

IV. AGENDA FOR FUTURE RESEARCH

In the foregoing, we have noted the major problems faced in Indian fiscal federalism, highlighted important contributions on the analysis of Indian federal fiscal problems and identified the areas deserving more detailed analysis. In this section, the important issues requiring further research are highlighted.

Any analytical study on Indian fiscal federalism would have to base itself on an appropriate/conceptual framework. This framework would have to recognise and take into account the specific conditions prevailing in the country. Low levels of income, wide inter-regional disparities in the levels of living of the people and the more active State participation in economic activities call for a different analytical framework, where, the scope of the allocation function of the government is much larger in the shape of development planning than in the more developed countries. The incorporation of the planning dimension in a decentralised set up creates additional complications and contradictions and this has to be taken into account in any framework adopted to analyse Indian fiscal federalism.

We have already reviewed a number of studies making assertions on the virtues of decentralisation while criticising the centripetal bias in the functioning of Indian fiscal federalism. However, there have not been any studies attempting to measure the net gains from decentralisation or trying to quantify the net losses on account of centralisation. Mitra's (1987) assertion that centralisation has had adverse effects on economic growth and equity in the Indian federation provides, at best, a working hypothesis for future studies. At the theoretical level, more such working hypotheses have to be formu-

lated. The implications of centralisation and decentralisation under alternative assumptions of the government behaviour would be useful in forging a better understanding of the political economy of Indian federation. At the empirical level, more studies on the trends in centralisation and quantification of the gains from decentralisation would be helpful in any attempt at redesigning the functions. This requires the estimation of scale economies through properly specified cost functions of various public services and the analysis of the diversity in demand conditions and estimation of income and price elasticities of demand for public services.

As mentioned in the earlier sections, there are virtually no worthwhile studies on the economics of State-Local fiscal relations in India. The important aspects that require detailed attention of the researchers are, the evolution of an appropriate analytical framework for the distribution of functions and sources of finance between the two levels of the government, factors inhibiting the autonomous functioning of the local bodies which would enable them to provide public services according to the diversified preference patterns, objective methods of making transfers to local bodies for both general and for specific purposes and their appropriate design, effects of intergovernmental transfers in terms of stimulating or substituting local expenditures, problems arising from the interaction of rural-urban local bodies, issues of tax harmonisation between the State and local areas and evolving an appropriate institutional framework for conducting State-Local relations.

The most important shortcoming in the literature that prevails presently is the lack of a comprehensive analytical framework for designing Central transfers to the States. In future, any study to be usual, would have to consider introducing such a framework. The framework thus evolved would have to include the planning dimension and would have to recognise the various channels of financial flows between the Centre and the States and among the States inter se

through the banking system and the institutional financial agencies. The framework would also have to assign clearly defined roles to the Planning Commission and the Finance Commissions and should have a clear specification of the objective functions of the two institutions. The clearly defined objective functions would then help determine the roles of general purpose and specific purpose transfers on the one hand and grants and tax shares on the other. As we saw, the tax share are now not related to fiscal needs or fiscal disadvantages. One major question to be decided is whether the existing basis should be changed so that all general purpose transfers would be related to fiscal disadvantages. Additionally, there must be found a way to incorporate the planning dimension in the general framework of transfers.

One of the important prerequisites of linking general purpose transfers to fiscal disadvantages of the States is the empirical estimation of the fiscal disadvantage itself. Methods of estimating fiscal capacities, in spite of a number of studies that have been done so far have remained imperfect. Some of the peculiar problems that are faced in the estimation of taxable capacity are, non-uniform allocation of the tax powers to the local bodies in different States, tendency of the States to export the tax burden to the residents of other States and the non-availability of data on tax bases at the required level of disaggregation. Continuous effort would have to be made in improving both the data base and information system as well as the methodology of estimating taxable capacity and effort of the States. On the non-tax revenue front, there are virtually no analytical studies available determining appropriate user charges for various services rendered. Some of the important undertakings such as electricity boards and road transport corporations would have to be subjected to much more detailed analysis before appropriate norms on the rates of return are stipulated. Adopting a uniform norm irrespective of the hydro-thermal mix in the generation of electricity and applying a single

rate of return for road transport corporations without considering the peculiar problems prevailing in different States as has been done by the Finance Commissions is not very scientific. Detailed studies of various taxes in individual States over a time period would also be useful in order to help in understanding the determinants of tax revenues in the States better and could be extremely helpful both in developing an appropriate forecasting method and in the development of norms for the purpose of the Finance Commissions. Detailed periodic studies of individual Central taxes with a view to making judgments about the revenue potential of these taxes and identifying the ways and means to improve revenue productivity would also be needed to determine the extent of Central transfers. Also, the studies estimating revenue potential of tax bases listed under Articles 268 and 269 would be helpful in determining their feasibility.

In contrast to the analysis on fiscal capacity, as mentioned already, there are hardly any studies on estimating expenditure needs and cost disabilities of providing public services in different States. The existing few expenditure determinants' studies suffer from severe limitations of both theoretical and empirical nature. Quantitative analysis of States' expenditures in more rigorous and properly specified models is essential both for designing general purpose and specific purpose transfers and for analysing their effects. Quantification of the units of public services provided and identification of cost factors within and beyond the control of State governments provide extremely useful inputs in designing the transfer schemes which would be effective in fulfilling the intended objectives. Such studies can also be employed to estimate expenditure needs of the States which, along with this revenue capacity can be employed to determine the norm for making general purpose transfers. The estimation of income and price elasticities of different types of transfers is not only helpful in the design of various specific purpose transfers but also would be helpful in

analysing the extent of misallocation caused on account of commanding the States' resources to fulfill the objective of providing a specified level of public services desired by the Central government.

Another important area of study is the States' indebtedness in general and borrowings from the Central government in particular. Some of the important issues that should be covered in such studies are: the magnitude of the burden of States' borrowings; the problem of sustainability and corrective measures required to reduce the burden on the States; the merits of borrowing from the market vis-a-vis from the Central government; the terms and conditions of borrowing from the Centre and their reasonableness; appropriate methods of providing for amortisation; and the issues concerning the externally aided projects, the allocative problems created on account of additionality and its effects on States with different levels of development.

While the issues relating to the relationship between the Centre and the States have evoked considerable attention, there has not been much analysis of the problems arising from the interaction of the States among themselves. The effects of inter-State tax competition to attract capital, the analysis of inter-State tax exportation and estimation of inter-regional incidence of State taxes are all important areas requiring detailed analytical scrutiny.

The above list is by no means comprehensive. These are only the more important areas as we see them. It is our fond hope that the present state of Centre-State relations itself which is by no means harmonious, would give rise to a number of analytical studies with a view to resolving the outstanding issues between the Centre and the States and among the States inter se.