

# Finance Commission Grants: Quantum and Utilisation

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**Manish Gupta**

National Institute of Public Finance and Policy, New Delhi

# Introduction

- ❖ As per Article 280(3) of the Constitution of India one of the Terms of Reference (ToR) of a Finance Commission is to make recommendations as to the “principles governing the grants-in-aid of revenues of the states out of the Consolidated Fund of India”
- ❖ There exists considerable heterogeneity among states in terms of their size, population, per capita incomes, etc. Also the gap between capacity to collect revenue and expenditure needs varies across states depending upon initial endowments, historical backgrounds, and the levels of development. This gives rise to a horizontal imbalance.
- ❖ Finance Commissions have addressed horizontal imbalance across states through the distribution of shareable central taxes using a number of criteria.
- ❖ Additionally, Finance Commissions have also addressed horizontal imbalances across states by recommending grants-in-aid of revenues from the consolidated fund of India.
- ❖ Under Article 275 of the Constitution, Finance Commissions are mandated to recommend the principles and the quantum of grants-in-aid to States that are in need of assistance and that the Commission can recommend different sums for different States.

# Evolution of Finance Commission Grants

- ❖ Examination of FC reports reveal that the grants recommended by them are predominantly in the nature of general purpose grants meeting the difference between the assessed expenditure on non-plan revenue account of each state and projected revenues including state's share in central taxes. These are referred to as '*gap filling grants*' (Rao 2010; Srivastava & Rao 2009; Vithal & Sastry 2001).
- ❖ Up to FC-V, grants were recommended for meeting the post-devolution non-plan revenue deficits of states with a few exceptions
- ❖ From FC-VI, there was a change in the ToR and FC was asked to consider requirements of states which were backward in standards of general administration so as to bring them to the levels of more advanced states.
- ❖ FC-VII, FC-VIII & FC-X were asked to consider upgradation of standards in non-developmental sectors
  - Recommended grants for meeting revenue expenditure deficiencies of certain states in general administration, administration of justice, jails, police, primary education, medical & public health, welfare of SCs/STs & OBCs, administration of taxes, and for sectors like education and health
  - Essentially to enable states to meet deficiencies in basic service provisioning

# Evolution of Finance Commission Grants

- ❖ Over the years, the scope of grants to States was extended further to cover special problems – FC-VIII to FC-XIII recommended grants for addressing special problem of states
- ❖ FC-XII extended the scope of grants to achieve partial equalization of expenditure across states in education & health sectors; recommended grants for maintenance of roads, bridges & public buildings, maintenance of forests and heritage conservation.
- ❖ FC-XIII gave grants for improving outcomes, protection of forests and incentive grants for grid-connected renewable energy and water sector. It also recommended grants for elementary education.
- ❖ Following 73<sup>rd</sup> & 74<sup>th</sup> amendments, FCs were charged with additional responsibility of recommending measures to augment Consolidated Fund of a State to supplement resources of local bodies. Grants to local bodies were prescribed by FC since the FC-X – further expanded the scope of grants
- ❖ Grants recommended by FCs can be broadly classified into five broad categories:
  - (a) deficit grants,
  - (b) grants for local governments,
  - (c) grants for disaster management,
  - (d) sector-specific grants and
  - (e) grants for state-specific needs

# Finance Commissions' Views/Approach to Grants

- ❖ **FC-XI** - dominance of tax devolution weakens equalising capacity of FC transfers, even though successive FCs have tried to redress this shortcoming by introducing redistributive elements in the formula
- ❖ **FC-XII** - grants have unique characteristics, as they could take better account of cost disabilities and redistributive considerations that were not adequately captured in the tax devolution formula
- ❖ **FC-XIII** - grants are an important instrument of financing that enabled more comprehensive transfers and allowed the Commission to make corrections for cost disabilities faced by many states.
- ❖ **FC-XV** - grants can make corrections for cost disabilities and other redistributive requirements not fully addressed through devolution formula. Grants are more directly targeted and used to equalise the standards of basic social services.
- ❖ **FC-XIV** – did not recommend any sector or state specific grants; felt that such grants are not necessary
  - sector specific grants constitute a small percent of total grants to states in a particular sector
  - although such grants covered large number of sectors, there was discontinuity in sectors recommended for grants by past FCs with a few sectors like health & education being considered on regular basis
  - Issue of duplication and overlap on account of grants flowing through multiple channels
  - Limited tenure of FC also adds to the constraints in designing the grants

Grants Recommended  
by Recent Finance  
Commissions

Grants	FC-XII (2005-10)	FC-XIII (2010-15)	FC-XIV (2015-20)	FC-XV-1 (2020-21)	FC-XV-2 (2021-26)
NPRD/RD	yes	yes	Yes	yes	yes
Local Bodies	yes	yes	Yes	yes	yes
Calamity/Disaster Management	yes	yes	Yes	yes	yes
State Specific Needs	yes	yes	×	yes	yes
Health Sector/Nutrition	yes	×	×	yes	yes
Education Sector	yes	yes	×	×	yes
Maintenance of Roads & Bridges	yes	yes	×	×	yes
Maintenance of Buildings	yes	×	×	×	×
Heritage Conservation	yes	×	×	×	×
Performance Incentive	×	yes	×	×	×
Maintenance of Forests	yes	yes	×	×	×
Renewable energy	×	yes	×	×	×
Water Sector Management	×	yes	×	×	×
Reduction in IMR	×	yes	×	×	×
Improvement in Justice Delivery	×	yes	×	×	yes
Incentive for issuing UIDs	×	yes	×	×	×
District Innovation Fund	×	yes	×	×	×
Improvement of Statistical Systems	×	yes	×	×	yes
Employee & Pension Database	×	yes	×	×	×
GST Compensation	×	Yes	×	×	×
Agriculture	×	×	×	×	yes
Grant for aspirational district & block	×	×	×	×	yes
Number of Grants	10	17	3	5	11

# Quantum of Finance Commission Grants

## Composition of Finance Commissions Transfers (%)

Finance Commission (award period)	Tax Devolution	Grants-in- aid	Total
FC-III (1962-66)	77.13	22.87	100.00
FC-IV (1966-69)	72.66	27.34	100.00
FC-V (1969-74)	85.12	14.88	100.00
FC-VI (1974-79)	74.58	25.42	100.00
FC-VII (1979-84)	91.96	8.04	100.00
FC-VIII (1984-89)	88.95	11.05	100.00
FC-IX (1989-95)	86.20	13.80	100.00
FC-X (1995-2000)	90.12	9.88	100.00
FC-XI (2000-05)	84.16	15.84	100.00
FC-XII (2005-10)	83.67	16.33	100.00
FC-XIII (2010-15)	85.83	14.17	100.00
FC-XIV (2015-20)	88.03	11.97	100.00
FC-XV-1 (2020-21)	80.96	19.04	100.00
FC-XV-2 (2021-26)	80.35	19.65	100.00

Source: Gupta and Sarma (2022); Report of FC-XV

- ❖ Though the scope, coverage & number of FC grants have increased over the years, their share in total transfers recommended by FCs have remained small
- ❖ Tax devolution accounts for a sizeable portion of total FC transfers.

# Quantum of Finance Commission Grants

## Share of Different Grants in Total FC Grants (%)

Grants	FC-XII (2005-10)	FC-XIII (2010-15)	FC-XIV (2015-20)	FC-XV-1 (2020-21)	FC-XV-2 (2021-26)
<b>1</b> NPRD/RD grant	39.9	16.3	36.3	35.8	28.5
<b>2</b> Local bodies	17.5	27.5	53.4	43.3	42.2
<b>3</b> Calamity relief/disaster management	11.2	8.3	10.3	13.9	11.9
<b>4</b> GST compensation	--	15.7	--	--	--
<b>5</b> State specific needs	5.0	8.8	--	3.3	4.8
<b>6</b> Sector specific grant	26.4	23.4	--	3.7	12.6
a) Health sector	4.1	1.6	--	3.7	3.1
b) Education sector	7.1	7.6	--	--	1.1
c) Environment	0.7	4.8	--	--	0.0
d) Agriculture	--	--	--	--	4.4
e) Other sectors	14.5	9.4	--	--	4.0
<b>7 All Grants</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>

Note: RD: Revenue deficit; NPRD: Non-plan revenue deficit

Source: FC reports; Gupta et al (2024)

- ❖ Since FC-XIII, local body grants have been the largest of all FC grants
- ❖ 3 grants - Deficit (non-plan revenue deficit /revenue deficit) grant, local body grants and disaster management grants account for most of the grants
- ❖ Share of sector specific and state specific grants is low



# Quantum of Finance Commission Grants

FC Sector Grants as Percent of States' Sectoral Revenue and Total Expenditure

Sectors	FC-XII (2005-10)		FC-XIII (2010-15)		FC-XV (2020-21)		FC-XV (2021-26)	
	% of Rev exp	% of Total exp	% of Rev exp	% of Total exp	% of Rev exp	% of Total exp	% of Rev exp	% of Total exp
Health/nutrition/ Reduction in IMR	4.35	3.90	1.62	1.46	4.38	4.00	4.46	3.85
Education sector	1.88	1.83	1.94	1.89			0.58	0.55
Agriculture							6.21	5.66

Source: FC reports, various years. Union government budget documents, various years; Gupta et al (2024)

- ❖ Share of FC sector specific grants as a percentage of states' revenue and total expenditure on respective sectors is very small

# Utilisation of Finance Commission Grants

## Utilisation of Select Finance Commission Grants (%)

FC Grant	FC-XII (2005-10)	FC-XIII (2010-15)	FC-XIV (2015-20)	FC-XV (2020-26)
Forest	93.4	88.6		
Water sector		28.3		
Grants for Rural Local Bodies	94.6	89.4	91.5	96.5
Elementary Education		92.1		
Health/ Improving IMR		100.0		44.8

Note: Utilisation is the ratio of releases to allocations

Source: FC Reports; Ministry of Finance, Ministry of Environment, Forest and Climate Change; Rajya Sabha Question; Ministry of Panchayati Raj

- ❖ Utilisation is the ratio of expenditure to allocations
- ❖ As data on expenditures is not easily available we have considered releases as a proxy for it
- ❖ State-wise data on releases of all FC grants is not easily/readily available
- ❖ Only those FC grants for which for which state-wise releases data were available have been considered

# Utilisation of Rural Local Body Grants

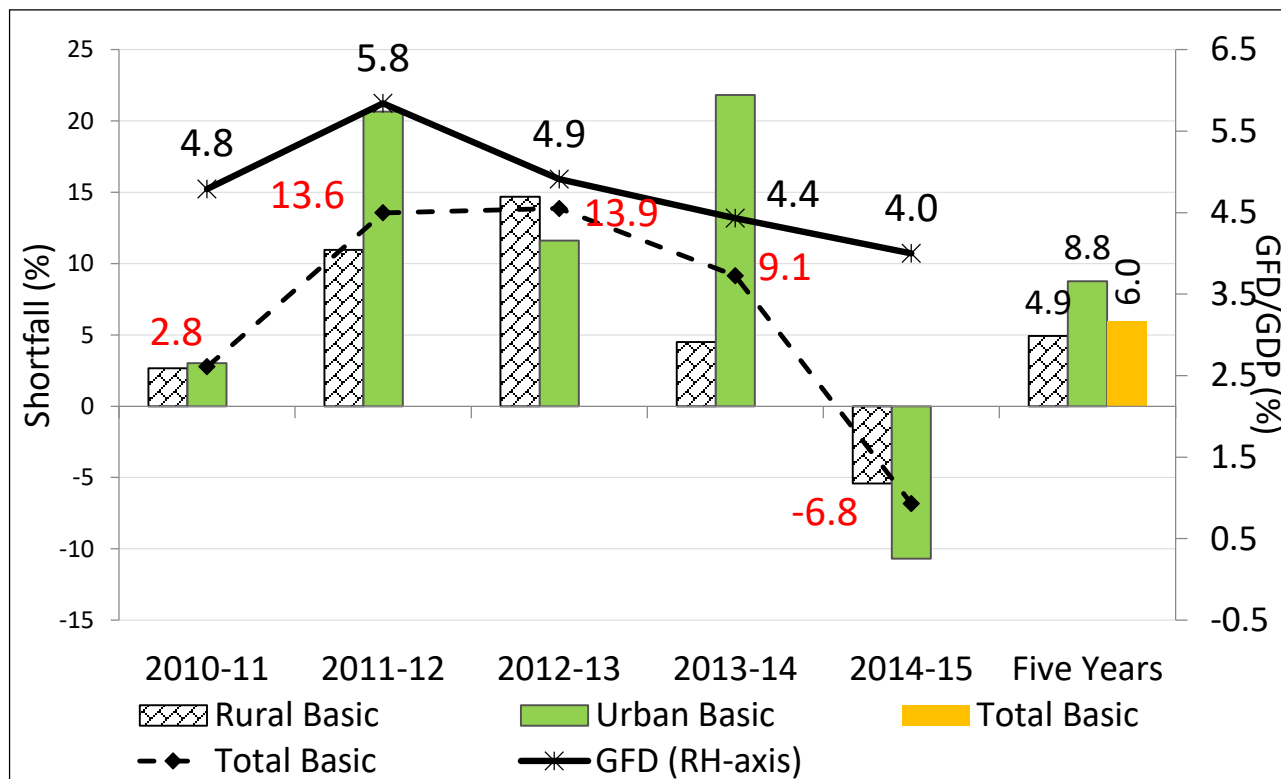
## Grants for Rural Local Bodies: Conditionalities and Utilisation

Finance Commission	RLB Grant	Utilisation (%)	Conditionalities
FC-XII	RLB Grant	94.63	No conditionality
FC-XIII	Basic Grant	95.07	1/3rd conditional
	Performance Grant	79.30	
	Total Grant	89.63	
FC-XIV	Basic Grant	98.44	10% for Gram Panchayats & 20% for urban LBs conditional
	Performance Grant	27.02	
	Total Grant	91.49	
FC-XV	RLB Grant	96.54	2020-21: 50% tied (65.78% for ULBs) 2021-26: 60% tied (72.62% for ULBs)

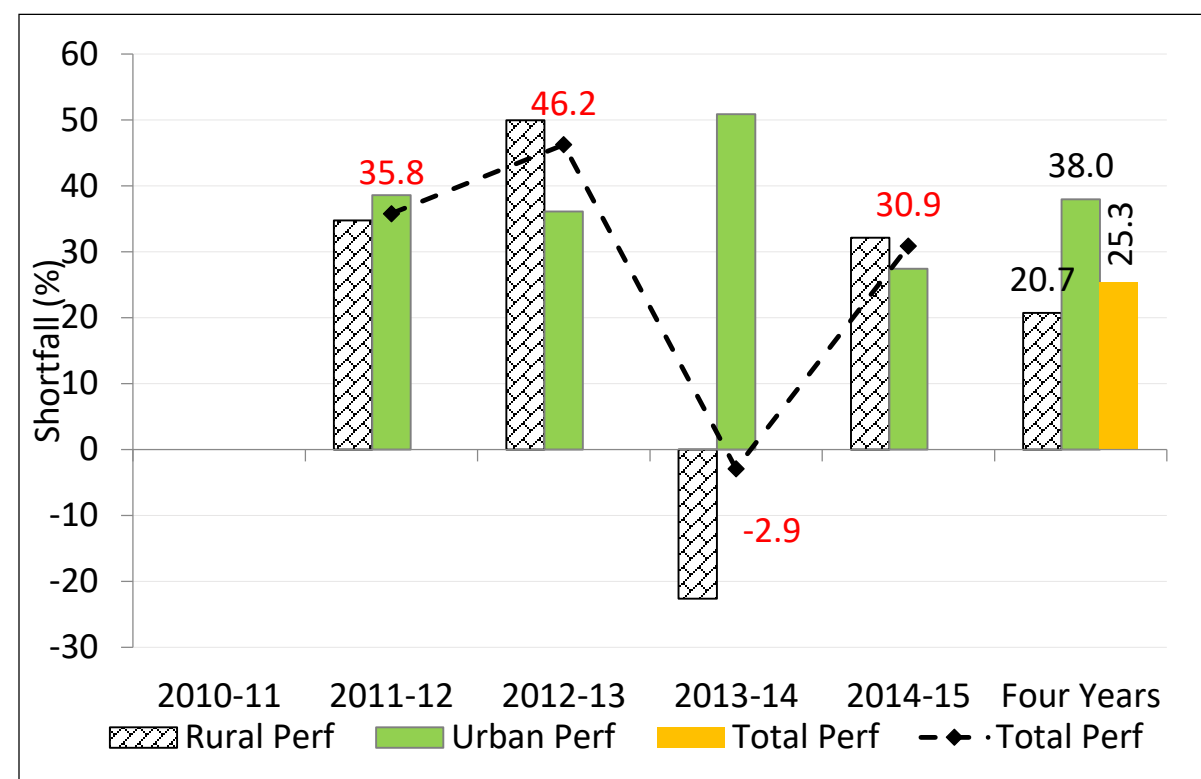
- ❖ FC-XIII divided its local body grant into two-parts (i) condition-free basic grant, and (ii) conditional performance grant
  - Basic grant's share was roughly two-thirds of total local grant; performance grant's share was one-third
- ❖ FC-XIV retained the two-part structure of FC-XIII - basic unconditional component (90% for Gram Panchayats)
- ❖ FC-XV local body grant had a tied component of 50% in its first report; increased 60% in the final report
- ❖ For FC-XIII & FC-XIV, utilisation percentage is lower for performance grants which are conditional.
- ❖ In some of the states, especially north-eastern states overall utilisation rates are very low across the four FCs

# Utilisation of Rural Local Body Grants (FC-XIII case study)

Shortfall of Receipts Against Allocations, Basic Local Grant, 2010-15



Shortfall of Receipts Against Allocations, Performance Grant, 2010-15



- ❖ The shortfall in total basic grant summing across rural and urban basic peaked in 2011–12 and 2012–13.
- ❖ A consolidated shortfall of 6%, implying 94% disbursement of allocations may not seem high enough to matter
- ❖ What is troubling is the yearly variation rather than the level of the shortfall by itself – shortfall was highest in years when the fiscal stress was highest at the centre
- ❖ For performance grants highest aggregate shortfalls observed in the stressed years 2011–12 & 2012–13, going up again in the last year, 2014–15.

# Utilisation of Rural Local Body Grants

		FC-XII		FC-XIII		FC-XIV		FC-XV	
		RLB Grant	Basic Grant	Performance Grant	Total Grant	Basic Grant	Performance Grant	Total Grant	RLB Grant
1	Andhra Pradesh	100.00	82.09	99.80	88.06	99.69	39.93	93.88	98.98
2	Arunachal Pradesh	40.00	51.68	6.97	36.24	99.91	17.35	91.88	41.74
3	Assam	70.00	100.00	64.13	87.62	100.00	40.19	94.18	100.00
4	Bihar	100.00	100.00	97.66	99.19	98.04	15.36	90.00	99.81
5	Chhattisgarh	100.00	100.00	84.64	94.70	100.00	40.19	94.18	100.00
6	Goa	44.28	13.88	6.87	11.46	100.00	40.21	94.18	53.06
7	Gujarat	100.00	100.00	21.24	72.80	100.00	40.19	94.18	100.00
8	Haryana	100.00	100.00	98.36	99.43	100.00	40.19	94.18	90.03
9	Himachal Pradesh	100.00	100.00	98.33	99.42	100.00	17.38	91.96	84.83
10	J&K	18.81	86.12	21.26	63.72	57.90	14.08	53.64	--
11	Jharkhand	0.00	100.00	68.89	89.26	100.00	17.38	91.96	88.20
12	Karnataka	100.00	100.00	97.63	99.18	98.88	39.70	93.12	92.66
13	Kerala	100.00	100.00	98.38	99.44	100.00	37.74	93.94	100.00
14	Madhya Pradesh	100.00	86.31	97.63	90.22	100.00	39.87	94.15	97.98
15	Maharashtra	100.00	100.00	97.64	99.18	100.00	17.38	91.96	90.35
16	Manipur	46.00	99.99	54.83	84.40	100.00	40.18	94.18	41.81
17	Meghalaya	80.00	51.68	7.10	36.29	--	--	--	37.21
18	Mizoram	80.00	51.69	26.73	43.07	--	--	--	57.77
19	Nagaland	100.00	22.78	6.99	17.33	--	--	--	52.93
20	Odisha	100.00	100.00	7.05	67.90	100.00	40.19	94.18	100.00
21	Punjab	80.00	100.00	54.71	84.36	100.00	17.38	91.96	86.97
22	Rajasthan	100.00	100.00	98.40	99.45	100.00	40.19	94.18	98.46
23	Sikkim	90.00	87.38	21.19	64.53	100.01	40.21	94.19	92.86
24	Tamil Nadu	100.00	100.00	21.24	72.80	93.07	17.38	85.71	100.00
25	Telangana	--	143.62	128.28	137.40	99.95	40.19	94.13	99.90
26	Tripura	70.00	74.77	54.82	67.88	100.00	40.18	94.18	92.92
27	Uttar Pradesh	100.00	100.00	97.64	99.18	99.93	17.33	91.89	100.00
28	Uttarakhand	80.00	100.00	7.06	67.91	100.00	29.16	93.11	92.50
29	West Bengal	100.00	74.77	69.60	72.98	96.57	16.80	88.81	99.80
All States		94.63	95.07	79.30	89.63	98.44	27.02	91.49	96.54

# Utilisation of FC Grants

State	FC-XII )	FC-XIII
Andhra Pradesh	100.00	94.72
Arunachal Pradesh	100.00	81.25
Assam	100.00	43.75
Bihar	100.00	55.00
Chhattisgarh	100.00	100.00
Goa	100.00	50.00
Gujarat	100.00	100.00
Haryana	100.00	100.00
Himachal Pradesh	100.00	100.00
Jammu & Kashmir	90.00	58.00
Jharkhand	80.00	100.00
Karnataka	100.00	100.00
Kerala	99.00	91.69
Madhya Pradesh	100.00	100.00
Maharashtra	60.00	100.00
Manipur	100.00	100.00
Meghalaya	70.45	62.50
Mizoram	91.32	86.50
Nagaland	80.00	81.25
Orissa	100.00	93.19
Punjab	80.00	81.25
Rajasthan	80.00	100.00
Sikkim	100.00	93.75
Tamil Nadu	100.00	100.00
Telangana	--	25.00
Tripura	50.00	87.50
Uttar Pradesh	100.00	100.00
Uttarakhand	100.00	81.25
West Bengal	100.00	100.00

Forest  
Grant



States	FC-XV Health grant through local bodies	FC-XIII Grant for Water Management	FC-XIII Elementary Education	FC-XIII Reducing IMR
Andhra Pradesh	64.41	25.00	100.00	100.00
Arunachal Pradesh	30.88	0.03	16.67	100.00
Assam	31.37	25.00	75.21	100.00
Bihar	31.76	25.00	100.00	100.00
Chhattisgarh	32.24	0.00	100.00	100.00
Goa	32.42	0.00	18.18	100.00
Gujarat	51.05	25.00	100.00	100.00
Haryana	32.23	25.00	100.00	100.00
Himachal Pradesh	32.24	25.00	100.00	100.00
J&K	--	0.00	56.79	100.00
Jharkhand	32.11	0.00	76.51	100.00
Karnataka	43.25	0.00	100.00	100.00
Kerala	56.49	25.00	100.00	100.00
Madhya Pradesh	63.14	25.00	75.77	100.00
Maharashtra	19.25	100.00	100.00	100.00
Manipur	31.30	0.00	40.00	100.00
Meghalaya	32.23	0.00	76.92	100.00
Mizoram	32.15	25.00	20.00	100.00
Nagaland	32.21	50.00	57.14	100.00
Odisha	64.38	25.00	57.09	100.00
Punjab	32.10	25.00	61.61	100.00
Rajasthan	32.23	25.00	100.00	100.00
Sikkim	32.28	0.00	40.00	100.00
Tamil Nadu	97.80	25.00	76.57	100.00
Telangana	64.37	--	--	--
Tripura	31.85	25.00	39.13	100.00
Uttar Pradesh	32.22	25.00	100.00	100.00
Uttarakhand	32.28	25.00	100.00	100.00
West Bengal	64.43	25.00	100.00	100.00

# Conclusion

- ❖ Although a large number of grants have been recommended by FCs, they account for a small proportion of total FC transfers; share even smaller in total central transfer
- ❖ Local body grant, deficit grants and grants for disaster account for a sizeable portion of FC grants; share of sector specific and state specific grants small
- ❖ Utilisation of some of the sector specific grants low; utilization even lower in NE&H states
- ❖ States have raised concern about growing tendency of attaching conditions to grants which adversely impact their utilization - stringent conditions attached to grant releases responsible for low utilization
- ❖ In addition to conditions set by FCs, central ministries & department stipulate additional conditions
- ❖ States were of the view that FC should ring-fence its conditions so that no additional conditions can be imposed.
- ❖ Most states felt that conditions, if required, should be minimum, pragmatic and implementable
- ❖ Are states being paid too little money in the form of grants (FC grants) and being asked for too much in the form of performance?