants-in-Aid (% Share)	Share in Taxes (% Share)	Total (%)
Seventh	1979-84	7.72	92.28	100.00
Eighth	1984-89	9.55	90.45	100.00
Ninth*	1989-95	9.96	90.04	100.00
Tenth	1995-2000	8.96	91.04	100.00
Eleventh	2000-05	13.47	86.53	100.00
Twelfth	2005-10	18.87	81.13	100.00
Thirteenth	2010-15	18.03	81.97	100.00

*Ninth Finance Commission covered six year and provided.

Source: Report of Twelfth Finance Commission

Table 2- Growth Rate of grants-in –aid

FINANCE COMMISSIONS	GRANTS-IN-AID(Rs.cr.)	GROWTH RATE
NINTH FC	15017.18	298.39
TENTH FC	20300.30	35.18
ELEVENTH FC	58587.39	188.60
TWELFTH FC	142639.60	143.46
THIRTEENTH FC	258581.0	81.28

Ninth finance commission covered six years (1989-95)

Source: Reports of various Finance Commissions

Table 3- Change in Per Capita Grants during Successive Finance Commissions High Income States

High income states	Tenth F.C.	Eleventh F.C.	Twelfth F.C.	Thirteenth FC
Gujarat	170.00	5.01	161.50	-929.21
Haryana	273.57	97.19	105.92	1012.87
Maharashtra	414.69	15.80	180.34	1887.21
Punjab	170.00	110.41	389.44	71.66

Source : Calculated from Reports of various Finance Commission

Table 4- Change in per capita Grants during successive Finance Commissions Low Income States

Low income States	Tenth F.C.	Eleventh F.C.	Twelfth F.C.	Thirteenth F.C.
Bihar	-28.10	32.45	847.71	183.75
Madhya Pradesh	-37.46	6.04	407.23	267.22
Orissa	-26.69	45.41	225.28	-976.87
Rajasthan	-40.08	-109.70	32.95	1113.00
Uttar Pradesh	-26.32	-7.42	640.80	99.64

Source: Calculated from Reports of Various Finance Commissions.

Table 5- Income Elasticity of Finance Commission Transfer

Projected Transfers	Ninth F.C.	Tenth F.C.	Eleventh F.C.	Twelfth F.C.	Thirteenth F.C.
Grants	-2.09	-1.18	-1.39	-1.54	-1.52
Tax Shares	-1.59	-1.57	-1.86	-1.68	-1.70
Total Transfers	-1.61	-1.53	1.82	-1.64	-1.66

Source- Report of Finance Commission, Rao M. Govinda & Pratap R. Jena (2005).

Table 6- Grants-in-aid Transfers as percentage of GDT and GDP

Item	IX^{th} FC	X^{th} FC	XI^{th} FC	XII^{th} FC	$XIII^{th}$ F.C.
GIA Transfers	17,343	24,267	46,443	99,008	25,8581
GIA as % of GDT	33.4	27.7	35.2	43.8	43.01
GIA as % of GDP	2.3	1.6	1.6	2.4	2.2

Source: Based on Reports of RBI 2007- RBI 2010 (Kurian, NJ- 2008)