

Resources for Autonomy

Ratan Khasnabis

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Resources for Autonomy – Financing the Local Bodies

Ratan Khasnabis

1. Introduction: Decentralization and Development

Decentralized governance is believed to ensure efficiency in the functioning of the state in a civil society. The modern State, which is basically a centralized seat of power, can function efficiently, as the wisdom goes, only by transferring certain responsibilities to the Local Bodies so that the alienation of the state from the citizens is minimized. The regulatory functions of the state are not supposed to be decentralized much to the grassroots level. But, the contemporary political wisdom is that a government should try to devolve the issues of state-sponsored welfare measures to the Local Bodies in as much as such a devolution fosters greater responsiveness of the policy makers to the will of the citizens and thereby a closer congruence between public preferences and state policies might be achieved. The other argument is that such a measure of decentralization creates a proper condition for honouring the diversity in public choices in a better way and thereby decentralized governance helps the choice mechanism function more effectively. Some researchers have observed that decentralization also promotes innovation to the extent it honours local knowledge and wisdom in implementing a programme for development. Above all, decentralization is accepted as a better choice because it is supposed to enhance democratic values which should be the basis of a modern society¹.

Recent literature on decentralization, however, highlights the fact that decentralization has a powerful economic advantage. It has been argued that the allocational efficiency is maximized under a decentralized structure. Difficulty of a centralized delivery system is that it has a tendency to provide uniform services across all regions irrespective of differences (*Smoke, E.J., 1994*). As a result, a centralized system fails to take account of the specific needs and conditions under which the public services are delivered. Consequently, it gives rise to inefficiency in allocation of resources. If the local diversities are to be taken care of, the delivery system has to be decentralized.

The other economic advantage of a decentralized system is that it might ensure production efficiency in a better way. The argument is that (and it is often supported by experiences) a decentralized system ensures the scrutiny of the local people in local projects so much so that the production efficiency of local public goods and services would be better under this dispensation. This is likely to be true

because close popular scrutiny, which is better ensured in a local project, makes local governments less wasteful in production of public goods. Again, there may be diseconomies of scale in a centralized delivery system for the local public goods (such as water supply, solid waste management, public transport). Such projects would operate with economy of scale if the project is designed by a local authority which takes care of the needs of the local people and operates with proper knowledge of local requirements. It is also argued that the positive externality of public goods produced at the local level might be higher because it might promote innovation which might generate greater diversity in local public goods². Researchers have also pointed out that the advantage of informational economies would be realized more efficiently in a decentralized structure³.

Decentralization is not, however, taken as an unmixed blessing in economic literature. Decentralization may cause efficiency loss in as much as the control and coordination often get neglected under a decentralized economy which has an emphasis on autonomy in planning and execution of projects. Control and coordination which function more effectively under a centralized regime, often contribute to enhancement of efficiency of the delivery system. Votaries of decentralization sometimes ignore this point.

It is argued that decentralization captures the economy of scale for certain type of projects in a better way. But then, the logic of the economy of scale might work against decentralization as well. If the technical requirement of a project is such that it should maintain such a critical minimum level which cannot be ensured in a decentralized set up, then the project should not be executed under a decentralized authority. Critics also point out that decentralization often suffers from the problem of externality. The local project might be chosen in such a way that it would optimize the local benefits without giving due consideration to the issues of such added benefits which might be accrued to the agents which are external to the locality. For example, local authorities are often found to give priority to local roads, thus neglecting the major thoroughfares that might serve the inter locality movement in a better way.

A major component of decentralized economy is fiscal decentralization which is attained by devolution of financial power to the local governments. The merits of financial devolution need not be discussed at length. No devolution is effective unless the Local Bodies are endowed with power to mobilize funds for implementing the developmental schemes. The Local Bodies should have enough power to raise tax and non-tax revenues for ensuring fiscal autonomy. However, financial devolution is sometimes criticized on the ground that the local authorities often fail to mobilize tax revenue from the local sources in a satisfactory way. The revenue mobilization by the Local Bodies remain poor in as much as such Bodies have the tendency to shift the burden of taxes to non-locals, which they adopt as a softer option. Also, a decentralized governance is not expected to consider the problem of equity in a fair way. There exist inter-regional variations in resource base.

The disparity can be minimized only by allowing inter-regional transfer of resources that can be taken up only by a higher-level authority, i.e., by a centralized authority⁴.

To sum up, there is always a trade off between benefits of centralization (in the form of equity in inter-regional transfer of resources and efficiency and externality of the centrally sponsored projects) and those of decentralization. While arguing for decentralization this particular point should be taken into consideration.

2. Decentralized Governance in India

In the Indian context, the debate on the advantages and disadvantages of decentralized governance hardly had any practical relevance before the 73rd and the 74th Constitutional Amendment Acts (1992) were passed in the Parliament. The said Acts have for the first time specified some functions of the state, which, with the approval of the concerned State governments might be devolved to the Local Bodies⁵. With the Constitutional mandate for devolving some functions of the state to the Local Bodies, the issue of decentralized governance came in sharp focus in the politics and economics of Indian society.

Following the 73rd Constitution Amendment Act (1992), a new generation of Panchayati Raj Institutions (PRI) has come into being in rural India. The 73rd Amendment Act recognized the fact that the Panchayats in India had not been able to acquire the status of viable peoples' bodies. This was due to several reasons including the absence of regular elections, insufficient representation of the weaker section including the women and above all inadequate devolution of power and lack of financial resources. The Amendment Act introduced a new section in the Constitution of India (Part IX, Section 243), which provided for a *Gram Sabha* (*Gram Sansad*) for the adults in a village or a part of a village (as in West Bengal) or for a group of villages. This was conceived as the basic forum for democratic functioning of the PRI at the grassroots level. The Act also recognized Panchayats at village and the intermediate levels. All the representatives would be of a fixed tenure of five years and the representative nature of these bodies would be maintained by holding elections after the tenure is over. A reservation for women and members of SC and ST communities was also assured. The Act also made it mandatory to make the posts of the *Sabhapati*, *Sabhadhipati* and *Pradhan* (Chairpersons at respective tiers) as elected posts for a fixed tenure of five years. In case of super session, the Constitution makes it mandatory to reconstitute the body within a period of six months from the date of super session.

The most significant parts of the Amended Act are 243G, 243H and 243I where the powers, authorities and responsibilities along with the mechanism by which the funds will be devolved to the PRI at various tiers have been discussed. Briefly speaking, the Act creates a provision (not mandatory, however) for devolution by the State Legislature, of powers and responsibilities, upon the

Panchayats with respect to the preparation of plans for economic development and social justice and for the implementation of development schemes. Provisions have also been made so that funds can be secured for the PRI by securing authorization from state legislatures for grant-in-aid to the Panchayats from the Consolidated Fund of the State, as assignment to or appropriation by the Panchayats of the revenues of designated taxes, duties, fees and tolls. The Constitution also makes it mandatory to set up a Finance Commission for the State within one year of the notification of the Act and thereafter, every five years to review the financial position of the Panchayats and to provide financial awards to the Local Bodies from the consolidated fund of the State for the next five years.

A suitable amendment in Section 280 (Finance Commission) was introduced so that ‘the measures needed to augment the Consolidated Fund of a State to supplement the resources of the Panchayats in the State on the basis of recommendations made by the Finance Commission of the State’⁶ can be taken. In 280C of the Constitution the same provision was made for the Municipalities, as well. Following such amendments a constitutional basis has been created so that the PRI and the Urban Local Bodies can now expect to get regular untied funds for implementing the programme of economic development at their own initiative. A new Eleventh Schedule was appended to the Constitution of India listing out 29 functions concerning issues of rural development on which the powers and authorities of the Panchayats can be created by the State governments. The Amended Act also created a provision for setting a Committee for District Planning so that such functions can be carried out by the PRI in a planned manner.

With respect to the Urban Local Bodies, the same exercise has been performed and the 74th Constitution Amendment Act (1992) incorporated changes in the Constitution of India so that the Urban Bodies may also function as the institutions of self government (part IX A, The Municipalities, Constitution of India). In order to make the constitutional provisions effective the Twelfth Schedule of the Constitution specifies 18 areas in which the Legislature of a State may, by law endow ‘the performance of functions and the implementation of schemes’ (243 (w), *Constitution of India*) to the Urban Local Bodies. However, as in case of the rural Local Bodies, these are to be assigned by the respective State governments.

Following the introduction of the Constitutional (73rd and 74th) Amendment Acts and the follow up State level Conformatory Acts, the scenario has admittedly changed for better. One point should, however, be mentioned in this context. The new Acts have definitely created a basis for decentralization in the functioning of the Indian state. But then, the spirit of Article 40 of the Constitution which wishes the Local Bodies to function as units of self-government is yet to be honoured by the policy makers of the country. The Indian state is yet to take such steps as will endow the Local Bodies with ‘such power and authority as may be necessary to enable them to function as units of self-government.’

Consider, for example, the nature of power and authority that the Local Bodies enjoy even after the said amendments of the Constitution. With respect to the much publicized power of the Local Bodies in the realm of economic development and social justice, there is again a structural limitation that stems from the Constitution itself. The Amendment Acts of the Constitution have listed the subjects on which the third tier of the government can exercise power and enjoy authority, but unlike the autonomy that the provincial governments enjoy in regard to List II of the Seventh Schedule of the Constitution, the Local Bodies have no such authority over any subject listed in the Eleventh and the Twelve Schedule. The extent of power that the Local Bodies might enjoy with respect to these subjects depends on the discretion of the concerned State governments

The basic limitation is that the Local Bodies have very little regulatory power. They are still viewed as agencies of local development under the control of the higher-level authority. Even after the much publicized Constitution (73rd and the 74th) Amendment Acts that define Panchayats and Urban Local Bodies as institutions of self-government, and contain provisions for the devolution of powers and responsibilities upon them, in reality such powers have been vested with respect to preparation and implementation of plans for economic development and social justice only and that also to the extent such authority is assigned to them by the concerned State governments.

The fact is that the Local Bodies cannot have any say over the regulatory functions of the state. The reality in most cases is that the Panchayats have no administrative control even over the staff that serves the Panchayats. As a result, devolution of power and authority for local development following the 73rd Amendment fails to achieve the desired goal of democratic decentralization. As it has been observed

The business of government is vertically arranged with departmental hierarchies stretching from the Minister-in-charge of a particular portfolio at the top to the lowest departmental functionary at ground level. The Panchayats are horizontal interventions in the vertical jungles of administration. Any hope that they would be able to secure horizontal co-ordination was doomed because the vertical hierarchies were well entrenched and the Panchayats did not have even minimum administrative weaponry to bring them within the coordinating discipline (*Mukarji and Bandyapadhyay, 1992,p.9*).

In this context, one may note the following point raised by Mr. E.M.S. Nambudiripad, a member of the Ashok Mehta Committee on the Panchayati Raj Reforms (1979). In his dissenting note, Nambudiripad observes

I am afraid that the ghost of the earlier idea that the Panchayati Raj Institutions should be completely divorced from all regulatory functions and made to confine

themselves only to developmental functions is haunting my colleagues (quoted from *Mukarji and Bandyopadhyay*, 1992, p.4)

The observation seems to be valid even after the 73rd and 74th Amendments of the Constitution that keep Panchayats and Urban Local Bodies confined to developmental activities and that too with very little power over their functions and functionaries. Even after the Constitutional Amendments, the reality is that the Local Bodies do not constitute a tier of the State⁷ in the true sense of the term. While evaluating the performance of the Local Bodies, this limitation, which may be considered as structural limitation, must be taken into consideration.

3. Fiscal Devolution: The Background

The issue of financial autonomy of the Local Bodies, the focus of the present study, is, however, more complex. One cannot hold outright that the performance of Indian Democracy in this regard is as poor as it happens to be with respect to two other building blocks of the autonomous institution of local self-government, viz., functions and functionaries of the Local Bodies. At the same time, as the relevant literature on the subject indicates, the act of devolution in this regard has several limitations that put constraint on the functioning of the Local Bodies even as agencies of local development.

It is true that the 73rd and the 74th amendment of the Constitution have not ignored the issue of fiscal devolution. It has incorporated relevant changes in Article 280 of the Constitution so that the issue of fiscal devolution to the Local Bodies from the Consolidated Fund of the State can be given due consideration. The Union Finance Commission has now the constitutional obligation to suggest 'the measures needed to argument the consolidated fund of a State to supplement the resources for the Panchayats in the State on the basis of the recommendations made by the Finance Commission of the State'. (*Constitution of India*, 280b)⁸.

One immediate benefit of the constitutional mandate is that the issue of local finance is now getting better attention from the Union Government of India. The first Union Finance Commission that had to adhere to the new provision of the Constitution was the Tenth Finance Commission (1995-2000). The commission did not have the opportunity to take up an in depth study of the problems of local finance. Even then met the constitutional obligation by making an ad-hoc provision for the Local Bodies⁹. That the Constitutional mandate has to be taken care of was further revealed in the deliberations of the next Finance Commission, i.e., the Eleventh Finance Commission (EFC). The EFC (2002-05) made a more comprehensive discussion on the problems and constraints of financial devolution in India¹⁰. The Commission had as many as twenty reports of the State Finance Commissions at its disposal to ascertain the needs of the Local Bodies in various States. Furthermore, it had built up its own data base for analysing the problems of local finance in India.

Following a comprehensive review of the issue on the basis of the available information, the EFC had made a recommendation which made it mandatory for the Union Government to devolve a sum of Rs.1600 crores for PRI (and Rs.400 crores for the Urban Local Bodies) for the period 2000–2005. While setting the norm for disbursement of such funds among the States, the EFC had also taken care of the extent of decentralization that a State has achieved. For this, the EFC had set an index on the basis of ten indicators, which was called an index of decentralization¹¹. The percentage share of various States following this index is reproduced from the EFC report in Table A1 of this paper. Admittedly, the index did not favour States such as Kerala, where decentralization did make some progress. On the other hand, it has favoured States like Bihar where there had been the least devolution¹². Again, the total fund allotted to the so called third tier of the State is abysmally poor. But then, the fact that the EFC has honoured the Constitutional obligation by making a recommendation for the Local Bodies on the basis of a norm, as it did in case of the second tier of the government, indicates that the issue of fiscal devolution following the Constitutional Amendment is getting serious attention from the centre of the Republic.

One difficulty with the finance of the Local Bodies is that there is hardly any reliable information on the existing condition of finance pertaining to these Bodies. The anomaly in the inter State variation in the EFC awards for the Local Bodies, following the index value of decentralization, is largely due to this limitation in information. There are 224838 villages and 5811 intermediate level Panchayats along with 3537 Urban Local Bodies in India. The villages Panchayats hardly have the requisite number of personnel for maintaining the records. The State Finance Commissions also fail to garner sufficient information from the line departments of the respective State governments so that a reliable database could be developed for studying the problems of the finance of the Local Bodies in India. The first serious efforts in this regard came from the EFC which appointed two research organizations for carrying out an in depth study on the status of local government finance in India. Based on this research, the EFC had two background papers¹³ and a data set on the local finance in India for the period 1990-91 to 1998-99. The summary of the findings of these studies is given in Section 8 of the EFC report and the state level data on the finance of Panchayats and Urban Local Bodies is given in Appendix VIII.2 of the Report. Based on the data provided by the Eleventh Finance Commission, a set of literature has come up which provide insightful analyses on local finance in India¹⁴. The other important service that the EFC has provided is that it has year marked a sum, to be spent on monitoring the accounts and also another sum for creating a database relating to the finance of the Local Bodies in India. It is expected that in near future a solid data base would be created on the basis of a reliable information on the financial accounts of the Local Bodies, thanks to these EFC grants, so that the future SFC reports would contain more reliable information that would help the researchers and the policy makers understand the financial problems of the Local Bodies in a better way.¹⁵

4. Fiscal devolution: An Analysis of the EFC data

The revenues of the Local Bodies fall into two major categories, namely, own revenue and inter governmental transfer. Own revenues are classified into (a) non-tax revenues such as income from properties, fees, receipts, user charges etc. and (b) tax revenues which can be classified further as (1) own tax revenues assigned and collected by Local Bodies and assigned but collected by the state government and given to Local Bodies and (2) revenues from shared taxes entirely collected by the state government but subsequently shared with the Local Bodies. The second category constitutes of revenue under inter-governmental transfers. Most of these transfers are grants by the Center either directly or through the States, frequently with small additional funding by the individual States¹⁶. Still now, the second category is the most important source of revenue for the Local Bodies. As regards the expenditure items, the major expenditure of the Local Bodies are on account of (1) general administrative services, (2) discretionary and obligatory services and (3) expenditure on developmental activities, mostly under the schemes sponsored by the higher tiers of the government.

The research on the finance of the Local Bodies do indicate that PRIs and Urban Local Bodies (ULBs) are now spending more fund compared to what they used to spend before the Constitutional Amendment. As the EFC has observed (*Report of the EFC, Annexure VIII 2A, VIII 2B*) the total expenditure at the PRI and ULBs level, as a percentage of GDP was 12.24 per cent in 1997-98; the comparable figure for 1992-93 had been only 5.53 per cent. This information, along with the fact that the total expenditure / GDP ratio of Union Government and the Provincial Governments taken together is 15.2 per cent in 1997-98, indicates that the local level revenue expenditure is now playing an important role in the public finance of the economy.

It does not, however, indicate that the Local Bodies are spending the fund more out of their own revenue sources. In fact, the dependence of such bodies on the respective state governments (and also on Central Government) on the financial matters seems to remain as strong as it had been before the 73rd and 74th Amendments. Tax revenue of the Local Bodies (PRI and ULBs) as percentage of the tax revenue of the states had been only 3.11 per cent in 1992-93. By 1997-98, as stated by the EFC, the ratio has increased, but even then it was only 5.01 per cent¹⁷.

Research on fiscal situation at the level of the Local Bodies that have been carried out so far on the basis of the EFC data¹⁸ do indicate¹⁹ that the fiscal basis of autonomy is indeed very weak for the Local Bodies in India. The local tax / GDP ratio for the Local Bodies had been as low as 0.45 per cent in 1997-98. The revenue from other sources (such as non-tax items) had also been abysmally poor. Inter-state variation notwithstanding, the overall scenario is that the PRI and the ULBs depend

very much on the inter-governmental transfer. As observed by Oommen (2000), the financial autonomy ratio (the percentage of locally raised revenue to total local expenditure) had been as low as 4.81 per cent in 1997-98 for the 15 major States in India. There is inter-state variation in this regard. For example, in Punjab the financial autonomy ratio had been as high as 88.66 per cent (1997-98). But there are States like Karnataka where the ratio had been as low as 4.65 per cent for the same reference year. Between the urban and rural Local Bodies, an observable variation in this regard does exist. For example, in Orissa the financial autonomy ratio for the rural bodies had been as low as 6.81 per cent in 1997-98. In the same year the financial autonomy ratio for the urban bodies of the State had been 57.09 per cent. The scenario in each of the 15 major states in India, as worked out by Oommen (2000) is given in Table A.2 of this paper. The results indicate that inter State variation notwithstanding, internal revenue mobilization plays a very limited role in the finance of the Local Bodies in the States of India²⁰.

There is a strong opinion that the PRI and the ULBs fail to mobilize much resources from internal sources largely because they fail to raise revenue by way of the levy of taxes as assigned to them by the respective State governments. Among the reasons for the failure of the Local Bodies in this regard, 'the general reluctance on the part of the Panchayats to levy taxes for fear of erosion in the vote base, lack of necessary administrative machinery to collect taxes and limited capacity to pay tax in the villages, specially in drought hit and other disaster hit villages' (Rangarajan, 2004), are considered as important.

While it is true that the Local Bodies do not perform well in mobilizing local resources, some researchers have observed that there are structural reasons for a low revenue compliance of the Local Bodies. The own levy rights of Panchayats are mainly on buildings and non-agricultural land; taxes on entertainment and motorized vehicles is another important source of local revenue for some tiers of Panchayats. These have least tax buoyancy²¹. The Professional tax which is a constitutionally sanctioned local duty that has much revenue potentiality is not assigned to Local Bodies in any State (except in Kerala). User fees and charges are the sources of revenue in almost every tier of the Local Bodies. But these are the areas where the tax compliance is low.

The PRI in India cannot expand the own revenue base because the assigned items of tax revenue for the Local Bodies have least tax buoyancy. Again, the tax compliance is weak at the village level. A somewhat better scenario as regards tax compliance exists in the intermediate tier of the PRI. But then, the revenue base for the intermediate tiers of the PRI is rather narrow. Roughly about 80 per cent of Panchayat's own revenues are collected by the *Gram Panchayats*, a pattern that remained unchanged between 1990-91 and 1997-98. (Exceptions are Uttar Pradesh and Rajasthan where higher tiers have a substantial share in collection). According to Rajaraman, the revenue potential of the Local Bodies can improve if a crop-specific levy on agricultural land is imposed in rural areas (see Rajaraman, 2004 and 2003).

We should add that the present scenario as regards the collection of revenue from own sources is not as bleak for the Local Bodies as it is projected to be. Following the Constitutional Amendments, the Local Bodies started functioning better. In many States, with some devolution of functions and functionaries, the mobilization of internal revenue improved in a noteworthy way. It may be pointed out that between 1990-91 and 1997-98, there was a doubling in average per capita collection across all states aggregating across all tiers of the Panchayat²² .

5. Fiscal Devolution: Inter Governmental Transfer

While it is true that the performance of the Local Bodies in mobilizing resources from their own sources has improved in the recent years, the fact remains that still now the major source of fund for the Local Bodies is inter governmental transfer of financial resources. Under the Constitutional mandate, the Central Finance Commissions would devolve a sum to the Local Bodies²³ . Again, following the Constitutional Amendment Acts (73rd and 74th), the PRI and the ULBs are supposed to get a devolved fund as inter governmental transfer from the Consolidated fund of the State from the State governments, as well (revenues of designated taxes, duties, fees and tolls collected by the State governments). The devolution of financial resources to these bodies from State governments is supposed to be ensured through periodic constitution of the State Finance Commissions that are required to make recommendations on the sharing and assignment of various taxes, duties, tolls, fees, etc. and on the grants-in-aid to these Bodies from the Consolidated Fund of the States. These provisions are closely related to Articles 243G and 243W of the Constitution.

It is argued that the performance of the Local Bodies in mobilizing revenue from own sources has not been satisfactory. But what about the role of State Governments in executing the provision of inter governmental transfer to the Local Bodies? As the Eleventh Finance Commission has observed, in most of the States in India the extent of devolution through inter governmental transfer, has remained poor. The SFC reports which are supposed to serve as the basis for financial devolution are often prepared in a perfunctory way. Also the SFC reports do not follow a uniform pattern and consequently Central Finance Commission could hardly utilized these reports while suggesting measures for augmenting the financial resource base of the Local Bodies. Again, in many cases, the SFC reports did not specify the sources from which the shared revenue would devolve to the Local Bodies. Even when such reports were placed to the State governments, in some cases, the concerned authorities do not take any step for implementing the recommendations of the SFCs²⁴ .

The basic reason for poor financial devolution is that the Conformationary Acts, in most cases, are weak. For example, there are States such as West Bengal in which the Conformationary Act did not specify the ways and means for achieving financial

(and administrative) autonomy. The Haryana Act specifically states that the objective of the PRI is to 'make arrangement' for administering the rural areas better²⁵. Admittedly, there are States, such as Kerala where 44 State Legislations were amended following the Conformatory Act to broaden the entitlement of Local Bodies. But, these are exceptions to what prevails in the States of India.

Apparently, the problem can be met by appreciating the fact that the Local Bodies are perceived by the Constitution (*Article 40 in the Directive Principles of the State*) as a tier of the government. A tier of the government should have a concomitant revenue base, as in case of the second tier of the state, namely, the Provincial Governments. If the third tier gets the authority to take up the Constitution-sanctioned duties (as in the Eleventh and the Twelfth Schedule), it is logical that it would automatically get a concomitant resource from the Consolidated Fund of the State. Often, this logical consequence of the Constitutional Amendment Acts (73rd and 74th) is not appreciated by the State governments in India.

The Eleventh Finance Commission noted this point while mentioning in its report that a financial devolution for the Local Bodies does not need a measure to augment the Consolidated fund of the State, *per se*. A devolution from the existing Consolidated Fund of the State is possible, to the extent the act of transferring the duties and functions listed in the Eleventh and the Twelfth Schedule of the Constitution is performed by the concerned State. It does not involve the augmentation of resources because the transfer of such duties and functions should involve concomitant transfers of staff and resources from the State government, a measure which does not entail any extra financial burden on the State. As there is a provision for direct devolution from the Central government to the State governments, as per recommendation of the Central Finance Commission, the Local Bodies should also get a devolved fund from the Consolidated Fund of the State, following the recommendation of the State Finance Commissions, as the functions and functionaries are transferred to the Local Bodies. The process of transfer should be as automatic as in case of the second tier of the state of India.

To what extent such devolution has taken place in India? This is the central issue pertaining to financial devolution to Local Bodies. To what extent the State governments have addressed this issue can be discussed by considering the relevant data from the State budgets of India. Such data are available from the Reserve Bank of India (RBI). The RBI in its yearly publication *State Finances: Study of State Budgets* contains this information. In the yearly statement of the State budget, as compiled by the RBI, there are five broad divisions in which the revenue expenditure of the State governments is placed. These are Development Expenditure, Non-development Expenditure, Grants-in-aid and Contributions, Reserve with Finance Department and finally, Compensation and Assignments to Local Bodies and Panchayati Raj Institutions. The last mentioned head contains the quantitative information on the inter governmental transfer to the Local Bodies from the Consolidated fund of a State. Such Compensation and Assignments are supposed to

be untied fund devolved to the Local Bodies but the State budgets sometimes transfer the project-tied funds under this head in order to put on paper that the statutory devolution to the Local Bodies has been honoured.

Be that as it may, the RBI data on Compensation and Assignments to Local Bodies do provide a rich set of information on the extent of inter governmental transfer that has taken place with respect to the Local Bodies in India. In the remaining part of this paper we would analyse these data for the period 1992-93 to 2002-03. The trend of financial devolution over time and the extent of inter State variation in this regard might be discussed on the basis of this data set.

We consider first the scenario with respect to the per capita Compensation and Assignments to the Local Bodies from the State budgets, as derived from the RBI data. The detailed information is given in Table 1²⁶. At the very outset, it should be pointed out that the average per capita revenue expenditure (at constant price) by the Local Bodies due to inter governmental transfer from the State budgets for 16 major States²⁷ of India, taken as a whole, had been increasing steadily over the period (Table 1, last row). Even then there is reason to believe that the extent of devolution as inter governmental transfer to the Local Bodies had still remained poor. This becomes apparent, as we consider the State fund devolved to the Local Bodies as percentage of total revenue expenditure of (Table 6). In 1992-93, the revenue expenditure on Compensation and Assignments to Local Bodies as percentage of total revenue expenditure of the States had been 1.34 per cent. After the introduction of Conformatory Acts, the situation did not improve in a noteworthy way. The relevant percentage was just 1.87 in 2002-03²⁸.

One should not however, hold that the Constitutional Amendments did not have any effect on the State finance in India. The State governments did make some efforts to honour the Constitutional provision and the extent of devolution did increase during this period. The per capita assignment to Local Bodies at constant price had been Rs.14.53 for 16 major States in India. By 2002-03 the per capita revenue expenditure by the Local Bodies has increased to Rs.33.33 (Table 1).

A further analysis of the data, however, indicates that there exists wide variation among the States with respect to inter governmental transfer to Local Bodies. The other indication is that there is much volatility in the disbursements of funds to the Local Bodies in many States of India. On the basis of the data contained in Table 1 and Table 6, the paper attempts to analyse these phenomena in the subsequent part of this discussion.

The Conformatory Acts were passed in all States by April, 1994. The consequential change in the disbursement of the Consolidated fund of the State should be effective at least by the financial year 1996-97. We take this factor into consideration and check whether a change for better has taken place in post

Conformatory Act regime. A dummy incorporated regression analysis considered in Table 1(a) does indicate that the all India data on per capita Compensation and Assignments to Local Bodies do not rule out the possibility that the overall scenario has changed for a better for the Local Bodies in post 1995-96 years²⁹.

To what extent the scenario has changed in the post constitutional reforms period in the States of India? Table 3 considers this issue. The average per capita devolution for the period 1992-93 to 1995-96 (Period 1) in 16 major States in India had been Rs.14.44. The average for the period 1996-97 to 2002-03 (Period 2) was Rs.28.70, i.e., about double the amount recorded in the previous period. Evidently, the scenario has changed for a better, on an aggregate, in the post constitutional reforms period, just as Table 1(a) suggested.

The State level data indicate that in both the periods, average per capita devolution was the highest in Tamil Nadu and the lowest was in Bihar. The difference in per capita devolution to Local Bodies was as high as Rs.32.06 in period1 and Rs.101.65 in period 2, between the best and the worst performer (Table 3). The differences among some other performers were also quite high. The other important feature is that the performance was not consistent over years for some of the States. Thus, the average per capita devolution in West Bengal, the State which is considered as the pioneer in developing the PRI of the new era, had in fact declined in period 2 (the period after the Conformatory Act had been introduced). Haryana and Assam are the other States where the average per capita devolution had declined in period 2. With respect to Kerala, the other States which introduced radical measures for decentralized development by peoples' planning, the per capita devolution remained almost unchanged³⁰ in period 2. Stagnation at a low level of per capita devolution had been observed in States like Rajasthan and Bihar. In some States, such as Maharastra and Uttar Pradesh the tempo of devolution accelerated much following the Constitutional Amendments.

Apparently, there is much volatility in per capita devolution in almost every major State of India. The average value of per capita devolution for a particular period might not therefore, indicate much about what is really happening in the States. A better measure, particularly for studying the relative performance, would be the rank of the States according to the average rank scores on per capita devolution for the period under study. We, therefore, rank the States in terms of per capita devolution for each year and find the average rank score for a State for a given period. The States are then ranked again in terms of their average rank scores for Period 1, Period 2 and also for the entire Period. The results have been recorded in Table 4.

Ranks of the states in two periods calculated on the basis of average rank scores indicate that Karnataka and not Tamil Nadu had been the best performer in Period 1. In fact, Karnataka was followed by Tamil Nadu, Madhya Pradesh and West Bengal (all having the same rank). Bihar, Rajasthan and Assam had been in the other

end of the distribution of States according to average rank scores. As Table 4 indicates, the ranks of the States according to average rank scores for two different periods did not differ much in case of the majority of the States. However, the rank of West Bengal declined sharply (from rank 2 to rank 8). For Kerala also there was deterioration in rank after 1995-96. Among the States, which have improved their relative positions after 1995-96, there are Uttar Pradesh (rank 7 to rank 4) and Maharashtra (rank 11 to rank 6). The scenario remained almost the same for Orissa and Haryana; Bihar holds the last position in both the periods. Considering the entire period, we observe that Tamil Nadu is the best performer (the distinction that it obtained not in period 1, but in period 2) and the next best is Karnataka. Among the 16 major States the position of West Bengal and Kerala are the 6th and the 7th respectively. The worst is the performance of Bihar. Rajasthan, Assam and Haryana are the other States in which the per capita devolution from the Consolidated fund of the State did not register a noteworthy progress (Table 4).

With respect to 16 major States the extent of volatility in the yearly per capita devolution to Local Bodies, as measured by coefficient of variation, has been reported in Table 5. Noting that a low coefficient of variation would indicate that the State has a high temporal consistency in per capita devolution to the Local Bodies, we observe that for the entire period of 11 years, the performance of West Bengal was the best among the 16 major States in India in terms of this indicator. Gujarat and Punjab are the other two States in which the overall rank with respect to variation in per capita revenue expenditure is the second and the third respectively. The most volatile was the scenario in Orissa and Maharashtra where the coefficient of variation had been as high as 100.2 per cent and 88.79 per cent respectively. In pre-Conformatory Act years, the least volatile had been the performance of Andhra Pradesh which was followed by Rajasthan and Gujarat. The highest volatility had been registered in Orissa. Bihar and Haryana had been two other States where volatility had been very high. It is interesting to note that Tamil Nadu, the State which ranked very high in terms of per capita devolution had also been the State where volatility had been the highest in Period 1 and very high (rank 9) in Period 2. West Bengal was the State in which the variation was the least (6.15 per cent) in post 1995-96 period, Haryana being the State where the volatility had been the second highest in this period. As we get from Table 5, the overall volatility was higher in the period when the States were devolving funds under Constitutional mandate.

The presence of high volatility does not indicate that the per capita devolution had been very low in the concerned State. Thus, in Tamil Nadu where the coefficient of variation in per capita devolution had been as high as 50.39 per cent in period 1, the per capita devolution, as Table 3 indicates, had been the highest (Rs.32.33). On the other hand, Rajasthan which ranked second in terms of the extent of absence of volatility in period 1 had average per capita devolution of Rs.2.78 only.

The performance of a State should not be measured only by the amount of fund that it devolves, on an average, to the Local Bodies, neither should it be

measured by the indicator of consistency in the act of devolution, alone. What we need is a measure by which we can capture the performance of a State in terms of both average per capita devolution and the extent of consistency in it. In a measure that considers both these attributes, the relative performance of a State can be assessed in a balanced manner. A State which ranks very high in terms of per capita devolution and at the same time has a low value of coefficient of variation (indicating a high level of temporal consistency) would be a good performer.

We would now consider the performance of the States in terms of this twin measure. Based on the information contained in Table 5 we classify the States in four groups, separately in terms of rank in average per capita devolution and the rank with respect to coefficient of variation in per capita devolution for a given period. Groups are arranged in descending order of performance, namely, I (Rank 1 – 4), II (Rank 5-8), III (Rank 9- 12) and IV (Rank 13 – 16)³¹. We then find the combination of ranks with respect to per capita devolution and the associated coefficient of variation for each State for the periods under study. Evidently there would be 16 combinations out of which the combination (I, I) would indicate the best, i.e., a State with very high per capita devolution with low level of variation in devolution for the period under study. Similarly, the combination (IV, IV) would indicate the group of worst performers. The results of this exercise are described graphically in Figure 1, Figure 2 and Figure 3 of this paper.

As we get from Figure 1, in period1, West Bengal had been the only State in Group (I, I). This State which was ranked 1 in terms of per capita devolution and ranked 4 with respect to CV appears to be the best performer in this period.. In the worst group we have Orissa, Haryana and Bihar. Kerala, Uttar Pradesh and Himachal Pradesh had been moderate performers in the pre Conformatory Act period. In the post Conformatory Act period, the scenario changed. Karnataka and Madhya Pradesh now belonged to the group of best performers. Rajasthan, Orissa and Haryana were however, in the worst group. Bihar had not been included in this group. This is because, the State maintained a low profile both in terms of per capita devolution and its dispersion over time consistently over this period. The overall scenario (for the entire period) is that Madhya Pradesh and Punjab are the best performers; they have high per capita devolution with a low level of volatility. West Bengal failed to attain this distinction as it had been ranked 6 in terms of per capita devolution to its Local Bodies. In the group of worst performers, we have Orissa and Haryana, as figure 3 points out. Bihar was excluded because its rank according to coefficient of variation had been 6 when we had considered its performance over the period of 11 years from 1992-93.

The analysis on per capita devolution lays bare the following features of financial devolution to Local Bodies in Indian States. In the first place, compared to what a State government spends in a year as its own Revenue Expenditure, the amount of per capita devolution to Local Bodies is very low even in the post reforms period. Nevertheless, in the post Conformatory Act days, there had been some

improvement in the scenario, as the regression analysis on the all India data on per capita devolution to Local Bodies indicates. Among the 16 major States, the performance had been commendable for States like Tamil Nadu, Madhya Pradesh, Punjab and Karnataka. The worst performers are States like Bihar, Rajasthan, Haryana and Assam. Data also indicate that there is much volatility in the performance of the States. Considering both per capita devolution and the volatility in the act of devolution by States over years, it appears that Madhya Pradesh and Punjab were the best in meeting the twin requirement of a high per capita devolution and a low variation in the fund devolved to the Local Bodies to be called the best among the 16 major States in India for the entire period of 11 years under study. West Bengal and Kerala did not perform well, particularly in the post Conformatory Act years. While Kerala might be considered to have a better devolution, given the fact that the State has already widened the own tax base of the Local Bodies, the case of West Bengal remains problematic. The State has enacted a large number of State Acts for facilitating decentralization but, as the RBI data indicate, it has not done much for ensuring financial decentralization at the level of the Local Bodies.

To what extent the financial devolution at the level to Local Bodies has been attained can also be measured by considering the share of Compensation and Assignments to Local Bodies in the Total Revenue Expenditure of a State. In fact, such a measure would be a better indicator of the relative importance that the Local Bodies are getting in the disbursement of funds from the respective State governments. For 16 major States in India we perform this exercise on the basis of the RBI data for a period of 11 years from 1992-93. Table 6 contains the State specific information pertaining to this measure in the States of India for the above mentioned period.

While the per capita devolution in constant prices has increased substantially during this period, as Table 1 indicates, the information contained in Table 6 suggests that the percentage of State fund devolving to the Local Bodies did not increase much during this period. For the 16 major States, taken together, the percentage of State fund devolved to the Local Bodies had been 1.34 in 1992-93. Following the Constitutional reforms, the ratio has increased. But then, the Compensation and Assignments to Local Bodies as percentage to Total Revenue Expenditure of the States has increased only to 1.87 per cent in 2002-2003. On an average, the ratio had been 1.48 per cent during this period. In no way, the extent of devolution could be noted as impressive.

One should not, however, ignore the fact that the Constitutional reforms did have a positive effect on the financial devolution to the Local Bodies. In period 1, i.e., in the pre-Constitutional reforms period, the percentage of State fund devolved had been 1.16. In the post-reforms period the combined average for the 16 States had been 1.66 per cent (Table 7). Admittedly, the share of the Local Bodies has increased after the reforms, although not at a very high rate. Moreover, as in case of per capita Assignments to Local Bodies, the percentage of devolved fund had an upward leap following the Constitutional Amendments (73rd and 74th). As we get from Table

6(a), there is a clear indication in the all India data that the trend of the percentage of State fund devolved to the Local Bodies should have a break in 1996-97. The dummy incorporated regression model on the all India data indicate that the hypothesis of no trend break in 1996-97 is rejected at 1% level of significance. Furthermore, a positive value for intercept term (b_0) indicates that the post reforms period percentages should be located at higher values.

A further analysis of the data, however, indicates that over the period of 11 years the yearly growth rates in the share of Local Bodies in the State budgets of 16 major States of India were converging (beta convergence) over time. The possibility of having growth convergence was calculated on the basis of the growth rates of first five years so that the change in growth behaviour following constitutional reforms could be incorporated in studying the growth convergence. The (log) linear regression on growth rates, as given in Figure 4 does indicate that the slope of the regression is negative, being significant at 5% level of significance. However, the rate of convergence is very low, as the value of b_1 indicates. The other interesting feature is that the dispersion across the States in terms of percentage of State funds devolved to the Local Bodies has in fact a tendency to diverge over time (Figure 5). The tendency of divergence is quite strong as the value of the slope of regression, which is significant at 5% level, indicates. The implication is that, following the constitutional reforms, the bad performing States are catching up the good performers in terms of growth in financial devolution to the Local Bodies although the rate at which the 'catching up' takes place is very low. At the same time the variation among the States in honouring the Constitutional mandate does remain quite powerful possibly due to huge initial differences on which the growth convergence is taking place. One would, however, hope that with a convergence in the growth rates, the inter State variation in devolution to Local Bodies would reduce further in future.

Before 1996-97, the per cent devolution to Local Bodies from the State budget, averaged over 1992-93 to 1995-96 had been the highest in West Bengal. In the next period the relative performance of West Bengal deteriorated. States such as Tamil Nadu, Madhya Pradesh and Uttar Pradesh performed better as Table 7 indicates. In fact, Tamil Nadu was now the best performer, recording an average devolution of 4.66 per cent from the State budget to its Local Bodies this is consistent with the earlier observation that the per capita devolution was the highest in Tamil Nadu during 1996-97 to 2002-03. Karnataka and Madhya Pradesh retained their respective positions in Period 2 as the leading States to honour the mandate of the Constitution. Maharashtra improved its position in post 1995-96 period, so also did Orissa. Andhra Pradesh, Kerala and Punjab had been the moderate performers in the first period (1992-93 to 1995-96). They retained their positions in Period 2, as well³². The worst performer, in both the periods had been Bihar. Assam along with Himachal Pradesh had been the other States where the performance had not been good.

What transpires is that the nature of inter-State difference in percentage of State fund devolved to the Local Bodies was more or less the same, as it happened to be in case of per capita devolution. The implication is that the bad performers were performing bad because they were devolving proportionately less from the Consolidated Fund of the State, than the good performers; the results indicate that the per capita devolution was less for the bad performers not in spite of a higher rate of transfer to the Local Bodies.

If we consider the performance of the States in two different periods in terms of rank of the average rank scores on percentage of State fund devolved to the Local Bodies in a given period, it appears that the performance of West Bengal had been the best in pre-reforms period (Table 8). Following the reforms, the position of West Bengal relegated to Rank 5. The worst performer, i.e., Bihar ranked 16 among 16 major States in the post-reforms period as well. The consistency in rank was observed in case of Andhra Pradesh, Karnataka, Madhya Pradesh and Punjab. The impact of Constitutional reforms was very strong in Maharashtra. The rank of Maharashtra had been 10 in pre-reforms period. After the Conformatory Act had been introduced, the Maharashtra government devolved a large proportion of State fund to the Local Bodies. Consequently, the relative position of Maharashtra change for better. Its rank in the post reforms period improved to 6.

Comparing with the results contained in Table 4, it appears that the rank according to per capita devolution to Local Bodies had been consistently better than the rank according to the percentage of fund devolved from the State budget for some of the States (Karnataka, Himachal Pradesh and Punjab). It was consistently worse in case of Orissa and Uttar Pradesh. Rank according to per capita devolution almost matched with that according to percentage of State fund devolved to the Local Bodies in case of Tamil Nadu, Madhya Pradesh and Karnataka among the good performers. In general, rank consistency was also observed in case of the States having low rank positions.

The volatility of the States in the matter of fiscal devolution can be captured by considering the coefficient of variation of the devolution percentages. This exercise was performed in Table 9. As we get from Table 9, the least volatile had been the scenario in Andhra, if we consider the dispersion for the entire period. The most volatile had been the scenario in Haryana. West Bengal along with Uttar Pradesh, Punjab and Bihar had been the States where the volatility had been moderate. In the pre-reforms period the most volatile was the situation in Haryana and the least volatile had been the situation in Rajasthan³³. In the post-reforms period, wide yearly variation in the percentage of State fund devolved to the Local Bodies was observed in Uttar Pradesh, Bihar and Himachal Pradesh. The volatility was the least in Madhya Pradesh which was followed by Karnataka.

Comparing the variation in percentage of devolved fund with that in per capita devolution, we find that a somewhat consistency was observable in every period for Gujarat, Karnataka, Maharashtra and Madhya Pradesh where the volatility in per capita devolution was very near to the volatility in the percentage of devolved fund over years. Rank according to coefficient of variation in percentage of devolved fund differed widely from the rank according to coefficient of variation in per capita devolution in post-reforms period in case of Bihar, Orissa, Rajasthan and Uttar Pradesh. Over the entire period of 11 years the most consistent behaviour was found in Tamil Nadu, Rajasthan, Orissa and Himachal Pradesh. In West Bengal, the volatility in per capita devolution was the least, but the State ranked 7 in terms of the coefficient of variation in the percentage of State fund devolved to the Local Bodies.

We pointed out, while analyzing the data on per capita devolution, that a better measure for the consistency in the behaviour of a State in implementing the Constitutional provision for financial devolution is the performance of the State in terms of both the average behaviour and the dispersion over a specified period pertaining to the indicator that we adopt. We also argued that the performance of a State should be considered as the best if it belongs to a group in which the rank in terms of average rank scores for a period is between 1 and 4, (category I) and at the same time, the rank according to coefficient of variation is in the same category. The worst performer would be the State belonging to category IV with respect to both the average and the coefficient of variation in the given period. While considering the performance of the States with respect to the percentage of State fund devolved to the Local Bodies, we may analyze the data of Table 9 following this approach. In Figure 6, Figure 7 and Figure 8 we describe the results of this exercise for period 1, period 2 and the entire period of 11 years respectively. As it appears from Figure 6, no State can be considered to belong the category of best following this criterion. In the group of the worst States, in period 1, the only State that met this criterion have been Haryana (14 in rank according to ARE1, and 16 in rank according to CV1). This highlights the fact that the average of the per cent devolved to the Local Bodies for various States did not maintain consistency except in case of Haryana which had been a poor performer, in the pre-reforms years. In the post-Constitutional reforms period (period 2), the States belonging to category 1 on both the counts were Madhya Pradesh (2 in ARE2 and 1 in CV2) and Karnataka (4 in ARE 2 and 2 in CV2). In the group of worst performers we have Assam and Bihar. The other States for which rank in per cent devolved had not been consistent with the rank according to the measure of variation of the fund devolved during this period are Uttar Pradesh, Tamil Nadu, Rajasthan and Haryana (Figure 7). If we consider the overall scenario (Figure 8), it appears that Karnataka and Madhya Pradesh had been the best performer and Haryana had been the only State in the group of worst performers.

Considering the performance of the States with respect to both average per capita devolution in a period and percentage of State fund devolved to the Local Bodies, what transpires is that on the basis of the performance of the States over the entire period of 11 years, Madhya Pradesh should be considered as the 'best' among

the 16 major States in India, in the act of devolving State funds to the Local Bodies. It was the State in which the rank according to per capita devolution among the 16 major States of India had been 3 and the rank according to coefficient of variation of the per capita devolution had been 4. on the basis of the other criterion, namely, the percentage of State fund devolved to the Local Bodies, the rank of Madhya Pradesh for the entire period of 11 years was 2 and the rank in terms of coefficient of variation in the State fund devolved to the Local Bodies was also 2. The State thus belonged to the category I on both the measures of relative performance of States in the act of financial devolution to the Local Bodies. Tamil Nadu, which apparently is the best performer had, in fact, been the State in which the coefficient of variation in both per capita devolution and the devolved State fund had been very high (ranked 12 in both the cases). West Bengal was the State in which the coefficient of variation had been at the median level for the percentage of State fund devolved; in terms of average per capita devolution, the variation in the State had been the smallest (rank 1). However, the State ranked 6 among the 16 major States when we consider the average per capita devolution that took place during the period of 11 years. They did not perform as high as Madhya Pradesh did.

6. Concluding Observations

The Local Bodies in India function with the limitation that they are not endowed with such power and authority that may enable them to function as the third tier of the government. However, following the Constitutional reforms the issue of fiscal autonomy of the Local Bodies is getting more attention from the concerned authorities of the State. The research on the basis of the EFC data on fiscal situation in the Local Bodies indicate that the fiscal basis of autonomy is indeed very weak for the Local Bodies in India. The PRI and the ULBs fail to realize much resources from their own sources, largely because the Local Bodies operate on a very weak revenue base. The assigned items of tax revenue for the Local Bodies are very few in number and these have least tax buoyancy. The revenue potential of the Local Bodies can improve if the tax base is widened empowering them professional taxes and to levy a crop-specific tax on agricultural income.

What the paper highlights is that the Local Bodies can function in a better way if the devolution from the Consolidated Fund of the State, following the Constitutional provision, is ensured by the State governments as and when the functions of the State as outlined in the Eleventh and Twelfth Schedule of the Constitution are devolved to these Local Bodies at a greater scale. It does not involve the augmentation of the existing resources. Local Bodies can take up these devolved responsibilities, even without strengthening its own revenue base any further, only if a concomitant devolution takes place from the Consolidated Fund of the State. On the basis of the RBI data on the State budgets the paper argues that this is not being done by the State governments at the required level. The paper analyses the State specific data on Compensation and Assignments to the Local Bodies and concludes that both the average per capita devolution and the percentage of State fund devolved to the

Local Bodies remained abysmally poor during the period 1992-93 to 2002-03. The average per capita devolution in 16 major States of India taken as a whole, had been only Rs.23.51. The percentage of State fund devolved to these Bodies had been 1.48, on an average, over the years.

A further analysis of the data indicate that the Constitutional Amendments (73rd and 74th) did have a positive impact on the act of financial devolution to the Local Bodies. A trend break in the data is discernable at 1996-97 in case of both per capita devolution and the share of the Local Bodies in the Consolidated Fund of the State. The data also indicate that the growth rates in the share of the Local Bodies have a tendency to converge (weak but statistically significant). A tendency of divergence in the dispersion of these shares has also been observed at the same time. It seems that following the Conformatory State Acts the inter-State variation in the percentage of State fund devolved to the Local Bodies, which is very high, did not decline. However, the growth rates in the share of the devolved fund have developed a tendency of convergence. Although the tendency is still weak, it has a significance that should not be ignored. By next few years the magnitude of year-wise inter-State variation in devolution to Local Bodies is likely to be reduced, if the growth rates come still closer to one another.

But the contemporary reality is that there exists wide inter-State variation both in per capita devolution and in the percentage of State fund devolved to the Local Bodies. There are States like Tamil Nadu where the average per capita devolution is as high as Rs.76.48. At the other extreme there are States like Bihar (which includes Jharkhand) in which the per capita devolution is as low as Rs.0.20. The RBI data also indicate that the dispersion over years in both average per capita devolution and the percentage of fund devolved to the Local Bodies vary widely among the States. There are States like Orissa and Maharastra in which the coefficient of variation had been as high as 100.2 per cent and 88.79 per cent respectively in average per capita devolution over 11 years. There are also States like West Bengal and Gujarat where the dispersion have been low (13.21 per cent and 23.62 per cent respectively).

Considering both the average per capita devolution and its coefficient of variation along with average of the percentages devolved to the Local Bodies over the entire period of 11 years and their coefficient of variation, we observe that the best performer had been the State of Madhya Pradesh. Other good performers are Karnataka and Punjab. Bihar, Haryana, Assam and Orissa are the States where the Local Bodies were not getting the benefits of the Constitutional mandate in the way the other States were receiving. There might be State specific reasons for variation in the act of financial devolution which should be analysed. But this is outside the scope of this paper.

Table 1: Per capita Revenue expenditure (at constant price) of 16 Major States: Compensation & Assignments to Local Bodies & Panchayati Raj Institutions. (Rs.)

State	1992-93	1993-94	1994-95	1995-96	1996-97	1997-98	1998-99	1999-00	2000-01	2001-02	2002-03
Andhra Pradesh	9.70	10.12	9.93	9.11	10.71	13.42	14.66	11.75	14.11	22.88	20.91
Assam	3.03	4.09	2.20	3.27	1.31	2.18	2.84	1.77	2.17	0.90	2.78
Bihar*	0.34	0.30	0.26	0.16	0.16	0.15	0.15	0.17	0.13	0.18	0.17
Gujarat	6.88	5.99	7.05	7.36	7.96	8.48	7.62	7.04	6.43	6.86	12.73
Haryana	7.33	3.38	3.28	4.03	3.14	0.20	0.18	0.16	4.66	9.03	4.72
Himachal Pradesh	7.74	6.85	5.99	6.24	6.53	14.85	18.13	22.35	21.92	21.22	53.99
Karnataka	29.56	26.69	27.69	19.76	31.28	41.83	47.00	56.02	65.78	66.31	64.48
Kerala	14.74	20.24	19.39	20.48	30.04	31.58	11.51	17.23	11.21	13.05	12.75
Madhya Pradesh*	19.43	21.24	19.66	27.95	32.71	31.50	36.38	54.16	44.30	37.08	40.57
Maharashtra	7.94	5.31	4.82	4.51	7.82	12.25	13.73	41.55	46.92	34.52	51.90
Orissa	4.54	6.10	1.32	3.15	3.63	5.99	4.81	3.98	26.53	25.26	24.22
Punjab	17.39	27.17	19.82	24.29	23.59	23.42	22.64	14.80	23.91	42.44	27.70
Rajasthan	2.81	2.52	2.72	3.07	2.85	2.73	3.87	2.31	2.01	2.04	0.02
Tamil Nadu	56.01	22.78	20.54	29.99	44.36	105.06	122.32	116.08	102.32	71.57	150.23
Uttar Pradesh*	18.48	15.55	14.18	14.79	15.04	29.18	38.11	35.54	42.40	35.24	43.81
WestBengal	26.51	24.83	25.53	20.88	19.00	20.42	19.11	21.53	17.95	20.19	20.74
Avg. for 16 Major States	14.53	12.70	11.52	12.44	15.01	21.45	22.69	25.40	27.05	25.55	33.23

Source: Compiled from RBI data (State Finances: Study of State Budgets; various years) deflated by wholesale price index (base 1993-94) and the State population data** for various years

Note: ** the State population for each year (except 2001-02) on the basis of the estimated growth rate of population between 1991 and 2001. For 2001-02, the Census (2001) Population data has been used.

* We have combined the data for Chatisgarh, Jharkhand and Uttaranchal with Madhya Pradesh, Bihar and Uttar Pradesh respectively and have dropped Delhi; the number of States has thus reduced to 16.

Table 1(a): A Dummy Variable incorporated Regression Analysis of Intertemporal Behaviour of Per capita Devolution to Local Bodies (All India@)

Regression Coefficients	PER CAPITA REV. EXP.
b_0	7.987*
b_1	1.924*
b_2	0.960

Source: As in Table 1

Note:

The Model:

$$Y_I = b_0 + b_1t + b_2D_1t + u_j, \text{ Where, } D_1 = 1 \text{ for period } 1996-97 \text{ \& above} \\ = 0, \text{ Otherwise}$$

* = Significant at 1% level.

@ = 16 Major States of India.

Table 2. Average Per Capita total Revenue Expenditure and Per Capita Devolution to Local Bodies) in 16 major States: 1992-93 to 2002-03 at current prices (Rs.)

States	Total Rev	Devolved to Local Bodies	Percentage devolved
Andhra Pradesh	2168.68	22.03	1.02
Assam	1873.27	3.22	0.17
Bihar*	1141.92	0.29	0.03
Gujrat	2904.30	12.00	0.41
Haryana	328.95	6.23	1.89
Himachal Pradesh	5082.37	25.22	0.50
Karnataka	2379.74	73.56	3.09
Kerala	2681.95	25.81	0.96
Madhya Pradesh*	1688.30	57.52	3.41
Maharashtra	2717.92	38.27	1.41
Orissa	1828.06	18.66	1.02
Punjab	3631.59	38.54	1.06
Rajasthan	2024.80	3.13	0.15
Tamilnadu	2630.23	133.33	5.07
Tripura	3812.43	59.98	1.57
Uttarpradesh*	1462.35	47.09	3.22
WestBengal	1832.19	31.20	1.70
All States	2040.63	36.75	1.80

Source: RBI, Study of State Budgets

Table 3. Average Per Capita Devolution (at constant price) to Local Bodies (Rs.): 16 Major States in India

State	Average (1992-93 to 1995-96)	Average (1996-97 to 2002-03)	Average for the entire period
Andhra Pradesh	9.72	15.49	13.39
Assam	3.15	1.99	2.41
Bihar*	0.27	0.16	0.20
Gujarat	6.82	8.16	7.67
Haryana	4.51	3.16	3.65
Himachal Pradesh	6.71	22.71	16.89
Karnataka	25.92	53.24	43.31
Kerala	18.71	18.20	18.38
Madhya Pradesh*	22.07	39.53	33.18
Maharashtra	5.65	29.81	21.03
Orissa	3.78	13.49	9.96
Punjab	22.17	25.50	24.29
Rajasthan	2.78	2.26	2.45
Tamil Nadu	32.33	101.71	76.48
UttarPradesh*	15.75	34.19	27.48
WestBengal	24.44	19.85	21.52
All States	14.44	28.70	23.51

Source: As in Table 1

Table 4: Ranks of the States according to Average Rank Scores on Per Capita Revenue Expenditure devolved to the Local Bodies

State	Avg. Rank Score of Period 1	RANK 1	Avg. Rank Score of Period 2	RANK 2	Avg. Rank Score for the entire period	GRAND RANK
Andhra Pradesh	8	8	8.86	10	8.55	10
Assam	13.5	14	14.43	15	14.09	14
Bihar*	16	16	15.71	16	15.82	16
Gujarat	10.25	10	11.29	12	10.91	11
Haryana	12.25	12	13.71	13	13.18	13
Himachal Pradesh	9.75	9	7.43	7	8.27	9
Karnataka	2.75	1	2.29	2	2.45	2
Kerala	6	6	8.43	9	7.55	7
Madhya Pradesh*	3	2	3.43	3	3.27	3
Maharashtra	10.75	11	6.57	6	8.09	8
Orissa	13	13	9.86	11	11	12
Punjab	3.75	5	6.00	5	5.18	4
Rajasthan	14.5	15	14.00	14	14.18	15
Tamil Nadu	3	2	1.00	1	1.73	1
Uttar Pradesh*	6.5	7	5.14	4	5.64	5
West Bengal	3	2	7.86	8	6.09	6

Source: As in Table 1

Note: Grand Rank = Rank according to the Average Rank Score for the entire period.

Period 1 = 1992-93 to 1995-96

Period 2 = 1996-97 to 2002-03

Entire Period = 1992-93 to 2002-03

Table 5: Rank of the States according to the CV and year-wise Rank of Average of per capita Revenue Expenditure devolved to the Local Bodies

State	ARE 1	CV1	Rank according to CV 1	ARE 2	CV 2	Rank according to CV 2	GRAND ARE	CV	Rank according to CV
Andhra Pradesh	8	4.52	1	10	29.77	7	10	34.46	5
Assam	14	24.67	11	15	36.08	10	14	37.76	7
Bihar*	16	28.02	13	16	9.48	2	16	35.56	6
Gujarat	10	8.62	3	12	26.12	5	11	23.62	2
Haryana	12	42.45	14	13	104.93	16	13	78.24	13
Himachal Pradesh	9	11.67	5	7	65.45	14	9	83.30	14
Karnataka	1	16.51	8	2	25.59	4	2	40.44	10
Kerala	6	14.38	7	9	48.64	11	7	38.17	8
Madhya Pradesh*	2	18.13	9	3	19.72	3	3	32.86	4
Maharashtra	11	27.74	12	6	61.10	13	8	88.79	15
Orissa	13	53.83	16	11	82.50	15	12	100.20	16
Punjab	5	19.81	10	5	33.01	8	4	29.44	3
Rajasthan	15	8.20	2	14	52.02	12	15	39.03	9
Tamil Nadu	2	50.39	15	1	34.05	9	1	58.83	12
UttarPradesh*	7	12.09	6	4	28.51	6	5	43.76	11
WestBengal	2	10.11	4	8	6.15	1	6	13.21	1
ALL STATES	X	9.83	X	X	22.94	X	X	36.18	X

Source: Compiled from Table 1

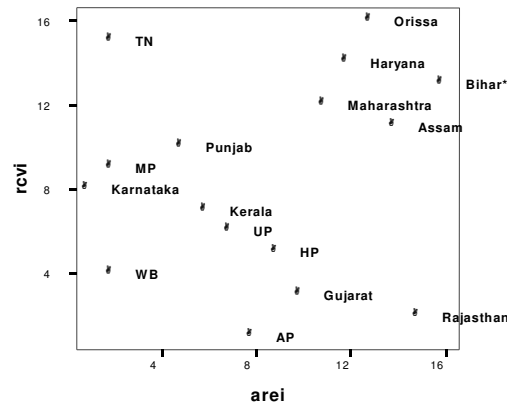
Note: CV1 = Coefficient of variation for 1992-93 to 1995-96

CV2 = Coefficient of variation for 1996-97 to 2002-03

CV = Coefficient of variation for 1992-93 TO 2002-03

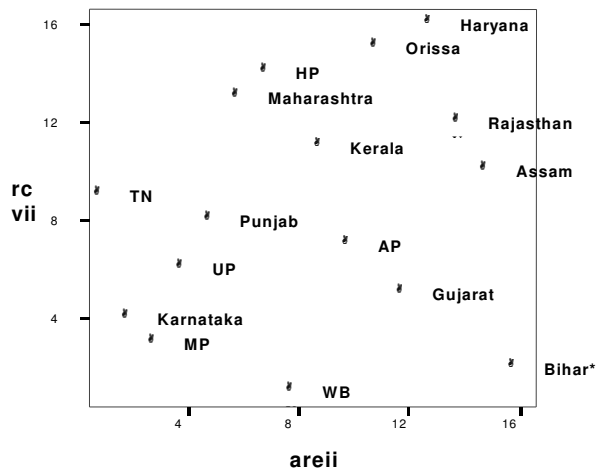
ARE = Rank According to Average Rank Score of Per capita Revenue Expenditure (as in Table 4)

Figure 1: Dispersion of the Ranks of the States according to Per capita devolution to Local Bodies and its Coefficient of variation (1992-93 to 1995-96)



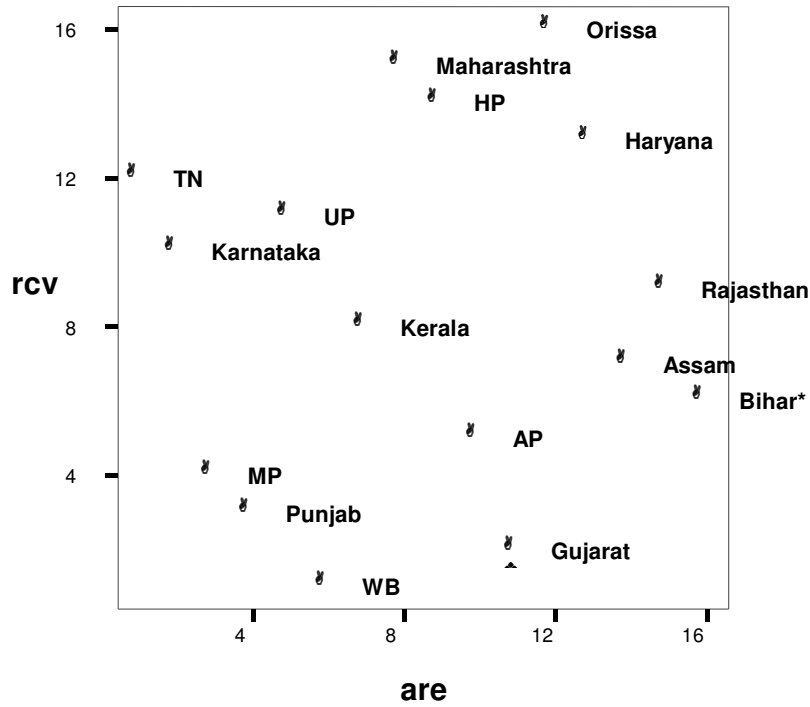
Note: rcvi : Rank according to Coefficient of variation in Period 1
 arei : Rank according to Average Rank Score in Period 1

Figure 2 : Dispersion of the Ranks of the States according to Per capita devolution to Local Bodies and its Coefficient of variation (1996-97 to 2002-03)



Note: rcvii : Rank according to Coefficient of variation in Period 2
 areii : Rank according to Average Rank Score in Period 2

Figure 3: Dispersion of the Ranks of the States according to Per capita devolution to Local Bodies and its Coefficient of variation (1992-93 to 2002-03)



Note: rcv : Rank according to coefficient of variation in entire Period are: Rank according to Average Rank Score in entire Period

Table 6: Compensation and Assignments to Local Bodies as Percentage to Total Revenue Expenditure of the State (1992-93 to 2002-03): 16 Major States of India.

State	1992-93	1993-94	1994-95	1995-96	1996-97	1997-98	1998-99	1999-00	2000-01	2001-02	2002-03(RE)
Andhra Pradesh	0.84	0.86	0.81	0.73	0.67	0.88	0.89	0.70	0.71	1.13	0.98
Assam	0.26	0.33	0.18	0.27	0.11	0.00	0.23	0.11	0.14	0.06	0.14
Bihar	0.04	0.04	0.04	0.02	0.02	0.02	0.02	0.02	0.02	0.02	0.02
Gujarat	0.43	0.37	0.46	0.46	0.45	0.43	0.33	0.28	0.23	0.25	0.47
Haryana	0.48	0.17	0.10	0.17	0.11	0.01	0.01	0.01	0.21	0.35	0.17
Himachal Pradesh	0.33	0.27	0.23	0.22	0.22	0.42	0.44	0.50	0.47	0.45	0.99
Karnataka	2.23	2.00	2.02	1.36	1.90	2.52	2.67	2.73	3.19	3.03	2.83
Kerala	1.09	1.40	1.29	1.29	1.71	1.56	0.54	0.68	0.46	0.57	0.51
Madhya Pradesh	2.19	2.15	2.18	2.91	2.87	2.86	2.92	4.01	3.53	2.60	2.65
Maharashtra	0.51	0.33	0.31	0.27	0.42	0.63	0.69	1.90	1.85	1.41	2.04
Orissa	0.44	0.57	0.12	0.27	0.31	0.50	0.35	0.24	1.69	1.51	1.38
Punjab	0.97	1.41	0.79	1.14	0.96	0.90	0.87	0.49	0.76	1.31	0.74
Rajasthan	0.23	0.20	0.22	0.22	0.21	0.21	0.25	0.13	0.11	0.12	0.00
Tamil Nadu	3.42	1.48	1.38	1.95	2.54	5.55	5.85	4.95	4.50	3.32	5.91
Uttarpradesh	1.91	1.70	1.54	1.56	1.55	2.78	3.35	2.99	3.50	2.92	3.16
West Bengal	2.99	2.53	2.69	2.14	1.72	1.80	1.44	1.25	1.00	1.12	1.12
ALL STATES	1.34	1.12	1.06	1.11	1.20	1.67	1.69	1.84	1.79	1.56	1.87

Source: Study of State Budgets, Reserve Bank of India, Various years.

Note: As in Table 1 RE= Revised Estimate.

Table 6(a): A Dummy Variable incorporated Regression Analysis of Intertemporal Behaviour of Devolution to Local Bodies as Percentage of Total Revenue Expenditure (all States^a)

Regression Coefficients	Percentage of Local to Total Rev. Exp.	Point to Point Growth rate of Local to Total Rev. Exp.
b ₀	1.025*	0.006
b ₁	0.038	-0.016
b ₂	0.271	0.205

Note:

The Model:

$$Y_I = b_0 + b_1t + b_2D_1t + u_j, \text{ Where, } D_1 = 1 \text{ for period } 1996-97 \text{ \& above} \\ = 0, \text{ Otherwise}$$

* = Significant at 1% level.

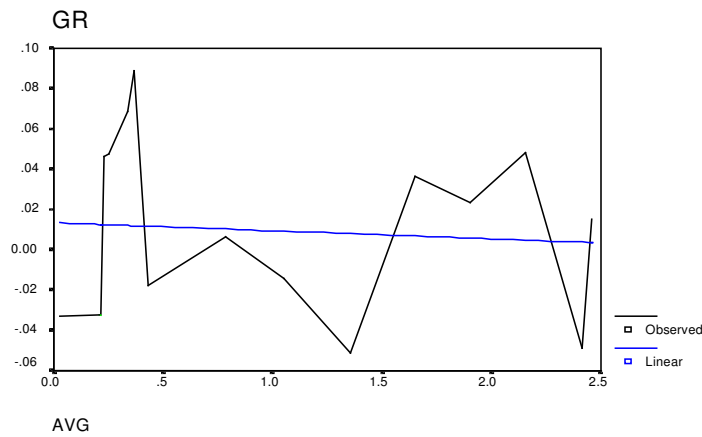
a = 16 major States of India

Fig 4: Growth (Beta) Convergence Among States With Respect To Percentage Of State Revenue Expenditure Devolved To The Local Bodies

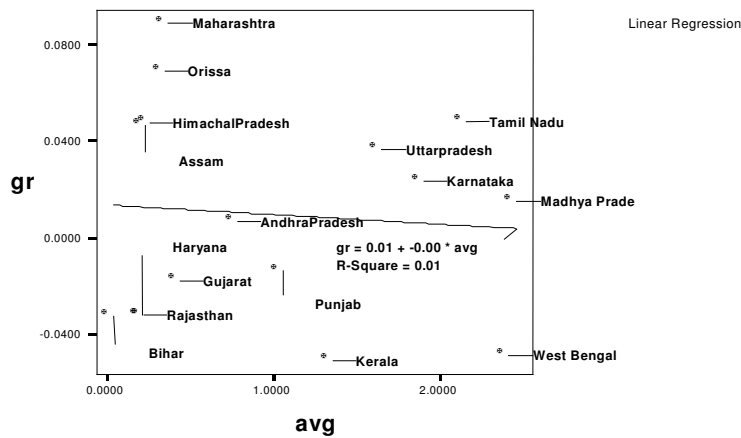
Dependent	Mth	Rsqr	d.f.	F	Sigf	b0	b1
GR	LIN	.006	14	.09	.770	.0135	-.0040*

* Significant at 1 % level

Slope coefficient is negative implying Beta Convergence



Interactive Graph



Source: As in Table 6

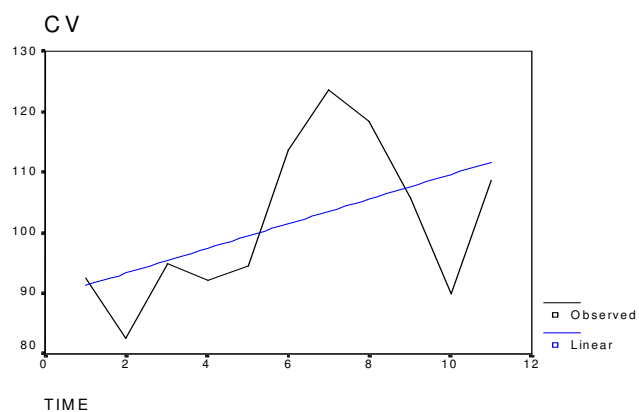
FIG: 5. Dispersion (Sigma) Divergence Among States With Respect To Percentage Of State Revenue Expenditure Devolved To The Local Bodies

Adjusted R Square .18062
Standard Error 11.94060

Variable	B	SE B	Beta	T	Sig	T
TIME	2.037982	1.138491	.512405	1.790	.1071	*
(Constant)	89.280473	7.721624		11.562	.0000	*

* Significant at 1 % level

Time coefficient is positive implying Sigma Divergence



Source: As in Table 6

Table 7: Average Devolution to Local Bodies as percentage to total Revenue Expenditure of the State: 16 Major States in India

State	Avg. Rank Score of Period 1	RANK 1	Avg. Rank Score of Period 2	RANK 2	Avg. Rank Score for the entire period	GRAND RANK
Andhra Pradesh	7.75	8	7.71	8	7.73	7
Assam	12	12	14.14	15	13.36	13
Bihar	16	16	15.57	16	15.73	16
Gujarat	10	9	11.57	12	11.00	11
Haryana	13.75	14	13.57	13	13.64	14
Himachal Pradesh	12.5	13	11.29	11	11.73	12
Karnataka	3.5	3	3.43	4	3.45	3
Kerala	6.25	6	8.71	10	7.82	8
Madhya Pradesh	2.25	2	2.71	2	2.55	2
Maharashtra	10.5	10	7.29	6	8.45	9
Orissa	11.5	11	8.57	9	9.64	10
Punjab	7	7	7.57	7	7.36	6
Rajasthan	13.75	14	13.71	14	13.73	15
Tamil Nadu	3.5	3	1.14	1	2.00	1
Uttar Pradesh	4.25	5	3.00	3	3.45	3
West Bengal	1.5	1	6.00	5	4.36	5

Source: As in Table 6

Note: Period 1 = 1992-93 to 1995-96

Period 2 = 1996-97 to 2002-03

Entire Period = 1992-93 to 2002-03

Table 8: Ranks of the States according to Average Rank Scores on Devolution to Local Bodies as percentage of Total Revenue Expenditure of the State: 16 Major States of India.

State	Average Period 1	Average Period 2	Average Entire Period
Andhra Pradesh	0.81	0.85	0.84
Assam	0.26	0.14	0.18
Bihar	0.03	0.02	0.02
Gujarat	0.43	0.35	0.38
Haryana	0.23	0.12	0.16
Himachal Pradesh	0.26	0.50	0.41
Karnataka	1.90	2.69	2.41
Kerala	1.27	0.86	1.01
Madhya Pradesh	2.36	3.06	2.80
Maharashtra	0.36	1.28	0.94
Orissa	0.35	0.85	0.67
Punjab	1.08	0.86	0.94
Rajasthan	0.22	0.15	0.17
Tamil Nadu	2.06	4.66	3.71
Uttar Pradesh	1.68	2.89	2.45
WestBengal	2.59	1.35	1.80
ALL STATES	1.16	1.66	1.48

Source: Compiled from Table 6

Note: Grand Rank = Rank according to the Average Rank Score for the Entire Period.

Period 1 = 1992-93 to 1995-96

Period 2 = 1996-97 to 2002-03

Table 9: Rank according to Coefficient of variation and Average Rank Scores of Revenue Expenditure devolved to Local Bodies as percentage of Total Revenue Expenditure of the State: 16 Major States of India.

State	ARE 1	C.V 1	Rank 1	ARE 2	CV 2	Rank 2	ARE	CV	Rank
Andhra Pradesh	8	7.02	2	8	19.87	10	7	16.28	1
Assam	12	23.58	10	15	38.56	12	13	44.89	10
Bihar	16	24.29	11	16	19.94	15	16	40.28	8
Gujarat	9	9.63	3	12	29.35	4	11	24.40	4
Haryana	14	73.31	16	13	106.32	6	14	90.94	16
Himachal Pradesh	13	19.15	8	11	47.28	14	12	53.34	13
Karnataka	3	19.85	9	4	15.41	2	3	23.00	3
Kerala	6	10.01	4	10	61.91	9	8	46.18	11
Madhya Pradesh	2	15.60	7	2	16.60	1	2	20.19	2
Maharashtra	10	29.83	13	6	53.74	13	9	75.18	14
Orissa	11	55.62	15	9	75.06	5	10	84.55	15
Punjab	7	24.61	12	7	28.86	8	6	28.16	5
Rajasthan	14	6.93	1	14	56.26	3	15	42.60	9
Tamil Nadu	3	45.60	14	1	27.90	7	1	46.66	12
Uttar Pradesh	5	10.18	5	3	22.40	16	3	32.53	6
WestBengal	1	13.70	6	5	23.29	11	5	38.80	7
ALL STATES	X	10.75	X	X	13.82	X	X	21.46	X

Source: As in Table 8

Note: ARE 1 = Average Rank Score according to Devolved Revenue Expenditure for Period 1

ARE 2 = Average Rank Score according to Devolved Revenue Expenditure for Period 2

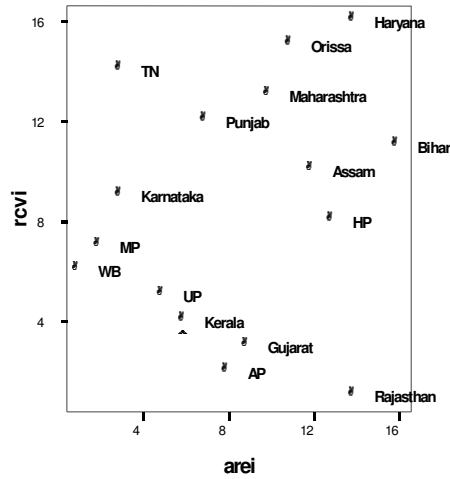
ARE = Average Rank Score according to Devolved Revenue Expenditure for the Entire Period

CV1= Coefficient of variation for Period 1

CV2= Coefficient of variation for Period 2

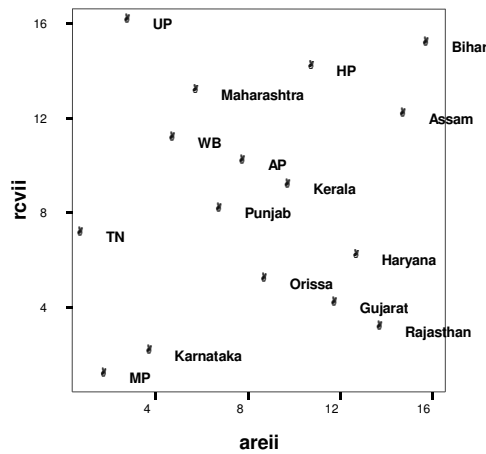
CV = Coefficient of variation for the Entire Period

Figure 6: Dispersion of the Ranks of the States according to Share of Devolution to Local Bodies and its Coefficient of variation (1992-93 to 1995-96)



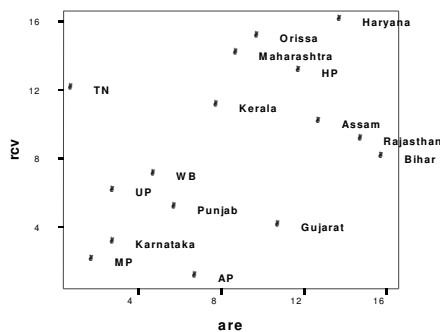
Note: As in Figure 1

Figure 7: Dispersion of the Ranks of the States according to Share of Devolution to Local Bodies and its Coefficient of variation (1996-97 to 2002-03)



Note: As in Figure 2

Figure 8: Dispersion of the Ranks of the States according to Share of Devolution to Local Bodies and its Coefficient of variation (1992-93 to 2002-03)



Note: As in Figure 3.

Table A. 1: Percentage Distribution of the Share of States in Allocation for Panchayats and Urban Local Bodies.

States	Panchayats	ULBs
Andhra Pradesh	9.503	8.233
Arunachal Pradesh	0.348	0.034
Assam	2.918	1.077
Bihar	9.813	4.695
Goa	0.116	0.232
Gujarat	4.351	6.626
Haryana	1.839	1.832
Himachal Pradesh	0.821	0.195
Jammu & Kashmir	0.93	0.783
Karnataka	4.926	6.241
Kerala	4.12	3.762
Madhya Pradesh	8.943	7.801
Maharashtra	8.209	15.813
Manipur	0.235	0.22
Meghalaya	0.32	0.135
Mizoram	0.098	0.192
Nagaland	0.161	0.089
Orissa	4.32	1.998
Punjab	1.933	2.736
Rajasthan	6.137	4.971
Sikkim	0.066	0.01
Tamil Nadu	5.826	9.668
Tripura	0.356	0.201
Uttar Pradesh	16.489	12.582
West Bengal	7.222	9.874
Total	100	100

Source: *The Eleventh Finance Commission for (2000-05)*

Note: ULB = Urban Local Bodies.

Table A.2: Financial Autonomy Ratio Of Local Bodies, Village Panchayats, Urban Local Bodies

STATES	A	B	C	D	E	F	G	H	I
Andhra Pradesh	0.86	1.09	126.6	26.31	40.45	153.74	0.38	0.83	217.93
Bihar*	NA	NA	NA	NA	NA	NA	NA	NA	NA
Goa	46.46	46.46	95.68	46.66	51.91	111.25	46.39	41.13	88.65
Gujarat	22.21	26.42	118.98	63.06	53.45	84.76	78.76	85.21	108.2
Haryana	33.34	32.01	96.01	50.46	38.79	76.87	28.9	30.23	104.61
Karnataka	6.15	4.65	75.55	15.93	12.37	77.66	46.2	36.42	78.83
Kerala	43.83	21.24	48.46	28.51	22.49	78.89	62.05	41.8	67.37
Madhya Pradesh*	21.89	7.49	34.22	4.71	3.84	81.5	40.03	23.85	59.58
Maharashtra	19.21	3.34	17.39	15.96	19.63	122.97	23.34	3.38	14.48
Orissa	19.73	11.85	60.03	6.81	4.8	70.44	57.09	61.76	108.18
Punjab	64.08	88.66	138.37	23.73	37.23	156.89	89.38	113	126.45
Rajasthan	19.46	20.28	104.21	4.35	1.64	37.61	74.35	77.75	104.57
Tamil Nadu	31.27	39.76	127.14	10.02	10.84	108.2	41.91	52.62	125.56
Uttar Pradesh*	15.98	14.47	90.55	0.9	0.51	57.35	27.59	28.44	103.11
West Bengal	9.76	68.5	701.75	3.19	4.11	128.9	17.96	163.1	907.94
Total	11.41	4.81	42.11	10.61	10.6	99.9	14.35	5.02	35.01

Source: Oommen (2000)

Note: A = Financial Autonomy Ratio of LBs 92-93, B= Financial Autonomy Ratio of LBs 97-98, C = Improvement Index*,
D = Financial Autonomy Ratio of VPs 92-93, E = Financial Autonomy Ratio of VPs 97-98, F = Improvement Index,
G = Financial Autonomy Ratio of ULBs 92-93, H = Financial Autonomy Ratio of ULBs 97-98, I = Improvement Index *
LB = Local Bodies (PRIs + ULBs), PRI = Panchayati Raj Institutions,
ULB = Urban Local Bodies,
VP = Village Panchayats

Financial Autonomy Ratio = (Locally raised Revenue / Total Revenue Expenditure)*100

Notes

¹ For a detailed discussion on political advantages of decentralization, see Wolman (1990)

² In this context, one may refer to the innovative exercises which were taken up by Calcutta Municipal Corporation in developing a solid waste management technique by utilizing the wetlands in the eastern part of the city. Such a device has created much positive externality, as evidenced by the economy of the East Calcutta wetlands.

³ Any organization faces a core difficulty in keeping its members informed of each other's activities. As the number of members rises arithmetically, the number of potential nodes for information exchange rises accordingly. The number of nodes in a centralized delivery system

is likely to be higher and consequently there might develop inefficiency in maintaining the informational network in a centralized delivery system. (*Helm and Smith, 1987*)

⁴ For a review of literature on fiscal decentralization, see Ísa Saðbaþ *Fiscal Decentralization in Theory*. As Saðbaþ observes: ‘decentralization has political and administrative advantages. It is also argued that allocative efficiency is maximized under highly decentralized political structures. However, it has disadvantages. The main potential disadvantages of decentralization are that it can work against the internalization of externalities and equalization through centrally provided mechanisms’ (Ísa Saðbaþ, *Fiscal Decentralization in Theory*; downloaded pdf file).

⁵ Following the Amendment Acts, which came into force in 1993, the Provincial governments in India had introduced the Conformatory Acts to incorporate the provisions of the Constitutional Amendment Acts in the functioning of the State governments with a third tier, i.e., the Local Bodies. There are State specific variations in the Conformatory Acts (see, UNDP (n.d.), New Delhi, India). But then, by April 1994, all the State Legislative Assemblies have compiled the constitutional mandate by adopting Conformatory Acts.

⁶ *Constitution of India*, Section 280.

⁷ For a critique of the Constitutional Amendment Acts (73rd and 74th) see Srinivasan, T.N. (2002). The prevailing option however, is that the Local Bodies do constitute a tier of the government see, Indira Rajaraman, *et al.* (*Economic and Political Weekly*, Vol. XXI, No.8) also Rajaraman (2003)

⁸ Amendment 280 (c) states that such measures are to be taken to ‘supplement the resources of the Municipalities’ as well.

⁹ An Ad hoc provision of Rs.100 per person as given in 1971 Census, for each state over a four year period. It has rightly been pointed out that the allocation for the Local Bodies as decided by the Tenth Finance Commission did not follow a norm that could ascertain equity in allocation of resources. However, one may point out that the Tenth Finance Commission did not have the opportunity to develop such a norm after consulting the reports of the State Finance Commissions, most of which were yet to be submitted. In fact, the conformatory State acts were passed only by April, 1994. As a result, the Commission had to comply the Constitutional mandate by making a recommendation only on an ad hoc basis.

¹⁰ See, Bandyopadhyay, D. (2003) for a fair review of the performance of the EFC.

¹¹ The index carried a 20 per cent weight in the formula used for determining state shares of the annual provision. In addition, the formula carried a weight of 10 per cent for own revenue collections at the local level, normalized (with equal weights) for state SDP from agriculture, as (perfectly justifiable) measures of revenue potential. See, Rajaraman (2004).

¹² See, Oommen (2000)

¹³ The background paper for rural bodies was prepared by The National Institute of Rural Development (NIRD). The study on Urban Local Bodies was done by National Institute of Public Finance and Policy (NIPFP). However, the quality of the basic data in both the studies remained open to criticism.

¹⁴ Ooman (2000), Rajaraman (2000).

¹⁵ One should, however, admit that the subsequent SFCs which should get the benefit of EFC recommendations for building a reliable data base are yet to meet this expectation. The progress with respect to second SFC reports is rather poor. Thus, as Rajaraman observes: only seven SFC-II reports are available in the public domain, of which one (Himachal Pradesh) has issued only the urban volume so far, and the other (Uttaranchal) is a new state without any prior point of comparison. In the remaining five, the own revenue information provided is

uneven and of uncertain provenance. Some just report projected revenue as supplied to the Eleventh Finance Commission (Rajaraman, 2004)

¹⁶ Inter governmental transfers to the Local Bodies are often tied in nature; the Local Bodies hardly have any option in utilizing these funds.

¹⁷ Oommen, M.A. (2000)

¹⁸ Quantitative analysis on the basis of the data of the Eleventh Finance Commission has the limitation that the latest year that could be covered in such analysis is 1997-98.

¹⁹ Oommen (2000), see also Rajaraman (2004).

²⁰ The internal revenue mobilization constituted only 4.17 per cent of the total of the Panchayats at all levels in 23 States during 1990-91 to 1997-98. In a few States like Bihar, Rajasthan, Manipur and Sikkim internal revenue mobilization for the period was totally absent.

²¹ Again, the minimum and maximum rates of such taxes are prescribed by the States, restricting the freedom of the Local Bodies to levy such taxes.

²² Rajaraman (2004). The state-wise performance, as given in Rajaraman (2003), Table 2.2 indicates that the performance was the best in Kerala where per capita own revenue collection by the PRI had been Rs.43.27. Among the worst performing states, there are Orissa, Madhya Pradesh, Assam and Tripura. Bihar, which is a major state in India did not collect anything as Panchayat's own revenue.

²³ This fund is devolved through the respective State governments

²⁴ At the time the Eleventh Finance Commission was submitting its report, Bihar, Goa, Gujarat and Haryana had been the four major States in which the report of the SFC 1 had not even been submitted.

²⁵ See, UNDP (n.d.), p.15

²⁶ In order to make the RBI data comparable over a period of eleven years, where the nominal values would be different from the real values we normalize the data on revenue expenditure by the Local Bodies with the wholesale price index as the deflator; the index had 1993-94 as the base year. The revenue expenditure as Compensation and Assignments to Local Bodies are thus captured in terms of constant price. The per capita Compensation and Assignments are then calculated for each state for each year by utilizing State population data for various years. The State population for each year (except 2001-02) was taken on the basis of the estimated growth rate of population between 1991 and 2001. For 2001-02, the census population data has been used.

²⁷ This includes all the Non-Special Category States excluding Delhi and Goa; Chattisgarh, Jharkhand and Uttaranchal have been combined with Madhya Pradesh, Bihar and Uttar Pradesh respectively. From the Special Category States, Assam has been included in this study.

²⁸ At current prices the average per capita total revenue expenditure for the States under study had been Rs.2040.63 per year, for the period 1992-93 to 2002-03. The average per capita transfer in current prices to the Local Bodies, on the other hand, had been only Rs.36.75 per year (Table 2).

²⁹ The results of the regression analysis indicate that the null hypothesis of no trend break in 1996-97 is rejected at 1% level. All the b-coefficients had been positive in the estimated line of regression.

³⁰ The case of Kerala should be viewed differently. In case of Kerala, the tax base for the PRI has widened in post Conformatory Act regime. The per capita tax collection by the Local

Bodies is the highest (Rs.43.27) in Kerala. Since the tax base has been widened, the need for devolution from the Consolidated Fund of the State might have declined there.

³¹ For average devolution the rank scores follow descending order (thus, the highest numerical value gets rank 1) and for coefficient of variation the rank score follows ascending order (the lowest numerical value is ranked 1, implying that the best has the least variation in per capita Assignment).

³² Although the percentage of State budget devolved to the Local Bodies declined sharply in case of Kerala, Kerala should still be considered as a better performer, a fact which is not reflected in these data (see Footnote 30).

³³ In case of Rajasthan the volatility was the least. But then Rajasthan is the State where the revenue expenditure of the local governments as percentage of revenue expenditure of the State was very poor. The lack of volatility was due to the fact that Rajasthan was maintaining a low level stability during the entire period, as Bihar was doing in terms of per capita devolution.

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