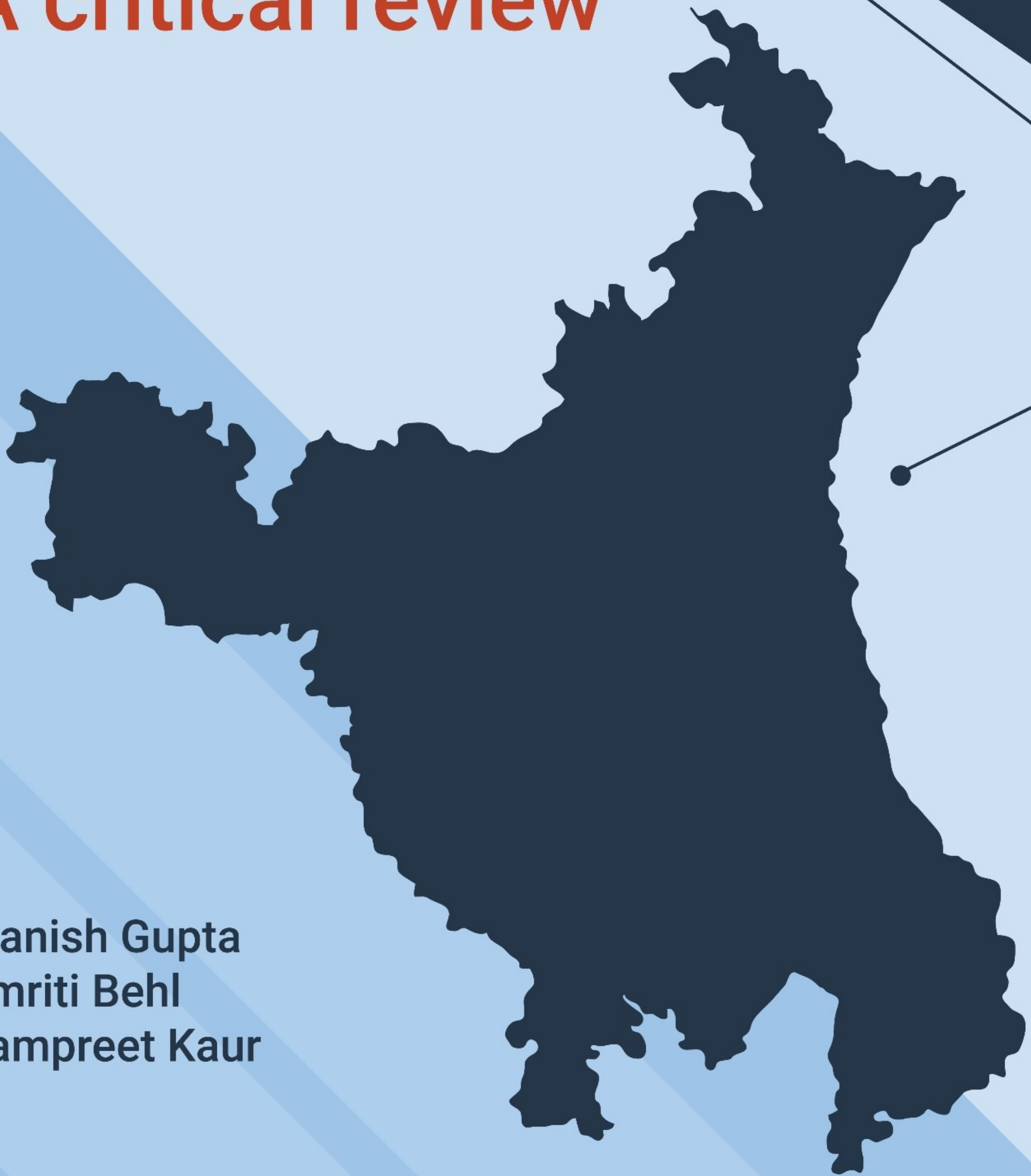
Devolution of funds to ULBs under State Finance Commissions in Haryana: A critical review



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Preface

This study has been undertaken by the National Institute of Public Finance and Policy at the instance of the Sixth State Finance Commission of Haryana.

The study team consists of Manish Gupta, Smriti Behl and Sampreet Kaur. The opinions and analyses here are those of the authors. The members of the Governing Body of the National Institute of Public Finance and Policy are in no way responsible for these.

November 2021 — Pinaki Chakraborty
New Delhi — Director

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- Mr. Sunil Dahiya, Accounts Officer, Finance Department at Sonepat Municipal Corporation.
- Mr. Ashok Kumar, Secretary and Mr. Jitender, Accountant at Pundri Municipal Committee.
- Mr. Manoj Kumar, Chief Accounts Officer and Ms. Ashu, Accounts Clerk, at Ambala Municipal Corporation

The authors are solely responsible for any errors or omissions.

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Executive Summary

- The objective of the study commissioned by the Sixth State Finance Commission (SFC) of Haryana is to conduct a critical review of the devolution of funds to ULBs in the state of Haryana recommended by successive SFCs, analyse the extent up to which conditions imposed by the SFCs have been adhered to in the release and utilization of funds by the urban local bodies (ULBs) and ascertain whether fund flows to ULBs are in compliance with the stated objectives of timely release and untied nature of the grants. The study also examines whether the SFC's grants to ULBs have been subsumed and used for substitution of state grants to municipalities. The study was also required to suggest devolution criteria, quantum, and distribution method among the ULBs of different categories to the Commission.
- The methodology involved examining the reports of all the five SFCs of Haryana along with the explanatory memorandums as to the Action taken on the recommendations made by each of the SFCs submitted by Government of Haryana. It also involved holding discussion/meetings with officers of Department of Finance and Directorate of Urban local bodies, Government of Haryana and senior officials of selected ULBs. The orders/instructions issued by the Department of Finance that operationalized the process and conditions for the release of grants to ULBs were also examined.
- Six urban local bodies - 2 Municipal Corporations, 2 Municipal Councils and 2 Municipal Committees were selected for survey – one from each of the six Administrative divisions of Haryana. The sample was selected in consultation with the Commission
- The Constitution provides for setting up of the SFCs within one year from the commencement of the Constitution Amendment Act 1992, and, thereafter, at the expiry of every fifth year. Government of Haryana constituted its first SFC on 31 May 1994. Subsequent SFCs in Haryana were constituted on a regular basis. Currently, the 6th SFC is in office which was constituted on 22 September 2020 and its recommendations will cover the period from 2021-22 to 2025-26 which is in sync with the award period of the Fifteenth Finance Commission.
- The SFCs in Haryana have taken considerable time in submitting their report. With the exception of the 5^{th} SFC which took 1 year 3.5 months to submit its report, all the other SFCs took around 34 months or more to submit their reports. In case of the 2nd and 4th SFCs, almost the entire award period had passed by the time the report was submitted.
- The reasons for SFCs taking so much of time in the submission of their reports, as highlighted by them in their reports include (a) considerable loss of time in getting office accommodation, setting up the office of the Commission, sanctioning and recruitment of the staff and arranging supporting facilities, (b) inadequate budgetary allocations causing delays in the purchase of office equipment like computers, furniture and other supporting

logistics, (c) non-availability of records of previous SFCs which meant considerable time is lost in re-designing questionnaires and other information formats to collect primary & secondary data.

- As regards the tabling of Action Taken Report by the Government of Haryana is concerned, it is observed that in case of all the five SFCs, the ATR was submitted after the commencement of the award period and in the case of 1st, 2nd and 4th SFCs it was submitted in the final year of the award period of the Commission implying that the entire 5 years of the award period was not available for implementing the recommendations of the Commission.
- The first and second SFCs of Haryana adopted source-specific criteria of sharing state revenues with the local bodies. The taxes to be shared with the local bodies included stamp duty and registration fees, proceeds from cattle fairs, conversion charges for land use, tax on vehicles, entertainment tax, show tax and royalty on minor minerals.
- The scheme of devolution adopted by the third SFC involved both sharing of specific taxes (i.e., shared taxes) and sharing a specific proportion of State's Own Tax Revenues (SOTR) net of the shared taxes and cost of collection with the local bodies. The devolution between RLBs and ULBs was done in the ratio 65:35. The Commission recommended district wise distribution among the local bodies using a number of criteria and weights. Within a district the devolution among ZP:PS:GP was done in the ratio 10:15:75. Further, the inter-se distribution among individual tiers, in both urban and rural areas is based on population and area in the ratio of 80:20.
- The Fourth SFC adopted global sharing mechanism. For the period 2011-12 to 2014-15, the scheme of devolution adopted by the Commission involved sharing specific taxes (i.e., shared taxes) and a specific proportion of State's Own Tax Revenues (SOTR) with the local bodies. During this period, the recommended distribution between RLBs and ULBs was in the ratio 65:35. For 2015-16 the commission adopted global sharing mechanism and recommended sharing 7 percent of SOTR (inclusive of shared taxes) net of Stamp Duty and 2 percent as cost of collections with the local bodies. The distribution between RLBs and ULBs was in the ratio of 50:50. However, due to the delayed submission of the report by the Commission, the Government did not accept its recommendations.
- The Fifth SFC adopted the principle of global sharing of resources. It recommended sharing 7 percent of divisible pool with the local bodies during its award period in the ratio of 55:45 for RLBs and ULBs respectively. Distribution of the RLBs' share between ZP:PS:GP was to be in the ratio of 10:15:75 whereas the distribution between each tier of PRI was on the basis of population and area in the ratio of 80:20. Similarly, the distribution of ULB share, after deducting grants-in-aid for Urban Shared Services Centre, between ULBs in the states was on the basis of population and area in the ratio of 80:20. The distribution scheme used by other states for devolution of funds between RLBs and ULBs was also examined.

- The grants recommended by each of the successive SFCs of Haryana along with the status of their implementation as per the reports were also examined. Grants recommended by SFCs in Haryana accounted for about 2.47-2.65 percent of the total SFC transfers recommended by them.
- We find that there has been a gradual increase in per capita actual devolution to local bodies in Haryana. The per capita devolution show an increase (at constant 2011-12 prices) from Rs. 297.57 in 2006-07 to Rs. 1119.77 in 2017-18 there after declining to about Rs. 659.20 in 2020-21.
- The study also examined the scheme of devolution recommended by latest SFCs in 16 states. We find that with the exception of SFC in Himachal Pradesh, in all other states SFCs have recommended global sharing of resources. While some SFCs have recommended sharing SOTR net of cost of collection, others have netted out some of the state taxes from the SOTR in addition to cost of collection. SFCs in three states have recommended sharing own revenue receipts (i.e., state's own tax and own non-tax revenues) with local bodies. The 5th SFC of Himachal Pradesh adopted a gap filling approach.
- SFCs in other states have used a variety of criteria to derive the share of PRIs and ULBs. While some SFCs (Maharashtra and Punjab SFCs) have used rural-urban population shares as per 2011 census, others (Sikkim and Rajasthan SFCs) have used projected population ratio during the award period of the Commission or projected population ratio in 2020 to determine such shares. In many states SFCs have recommended the sharing ratio in an ad hoc manner. For distribution of resources across different tiers of local governments, we find that the SFCs have used a number of indicators (assigning different weights) viz. Population, Area, SC/ST Population, Slum Population, Revenue Effort, index of infrastructure, number of BPL families, backwardness index etc.
- The Fifteenth Finance Commission in its report for the period 2021-22 to 2025-26 recommended grants of Rs.4,36,361 crore for local governments. This includes Rs. 70,051 crore as health grant to be channelized through local bodies to strengthen and plug the critical gaps in the health care system at the primary health care level.
- The local body grants for Haryana works out to Rs.9066 crores of which Rs. 2520 crore is meant for ULBs. As per the information from the Finance Department, Government of Haryana, in the current fiscal year 2021-22 (till mid October 2021) Rs. 218 crores has been released to Haryana as part of the 15th Finance Commission's ULB grants. This includes Rs. 24 crore for Faridabad which is the only Million-plus city in the state.
- The Commission had recommended several entry level conditions for availing local body grants. The study also examines the guidelines issued by the Ministry of Finance for operationalising these grants.
- Although 15th FC has recommended a much higher quantum as local body grants but a large percentage of it is performance/conditional/tied grants. The share of untied local

body grants recommended by the Commission is much lower than that recommended by 13FC and 14FC. In case of Haryana, the share of untied grants works out to 37.84 percent of aggregate local body grants meant for the state (excluding those for health and on the assumption that the entry level conditions are met). If one were to consider health grants as untied grants, the share of untied would increase to about 48.92 percent.

- From the Interaction with the officials and elected representatives of the selected ULBs we find (a) availability of SFC funds (both quantum and frequency) is not known to the ULBs at the beginning of a financial year, (b) SFC funds are spent on development activities and during covid these were used for payment of salaries and meeting establishment expenses, (c) slow progress of computerization in ULBs especially in councils and committees, (d) lack of training of ULBs staff at all levels, (e) shortage of manpower, (f) lack of awareness about SFC among elected representatives and (g) limited scope for raising own revenues at the council and committee level.
- The study recommends that (a) ULBs should be informed about SFC funds that are likely to be transferred at the time of preparation of the annual budget or before the start of the fiscal year to enable them to plan their activities better, (b) there is a need for greater digitization/computerization especially at the council and committee level, (c) there is a need for training (including induction training) of the staff at all levels in the ULBs on a regular basis, (d) there is also a need to educate the elected representative of ULBs about SFCs, (e) government should fill up vacant posts in the ULBs. Further, there is a need to restructure the entire administrative set-up routinely to check for posts that may have become redundant and create new ones as per the demands of the ULBs, (f) there is a need for devolving more funds by the SFC to the Municipal Councils and Municipal Committees as their sources of own revenues are limited.
- The study recommends that the Commission adopt global sharing mechanism and devolve 7.5 of the net SOTR during 2021-22 to 2023-24 and 8 percent of net SOTR during 2024-25 and 2025-26 to local bodies. The amount thus devolved is to be apportioned between RLBs and ULBs in the ratio of 50:50. It is recommended that the distribution of ULB share between Municipal Corporation, Municipal Council and Municipal Committees should be in the ratio of 50:30:20. Further distribution among individual tiers should be on the basis of Population and Area in the ratio of 75:25.

Devolution of funds to ULBs under State Finance Commissions in Haryana: A Critical Review

1. Introduction

With the constitutional recognition of urban and rural local bodies after the 73rd and 74th constitutional amendments in 1992, the structure of inter-governmental fiscal relations underwent changes. The 73rd and 74th Constitutional amendment envisages local bodies, both rural and urban, to be institutions of self-government. The State legislatures were required under Article 243G and 243W of the Constitution to transfer such powers, functions and responsibilities to rural and urban local bodies as to enable them to function as institutions of self-government. The 11th Schedule to the Constitution lists 29 broad areas for the panchayats while the 12th Schedule lists 18 functions for urban local bodies. In respect of these functions, the State governments, at their discretion were required to devolve these functions to local bodies who were to undertake them concurrently. The Legislature of a State has the power to authorize the Panchayats and the Municipalities to levy and collect suitable local taxes (Article 243H). However, there is no separate list of taxes (similar to the expenditure responsibilities listed in the 11th and 12th Schedules) assigned to them.

Despite Constitutional recognition, in reality the situation is somewhat different. The design and implementation of decentralization do not enable local bodies to function as institutions of self-government. It has been pointed out that many state governments have not devolved functions, funds and functionaries to local governments (Rajaraman and Sinha, 2007; Rao et al 2011). Even where the functions are notionally transferred to local bodies, the staff remains accountable to state governments, thereby adversely impacting the efficacy of carrying out the functions (Reddy and Reddy, 2019). The own revenue efforts of local governments have been poor (Jena and Gupta 2008; Rao and Rao 2008; Rao et al 2011; Gupta 2014; CPR 2014) and they are dependent on higher levels of government for resources and play the role of agents implementing schemes of State and Union Governments.

The legislature is also required to appoint a State Finance Commission (SFC) in all states.[1] Constitution of a State Finance Commission (SFC) is mandated in Article 243-I (1) and 243-Y (1) of the 73rd and 74th Constitutional Amendment Act (CAA), 1992. The SFCs are required to review the financial position of local bodies (i.e., Panchayats and Municipalities) and to make recommendations as to

a) the principles which should govern

[1] Per 73rd and 74th Constitutional Amendment Act 1992, Meghalaya, Mizoram and Nagaland were exempted from constituting SFCs.

(i) the distribution between the State and the local bodies of the net proceeds of the taxes, duties, tolls and fees leviable by the State, which may be divided between them under Part IX and IXA of the Constitution and the allocation between the local bodies (both rural and urban local bodies) at all levels of their respective shares of such proceeds;

(ii) the determination of the taxes, duties, tolls and fees which may be assigned to, or appropriated by, the local level governments;

(iii) the grants-in-aid to the local bodies from the Consolidated Fund of the State;

b) the measures needed to improve the financial position of local bodies; and

c) any other matter referred to the Finance Commission by the Governor in the interests of sound finance of the local level governments.

The Sixth State Finance Commission, Haryana was constituted by the Governor of Haryana on 22 September 2020. The Commission was to hold office for *One year* and was required to make recommendations for the five year period 2021-22 to 2025-26. The Term of the Commission was extended by three months till 31 December 2021 vide notification No. 18/1/2020-2(Pol.) dated 1 September 2021.

2. Objectives of the Study

The present study entitled "***Devolution of funds to ULBs under State Finance Commissions in Haryana: A critical review***" commissioned by the 6th SFC had the following objectives:

- To study the recommendations of the SFCs with respect to devolution and grants to ULBs.
- To analyze the conditions imposed by SFCs in the release and utilization of the funds to ULBs.
- To study the extent up to which conditions imposed by the SFCs have been adhered to and to ascertain whether fund flows to ULBs are in compliance with the state objectives of timely release and untied nature of the grants.
- To study the orders/instructions issued by the Department of Finance that operationalized the process and conditions for the release of grants to ULBs.
- To identify whether the SFC's grants to ULBs have been subsumed and used for substitution of state grants to municipalities.
- To study whether the SFC funds have been changed into 'schemes' by the States and if the nature of the grant has changed from general purpose to a conditionality based specific purpose.
- To suggest the devolution criteria, quantum, and distribution method among the ULBs of different categories to the sitting sixth State Finance Commission of Haryana. Also suggest

how to marry the SFC devolution with the 15th FC recommended criteria of performance – tied and untied grants.

3. Methodology

Given the objectives of the study, the methodology would involve

- Reviewing the reports of all the five SFCs of Haryana that have so far submitted their reports, the methodology adopted by each of them in carrying out their assigned task and the recommendations made by them in devolving funds (devolution and grants) to ULBs in the State.
- Examining the "Explanatory memorandum as to the Action taken on the recommendations made by each of the SFCs" (i.e, the Action Taken Report) submitted by the Government of Haryana.
- Holding discussions with the concerned departments of Haryana Government viz. Finance Department, Directorate of Urban Local Bodies; examining orders and notifications issued by them and release of funds.
- Interaction with officials and elected representatives of selected Urban Local bodies - Municipal Corporations, Municipal Councils and Municipal Committees. The selection of the ULBs is done in consultation with the State Finance Commission.

How the various objectives of the study is mapped to the proposed methodology is presented in table 1.

Table 1: Mapping of Study Objectives to the Proposed Methodology

Objectives of the study	Methodology
1) To study the recommendations of SFCs with respect to devolution and grants to ULBs 2) To analyze the conditions imposed by SFCs in the release and utilization of funds to ULBs	➢ Reviewing the SFC reports and the Explanatory memorandum as to the Action taken on the recommendations made by each of the SFCs submitted by Government of Haryana.
3) To study the extent up to which conditions imposed by the SFCs have been adhered to and to ascertain whether fund flows to ULBs are in compliance with the stated objectives on timely release and untied nature of the grants.	➢ Holding meetings/discussions with concerned departments of Haryana Government (Finance and Directorate of Urban Local Bodies). ➢ Validating these with interaction with officials and representatives of select ULBs - Municipal Corporations, Municipal Councils and Municipal Committees.
4) To study the orders/instructions issued by the Department of Finance that operationalized	➢ Holding discussions / meetings with officials of the Finance Department and

Objectives of the study	Methodology
the process and conditions for the release of grants to ULBs.	examination of relevant orders, instructions and notifications issued.
5) To identify whether the SFC's grants to ULBs have been subsumed and used for substitution of state grants to Municipalities.	➢ Holding meetings/ discussions with the concerned departments of Haryana Government. ➢ Validating these with interaction with officials and representatives of select ULBs.
6) To study whether the SFC funds have been changed into 'schemes' by the States and if the nature of the grant has changed from general purpose to a conditionality based specific purpose.	
7) To suggest the devolution criteria, quantum, and distribution method among the ULBs of different categories to the 6th SFC. Also suggest how to marry the SFC devolution with the 15th FC recommended criteria of performance – tied and untied grants	➢ Review of SFC reports of Haryana; interactions with officials of state government departments, officials and elected representatives of local governments; Reviewing latest available SFC reports of some of the other states, examining the vertical and horizontal distribution of resources to ULBs recommended by them; and lessons that can be learnt from other states. ➢ Examining the recommendations of 15th FC with respect to ULBs and the operational guidelines issues by Department of Expenditure, Ministry of Finance, Government of India.

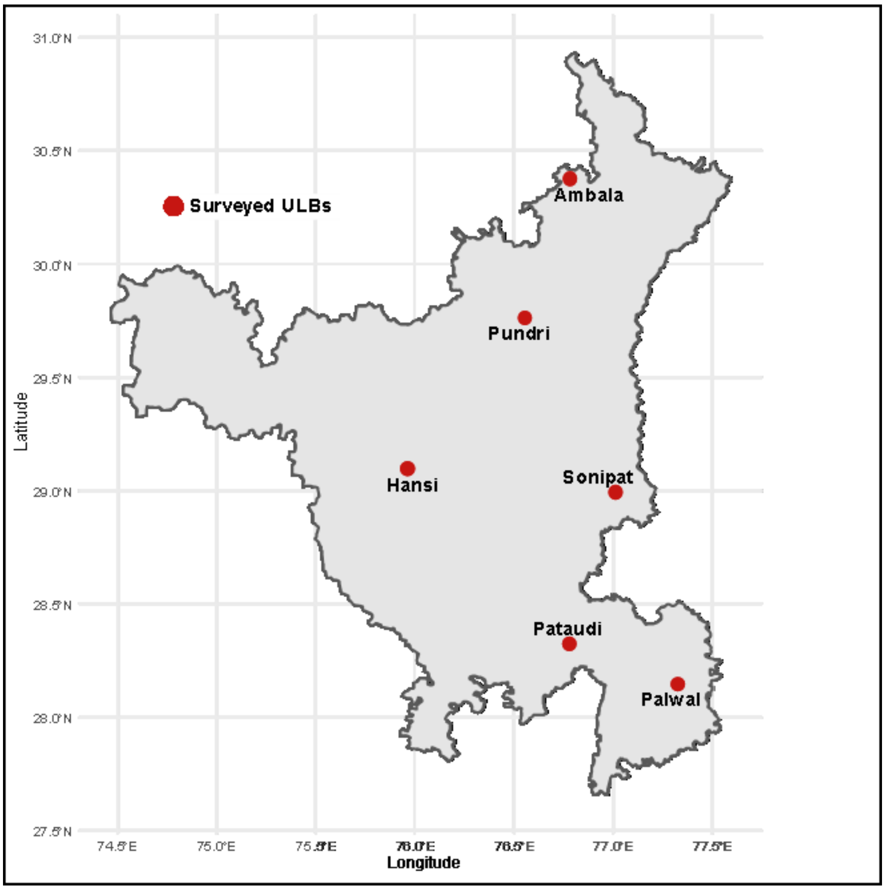
4. Sample Selection

A total of 6 ULBs (2 Municipal Corporations, 2 Municipal Councils and 2 Municipal Committees) were selected for survey – one from each of the six Administrative divisions of Haryana. The ULBs were selected through purposive sampling and in consultation with the Commission and Directorate of Urban Local Bodies (DULB). The selected ULBs are presented in table 2, while Fig-1 shows the location of surveyed ULBs in Haryana.

Table 2: Urban Local Bodies Selected for Survey

	ULB Name	ULB Type	District	Division
1	Sonepat	Municipal Corporation	Sonepat	Rohtak
2	Ambala	Municipal Corporation	Ambala	Ambala
3	Palwal	Municipal Council	Palwal	Faridabad
4	Hansi	Municipal Council	Hisar	Hisar
5	Pataudi	Municipal Committee	Gurugram	Gurugram
6	Pundri	Municipal Committee	Kaithal	Karnal

Figure 1: Urban Local Bodies Surveyed



5. Review of Reports of SFCs of Haryana

Following the constitutional provision of setting up of the first SFC within one year from the commencement of the Constitutional Amendment (73rd Amendment) Act 1992 and thereafter, at the expiry of every fifth year, the Government of Haryana constituted its first SFC on 31 May 1994. The Commission was to make recommendations for the period 1997-98 to 2000-01. While the Commission was required to submit its report by 30 May 1995 as per its initial ToR, its term was extended a number of times by the state government and the report was submitted on 31 March 1997 (table 3). The Commission took around 2 years 10 months to submit its report.

Subsequent SFCs in Haryana were constituted on a regular basis as evident from table 3. Currently, the 6th SFC is in office which was constituted on 22 September 2020 and its recommendations will cover the period from 2021-22 to 2025-26 which is in sync with the award period of the Fifteenth Finance Commission.

The SFCs in Haryana have taken considerable time in submitting their report. With the exception of the Fifth SFC which took 1 year 3.5 months to submit its report all the other SFCs took around 34 months or more to submit their reports. In the case of 2nd and 4th SFCs, almost the entire award period had elapsed by the time the report was submitted by the Commissions. The term of the Commissions were extended by the State Government by giving multiple extensions[2] without considering the award period of the Commissions. ***It is recommended that while giving extension(s) to the Commission, the government should keep in mind the award period for which the Commission has to make its recommendations.***

The reasons why SFCs have taken so much time in the submission of their reports, as mentioned by them include (a) Considerable loss of time in getting office accommodation, setting up the office of the Commission, sanctioning and recruitment of the staff and arranging supporting facilities, (b) Inadequate budgetary allocations also caused a lot of delays in purchase of office equipment like computers, furniture and other supporting logistics, (c) Furthermore it has been pointed out that due to the non-availability of the records of previous SFCs, whenever a new Commission is set up, considerable time is lost in re-designing questionnaires and other information formats to collect primary and secondary data from the concerned departments.

Table 3: Time taken to submit reports by SFCs in Haryana

SFC	Award Period	Date of Appointment as per ToR	Date of Submission as per initial ToR	Date of Actual Submission	Actual Time Taken
First	1997-98 to 2000-01	31 May 1994	30 May 1995	31 March 1997	2 years 10 months
Second	2001-02 to 2005-06	6 Sep 2000	31 Dec 2000	30 Sep 2004	4 years
Third	2006-07 to 2010-11	22 Dec 2005	31 Dec 2006	31 Dec 2008	3 years
Fourth	2011-12 to 2015-16	16 April 2010	31 March 2011	30 June 2014	4 years 2 months
Fifth	2016-17 to 2020-21	26 May 2016	May 2017	13 Sep 2017	1 year 3.5 months
Sixth	2021-22 to 2025-26	22 Sep 2020	Sep 2021		

Source: Reports of SFCs of Haryana

As regards tabling of action taken report (ATR) by the Government of Haryana is concerned it is observed that in case of 1st SFC, the government took 3 years and 5 months to table the ATR and in the case of 2nd SFC, the time taken to table the ATR was around 1 year 4 months (Table 4). In case of all the other SFCs the time taken by the government has been one year or less. In the case of 4th SFC, due to considerable delay in the submission of the report, the government in its explanatory memorandum as on the recommendations of the 4th SFC pointed out that *"Since, the Report of the 4th SFC has been received with only one financial year (2015-16) remaining for the Finance Commission period, there was no time left to follow*

[2] The term of the 1st SFC was extended 4 times vide notifications dated 31-05-1994, 26-05-1995, 30-11-1995, and 02-05-1996; the 2nd SFC's terms was extended 7 times vide notifications dated 02-03-2001, 04-10-2001,18-03-2002, 03-09-2002, 24-01-2003, 15-07-2003 and 15-10-2003. The 3rd and 4th SFCs got 2 and 4 extensions respectively, while the 5th SFC's term was extended once.

the required procedure of constituting a Cabinet Sub-committee for examining the recommendations of the final report of the 4th SFC and then incorporating the decisions in the shape of budgetary proposals in the 2015-16 Budget. Therefore, it is proposed to continue with the present devolution pattern in 2015-16 also". The government continued to transfer resources to local bodies in the state based on the recommendations of the 3rd SFC during 2011-12 to 2015-16 also. It is observed that in case of all the five SFCs, the ATR was submitted after the commencement of the award period and in the case of 1st, 2nd and 4th SFCs it was submitted in the final year of the award period of the Commission implying that the entire 5 years of the award period was not available for implementing the recommendations of the Commission.

Table 4: Status of Tabling ATR by Haryana Government

SFC	Award Period	Date of Actual Submission of Report	Date of Submission of ATR by Government	Time Taken to Table ATR
First SFC	1997-98 to 2000-01	31 March 1997	4 Sept 2000	3 years 5 months
Second SFC	2001-02 to 2005-06	30 Sep 2004	19 Dec 2005	1 year 4 months
Third SFC	2006-07 to 2010-11	31 Dec 2008	1 Sept 2009	8 months
Fourth SFC	2011-12 to 2015-16	30 June 2014	13 Mar 2015	7.5 months
Fifth SFC	2016-17 to 2020-21	13 Sep 2017	4 Sept 2018	1 year

Source: Reports of SFCs of Haryana and ATR reports submitted by Haryana Government.

5.1. Principles of Devolution/Revenue Sharing Recommended by SFCs in Haryana and Action Taken by Government of Haryana

Review of SFCs of Haryana and that of other states reveal that there are three approaches that are commonly used by them for sharing revenues with local bodies. These are

a) Sharing of specific taxes and duties (1st and 2nd SFCs, Haryana),
b) Sharing of fixed amount in monetary terms (5th SFC HP; 4th SFC WB; 3rd SFC AP), and
c) Global sharing of state revenues (3rd, 4th and 5th SFCs Haryana).

Post 80th amendment to the Constitution of India in 2000, the Union Finance Commissions (i.e., from the Eleventh Finance Commission onwards) also moved to a global sharing of tax revenues from the earlier sharing of specific taxes. Prior to that only two taxes (a) Personal Income Tax compulsorily and (b) Union Excise Duties, if needed were shared with the state governments.

Most SFCs also shifted from sharing of specific taxes to global sharing. The global sharing of taxes has advantages. It increases transparency, objectivity, and certainty and shares the buoyancy of state taxes directly with the local bodies. This enables them to plan their priorities in advance as the divisible pool becomes consistent and predictable.

While recommending revenue sharing mechanism, the basic objective of all the SFCs in Haryana was to suggest a scheme of fiscal transfers which could serve the purpose both of equity and efficiency and at the same time result in predictable and stable transfers.

Furthermore, the principle of equalisation had also been a guiding factor in their design of transfers.

Let us now examine the scheme of devolution recommended by the State Finance Commissions in Haryana and the action taken by the Government of Haryana on these.

First SFC (1997-98 to 2000-01): The Commission adopted source-specific criteria of sharing state revenues with the local bodies. The taxes to be shared with the local bodies included stamp duty and registration fees, proceeds from cattle fairs, conversion charges for land use, tax on vehicles, entertainment tax, show tax and royalty on minor minerals.

For rural local bodies (all three tiers), it recommended sharing

(i) 7.5 percent of the total receipts under Stamp Duty & Registration fee accruing from the registration of the rural lands/properties,
(ii) 10 percent of the proceeds under conversion charges for land use
(iii) 20 percent of the Royalty on Minor Minerals was to be shared with the local bodies of which 50 percent was to accrue to RLBs, and
(iv) Entire net income from cattle fair to be shared with panchayat samitis only.

For urban local bodies, it recommended sharing

(i) 50 percent of net income from Entertainment Duty and Entire proceeds from Show tax
(ii) 20 percent of the net proceeds from the taxes on vehicles, and
(iii) 20 percent of the Royalty on Minor Minerals was to be shared with the local bodies of which 50 percent was to accrue to ULBs

From the examination of the Action Taken Report (ATR) placed in the State Legislature by the state government we find that not all recommendations of the Commission with regards to sharing resources with local bodies were accepted. Some were accepted with modifications and many were not accepted at all. The government did not implement the recommendations relating to sharing of stamp duty and registration fees despite accepting it with modifications.

The details of SFC recommendations of the 1st SFC along with the action taken by the government is presented in Table 5.

Second SFC (2001-02 to 2005-06): The second SFC followed the same methodology as that of the first SFC and adopted source-specific criteria of sharing state revenues with local bodies.

For rural local bodies (all three tiers), it recommended sharing

(i) 3 percent of the total receipts under Stamp Duty & Registration fee accruing from the registration of the rural lands/properties,
(ii) 10 percent of the proceeds under conversion charges for land use

(iii) 20 percent of the Royalty on Minor Minerals was to be shared with the local bodies of which 50 percent was to accrue to RLBs, and
(iv) Entire net income from cattle fair to be shared with panchayat samitis only.

For urban local bodies, it recommended sharing

(i) 50 percent of net income from Entertainment Duty and Entire proceeds from Show tax
(ii) 20 percent of the net proceeds from the taxes on vehicles, and
(iii) 20 percent of the Royalty on Minor Minerals was to be shared with the local bodies of which 50 percent was to accrue to ULBs

To compensate the local bodies for loss in revenues due to abolishment of Octroi, Local Area Development Tax (LADT) was introduced. Its proceeds were to be shared with RLBs and ULBs after deducting 5 percent as collection charges.

From the examination of the Action Taken Report (ATR) placed in the State Legislature by the state government we find that not all recommendations of the Commission with regards to sharing resources with local bodies were accepted. Some were accepted with modifications and many were not accepted at all.

The details of recommendations of the 2nd SFC along with the action taken by the government is presented in Table 6.

Third SFC (2006-07 to 2010-11): The scheme of devolution adopted by the third SFC involved both sharing of specific taxes (i.e., shared taxes) with the local bodies and sharing a specific proportion of State's Own Tax Revenues (SOTR) net of the shared taxes and cost of collection with the local bodies. The shared taxes include Local Area Development Tax (LADT) and Revenues from State Excise.

The Commission recommended sharing 4 percent of SOTR net of LADT, revenues from state excise and 1.25 percent towards collection cost with the local bodies.

The recommendations of the 3rd SFC relating to sharing of revenues with local bodies were accepted with modification by the State Government and implemented. The recommendations were modified to 2 percent of the divisible pool[3] for the years 2006-07, 2007-08 and 2010-11 and 3 percent for 2008-09 and 2009-10.

As regards shared taxes, the state government accepted the recommendations of the Commission.

[3] The third SFC defined the divisible pool as: SOTR minus LADT, state excise revenues and 1.25 percent of SOTR as collection charges.

Table 5: First SFC (1997-98 to 2000-01)

Total Devolution to RLBs (Shared Taxes)		Total Devolution to ULBs (Shared Taxes)	
<u>Stamp Duty and Registration Fees</u> • 7.5% of net receipts under the head 'Stamp Duty & Registration fee accruing from registration of the rural lands/properties be transferred to RLBs. • District-wise distribution based on ***Decentralised Planning Scheme*** • Distribution in the ratio 10:15:75 to ZP:PS:GP. • Share of PS & GP within a district on Population basis	• **Accepted with modification** • Modified to 3% of net proceeds only for 2000-01. • Was not implemented as per 3rd SFC report.	**<u>Entertainment Duty and Show Tax</u>** • Entertainment Duty: 50% net income from Entertainment Duty devolved to ULBs on the basis of origin. • Show Tax: Entire proceeds from Show tax should devolved to ULBs on the basis of origin	• **Accepted with modification.** • 25% of the net proceeds to be shared. • Implmented
<u>Conversion charges for change of land use</u> • 10% of the proceeds are devolved to RLBs • distributed further on the basis of origin and criteria developed by the State government	• **Not Accepted**	**<u>Taxes on Vehicles</u>** • 20% net proceeds devolved of ULBs • Inter-se distribution among ULBs on the basis of Population (50%) and on criteria related to Road Length, their maintenance cost or some other criteria developed by State govt. (50%)	• **Accepted only for the year 1999-00** • Implemented
<u>Royalty on Minor Minerals</u> • 20% of net proceeds are devolved to Local Bodies (of which 50% accrue to RLBs) • Distributed partly on basis of origin and partly on basis of suitable criteria evolved by State government	• **Not Accepted**	**<u>Royalty on Minor Minerals</u>** • 20% of net proceeds from Royalty on Minerals are devolved to Local Bodies (of which 50% accrue to RLBs)	• **Not Accepted**
<u>Revenue from cattle fairs</u> • Entire income net of establishment expenses and 5% maintenance charges from cattle fair to be devolved to Panchayat Samitis	• **Accepted with Modification** • 80% to be devolved to PS & 20% to ZP		

Source: Report of the 1st SFC and ATR submitted by Government of Haryana.

Table 6: Second SFC (2001-02 to 2005-06)

Devolution to RLBs (Shared Taxes)		Devolution to ULBs (Shared Taxes)	
1. **Stamp Duty and Registration Fees** • 3% of net receipts accruing from registration of rural lands/properties be transferred to RLBs. • District-wise distribution based on **Decentralised Planning Formula** • Distribution between PRIs in the ratio 10:15:75 to ZP:PS:GP. • Share of PS and GP within a district on Population basis	• **Partially Accepted** • As per the report of 4th SFC it was not accepted	1. **Taxes on Vehicles** • 20% of net proceeds to be devolved to ULBs • 50% to be distributed on the basis of Population (50%) and 50% on criteria related to Road Length, their maintenance cost or some other criteria developed by the State govt.	• **Partially Accepted**
2. **Conversion charges for change of land use** • 10% of the proceeds are devolved to RLBs based on a criteria to be evolved by the Panchayat department	• **Not Accepted**	2. **Entertainment Duty and Show Tax** • ***Entertainment Duty***: 50% of net income to be devolved to ULBs on the basis of origin. • ***Show Tax***: Entire proceeds devolved to ULBs on the basis of origin	• **Partially Accepted**
3. **Local Area Development Tax (LADT)** • 65% of net proceeds to PRIs (deducting 5% as collection charges & adjustments for maintenance of roads & water supply) • Distribution based on the ratio 10:15:75 to ZP:PS:GP	• ATR is silent on this • 3rd SFC: As per HPC findings • 4th SFC: Accepted	3. **Local Area Development Tax (LADT)** • 35% of net proceeds to ULBs (deducting 5% as collection charges & adjustments for maintenance of roads & water supply areas) • Distributed on the basis of **Decentralized Planning** or any other criteria laid down by State Govt.	• ATR is silent on this • 3rd SFC: As per HPC findings • 4th SFC: Accepted
4. **Royalty on Minor Minerals** • 20% of net proceeds devolved to Local Bodies (50% to RLBs). • To be distributed partly based on origin and partly based on a suitable criteria to evolved by Panchayat dept	• **Partially Accepted**	4. **Royalty on Minor Minerals** • 20% net proceeds from Royalty on Minerals to be devolved to Local Bodies (of which 50% accrue to RLBs)	• **Partially Accepted**
Revenue from Cattle Fairs (for Panchayat Samitis) Entire net income devolved to Panchayat Samitis	• **Not Accepted**		
Decentralised Planning Formula/Criteria Population (40%); SC Population (10%); Rural Population (5%); Unemployment (5%); Backwardness in agriculture & irrigation (10%); Backwardness in industries (10%); Backwardness in elementary education (10%); Backwardness in hospital and veterinary facilities (10%)			

Source: Report of the 2nd SFC and ATR submitted by Government of Haryana.

Fourth SFC (2011-12 to 2015-16): The commission moved towards adopting global sharing mechanism and its devolution scheme involved two steps

Step 1 (for 2011-12 to 2014-15) – For the period 2011-12 to 2014-15, the scheme of devolution adopted by the Commission involved sharing specific taxes (i.e., shared taxes) and a specific proportion of State's Own Tax Revenues (SOTR) with the local bodies.

The Shared taxes include (a) Surcharge on VAT - 5 percent of it is shared with local bodies, (b) Excise duties, and (c) Stamp duty – entire proceeds devolved to local bodies. Further the Commission recommended sharing 2.5 percent of SOTR (inclusive of shared taxes) net of 2 percent as cost of collections with the local bodies.

Step 2 (for 2015-16): For 2015-16 the commission adopted global sharing mechanism and recommended sharing 7 percent of SOTR (inclusive of shared taxes) net of Stamp Duty and 2 percent as cost of collections with the local bodies.

Due to the delayed submission of the report by the Commission, the Government did not accept its recommendations.

Fifth SFC (2016-17 to 2020-21): The Commission adopted the principles of global sharing of resources. It recommended sharing 7 percent of divisible pool with the local bodies during its award period. The divisible pool comprised GST and non-GST SOTR components. While the GST component was transferred to the divisible pool as a whole, the non-GST SOTR was adjusted by netting out collection costs @ 1.5%, Stamp Duty @ 2%, registration revenue and VAT revenue.

The recommendations of the Commission were accepted and implemented by the state government.

5.2. Allocation Principle Recommended by SFCs in Haryana

First State Finance Commission: For the RLBs, the Commission recommended sharing 7.5 percent of the total receipts of Stamp Duty & Registration fee. The district-wise distribution of the proceeds was to be done on the basis of Decentralised Planning Formula/Criteria[4] (see Table 5). Within a district the distribution between Zilla Parishad (ZP), Panchayat Samiti (PS) and Gram Panchayat (GP) was on the basis of the following ratio ZP:PS:GP = 10:15:75. Further, the share of PS and GP within each district was on the basis of population. *This recommendation was accepted with the modification that only 3% of the total proceeds would be shared with the local bodies. However, it was not implemented.*

[4] The Decentralised Planning Formula/criteria consisted of the following indicators and weights: (i) Population (40%); (ii) SC Population (10%); (iii) Rural Population (5%); (iv) Unemployment (5%); (v) Backwardness in agriculture & irrigation (10%); (vi) Backwardness in industries (10%); (vii) Backwardness in elementary education (10%); (viii) Backwardness in hospital and veterinary facilities (10%).

The Commission recommended that 10 percent of the proceeds under conversion charges for land use were to be devolved to RLBs which was to be further distributed between ZPs, PSs and GPs on the basis of origin and criteria to be developed by the State government. *This recommendation was not accepted.*

It also recommended that the entire income from cattle fair net of establishment expenses and maintenance charge at the rate of 5 percent was to be devolved to Panchayat Samitis. *This recommendation was accepted with the modification that 80 percent of the net income was to be devolved to the Panchayat Samitis and 20 percent to the Zila Parishads.*

Of the taxes accruing to ULBs, 50 percent of the net income from Entertainment Duty was to be transferred along with the entire proceeds from Show tax, based on origin. *The recommendation regarding sharing of Show tax was accepted, however, instead of devolving 50 percent of the net income from Entertainment Duty, it was lowered to 25 percent.*

Further 20 percent of the net proceeds from the taxes on vehicles was also to be transferred to the ULBs. Inter se distribution among the ULBs was done on the basis of population (with 50 percent weight) and on criteria related to Road Length, their maintenance cost or some other criteria developed by State government (50 percent weight). *This recommendation was accepted and implemented only for the financial year 2000-2001.*

The Commission also recommended sharing 20 percent Royalty on Minor Minerals with the RLBs and ULBs in an equal proportion. This was to be distributed further partly on the basis of origin and partly on the basis of a suitable criteria to be evolved by the State government. *This recommendation was not accepted by the state government* (table 5).

Second State Finance Commission: For the RLBs, the Commission recommended sharing 3 percent of the total receipts of Stamp Duty & Registration fee. The district-wise distribution of the proceeds is to be done on the basis of Decentralised Planning Formula/Criteria (refer Table 6). Within a district the distribution between Zilla Parishad (ZP), Panchayat Samiti (PS) and Gram Panchayat (GP) is on the basis of the following ratio ZP:PS:GP = 10:15:75. Further, the share of PS and GP within each district is on the basis of population. *This recommendation was partially accepted to the extent of sharing Rs. 10 crores in lump-sum for the year 2005-06.*

The Commission recommended 10 percent of the proceeds from conversion charges for change of land use to be devolved to RLBs based on a criterion to be evolved by the Panchayat department of Haryana Government. It also recommended devolving entire income from cattle fair to the Panchayat Samitis. *Both these recommendations were not accepted.*

Of the taxes shared with the ULBs, 50 percent of the net income from Entertainment Duty was to be transferred along with the entire proceeds from Show tax, on the basis of origin. *This recommendation was partially accepted by the state government.*

The Commission recommended 20 percent of the net proceeds from the taxes on vehicles to be transferred to the ULBs which would be further shared equally on the basis of population and road length. *This recommendation was partially accepted by the state government.*

In order to compensate the local bodies for loss in revenues on account of abolishment of Octroi, the state government imposed the Local Area Development Tax (LADT). The proceeds from LADT were to be shared among the RLBs and ULBs in the ratio 65:35 after deducting 5 percent towards collection charges and making adjustments for maintenance of roads and water supply. The distribution among the PRIs was based on the ratio 10:15:75 for ZP:PS:GP respectively, that among the ULBs was based on the Decentralised Planning Formula[5] or any other criteria to be developed by the state government. *This recommendation was accepted by the state government.*

The Commission further recommended sharing 20 percent of the Royalty on Minor Minerals with the RLBs and ULBs in an equal proportion which was distributed further on the basis of origin and criteria to be developed by the State government. *This recommendation was partially accepted by the state government, to the extent of sharing Rs 5 crore in lump-sum for 2005-06.* (Refer to table 6 for further details).

Third State Finance Commission:

Shared Taxes**:** Shared taxes recommended by the commission were State Excise and Land Area Development Tax (LADT).

State Excise Revenue was devolved to local bodies based upon the sale of liquor in their respective jurisdictions.

Proceeds from LADT net of 5 percent collection changes was to be devolved between ULBs and PRIs in the ratio of 50:50. Further distribution of PRIs share of LADT between ZP, PS and GP should be in the ratio of 10:15:75.

Recommendations relating to the shared taxes were accepted by the state government.

Global Sharing: Recommended sharing 4 percent of the divisible pool with PRIs and ULBs in the ratio of 65:35. Although the Rural-Urban population share as per 2001 census was 71:29, the Commission recommended higher share to ULBs on account of faster growth of urban population in the state and to cater to the needs of mounting population pressure on urban infrastructure.

From the total yearly share of PRIs and ULBs 10 percent is kept aside as incentive grants and the rest is distributed district-wise separately among PRIs and ULBs.

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[5] The Decentralised Planning Formula/criteria consisted of the following indicators and weights: (i) Population (40%); (ii) SC Population (10%); (iii) Rural Population (5%); (iv) Unemployment (5%); (v) Backwardness in agriculture & irrigation (10%); (vi) Backwardness in industries (10%); (vii) Backwardness in elementary education (10%); (viii) Backwardness in hospital and veterinary facilities (10%).

District-wise distribution of PRI share is based on the following criteria and weights: (a) rural population (40%), (b) Rural BPL population (25%), (c) Rural Area (25%) and (d) Rural literacy gap (10%). Within a district the devolution among the RLBs is done in the ratio of 10:15:75 for ZP:PS:GP. Further distribution among individual tiers (i.e., PSs and GPs) is based on population and area in the ratio of 80:20.

District-wise distribution of ULB share is based on the following criteria and weights: (a) urban population (40%), (b) urban BPL population (25%), (c) urban Area (25%) and (d) urban literacy gap (10%). Further distribution among ULBs within a district is based on population and area in the ratio of 80:20.

Fourth State Finance Commission:

Shared Taxes (or Non-SFC Devolution)**:** Shared taxes were State Excise, surcharge on VAT and Stamp Duty.

The proceeds of state excise duties were to be shared with the Panchayati Raj Institutions (PRIs)[6] and Municipal Bodies. These proceeds were shared with local bodies i.e. RLBs and ULBs on the basis of the sale of liquor in their respective jurisdictions. The ratio for sharing the said proceeds between GPs: PSs: ZPs was 70: 20: 10.

The entire proceeds from Stamp Duty were transferred to the ULBs

Proceeds from surcharge on VAT at the rate of 5 percent was shared with local bodies in the ratio of 80:20 between ULBs and PRIs.

Global Sharing: For 2011-12 to 2014-15, the Commission recommended sharing 2.5 percent of the divisible pool with PRIs and ULBs in the ratio of 65:35 in conformity with the rural-urban population ratio as per the 2011 census.

For 2015-16, it recommended sharing 7 percent of the divisible pool with PRIs and ULBs. The distribution between PRIs and ULBs was in the ratio of 50:50.

District-wise distribution of PRI share was based on the following criteria and weights: (a) rural population (40%), (b) Rural area (25%), (c) Rural Literacy Gap (15%), (d) Sex ratio (10%) and (e) AAY Population (10%). Within a district the distribution among PRIs was in the ratio of 10:15:75 for ZP:PS:GP. Further distribution among individual tiers (i.e., PSs and GPs) was based on population and area in the ratio of 80:20.

District-wise distribution of ULB share was based on the following criteria and weights: (a) urban population (40%), (b) urban area (25%), (c) urban Literacy Gap (15%), (d) Sex ratio (10%) and (e) AAY Population (10%). Further distribution among ULBs was based on population and area in the ratio of 80:20.

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[6] The terms PRIs (Panchayati Raj Institutions) and RLBs (Rural local bodies) are interchangeably used in the report.

Since the report of the 4th SFC was tabled in June 2014 with only one year remaining, i.e., 2015-16, the government decided to continue with the devolution scheme recommended by the Third SFC. In other words, none of the recommendations of the Fourth SFC were accepted by the state government.

Fifth State Finance Commission: It recommended sharing 7 percent of the divisible pool of resources between PRIs and ULBs in the ratio of 55:45.

Distribution of PRI share between ZP:PS:GP was to be in the ratio of 10:15:75. Distribution between each tier of PRI was on the basis of population and area in the ratio of 80:20.

Distribution of ULB share, after deducting grants-in-aid for Urban Shared Services Centre, between ULBs in the states was on the basis of population and area in the ratio of 80:20.

The recommendations of the Commission were accepted by the State Government.

The criteria adopted by successive SFCs in Haryana for distribution of resources between PRIs and ULBs is summarised in table 7. Both the 3rd and 5th SFCs in the state had recommended higher share of funds to ULBs in the state on account of rapid pace of urbanisation in Haryana. However, the 4th SFC recommended sharing resources between PRIs and ULBs on the basis of their population shares as per 2011 census.

Table 7: Distribution of Shares between PRIs and ULBs

SFC	PRIs	ULBs	Remarks
1st SFC	-	-	● Adopted source-specific criteria of sharing state revenues with local bodies (Refer Table 5)
2nd SFC	-	-	● Adopted source-specific criteria of sharing state revenues with local bodies (Refer Table 6)
3rd SFC	65	35	● Rural-Urban population share as per 2001 census was 71:29 ● Higher share to ULBs on account of faster growth of urban population in the state and to cater to the needs of mounting population pressure on urban infrastructure
4th SFC	65	35	● Rural-Urban population share as per 2011 census
5th SFC	55	45	● Did not specify any reason for this distribution criteria

Source: Reports of SFCs of Haryana

Table 8 summarises the distribution of shares of PRIs and ULBs in the divisible pool among individual local bodies in Haryana since the Third State Finance Commission. While the third and fourth SFCs recommended district wise-distribution of PRI and ULB shares, the fifth SFC did not adopt this approach and recommended distributing the RLB share directly of the ZPs, PSs and GPs. The distribution of funds between the ZPs, PSs and GPs has been in the ratio of 10:15:75. This sharing ratio has remained the same across SFCs in the state. For inter-se distribution among each individual tiers, SFCs in Haryana have used population and area in the ratio of 80:20.

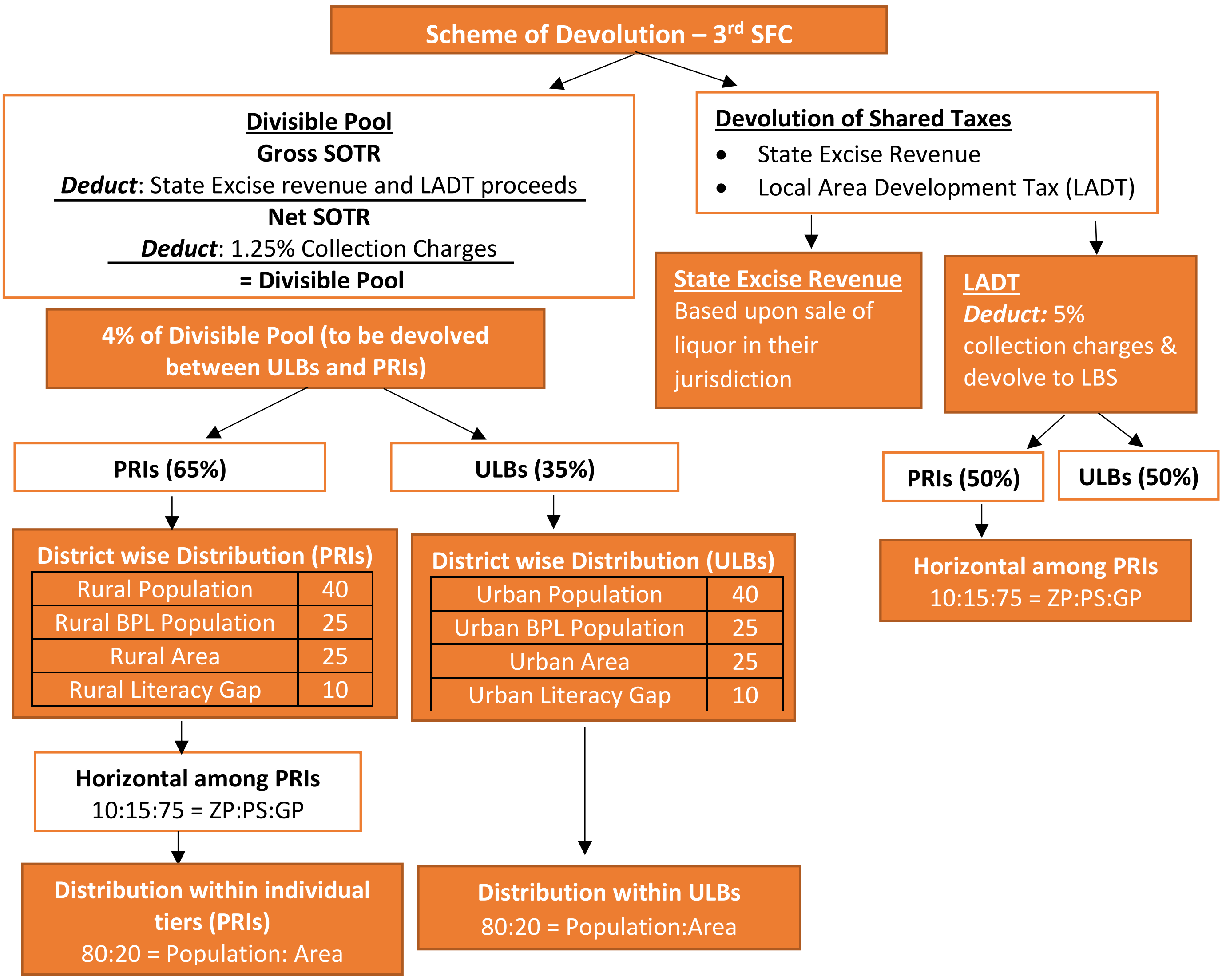
Table 8: Distribution of Shares of PRIs and ULBs to Local Bodies (Haryana)

SFC	District-wise Distribution	Inter se ZP:PS:GP	Horizontal Distribution (GP & PS and ULBs)
3rd	Composite Index comprising of • Population (rural/urban) (40%) • BPL Population (rural/urban) (25%) • Area (25%) • Literacy Gap (10%)	10: 15: 75	**Share of PS & GP within a district:** Population (80%) & Area (20%) **Inter se share of ULBs within a district:** Population (80%) & Area (20%)
4th	Composite Index comprising of • Population (rural/urban) (40%) • Area (rural/urban) (25%) • Literacy Gap (rural/urban) (15%) • AAY Population (10%) • Gender/Sex Ratio (10%)	10: 15: 75	**Share of PS & GP within a district:** Population (80%) & Area (20%) **Inter se share of ULBs within a district:** Population (80%) & Area (20%)
5th	Did not recommend district-wise distribution	10: 15: 75	**GP, PS & ZP:** Population (80%) & Area (20%) **ULBs:** Population (80%) & Area (20%)

Source: Reports of SFCs of Haryana

The scheme of devolution recommended by the 1st and 2nd SFC is summarised in tables 5 and 6 while that recommended by 3rd, 4th, and 5th SFCs is summarised in Figure 2, 3, and 4.

Figure 2: Scheme of Devolution Recommended by 3rd SFC (2006-07 to 2010-2011)



Incentive Fund at the District level each for PRIs and ULBs

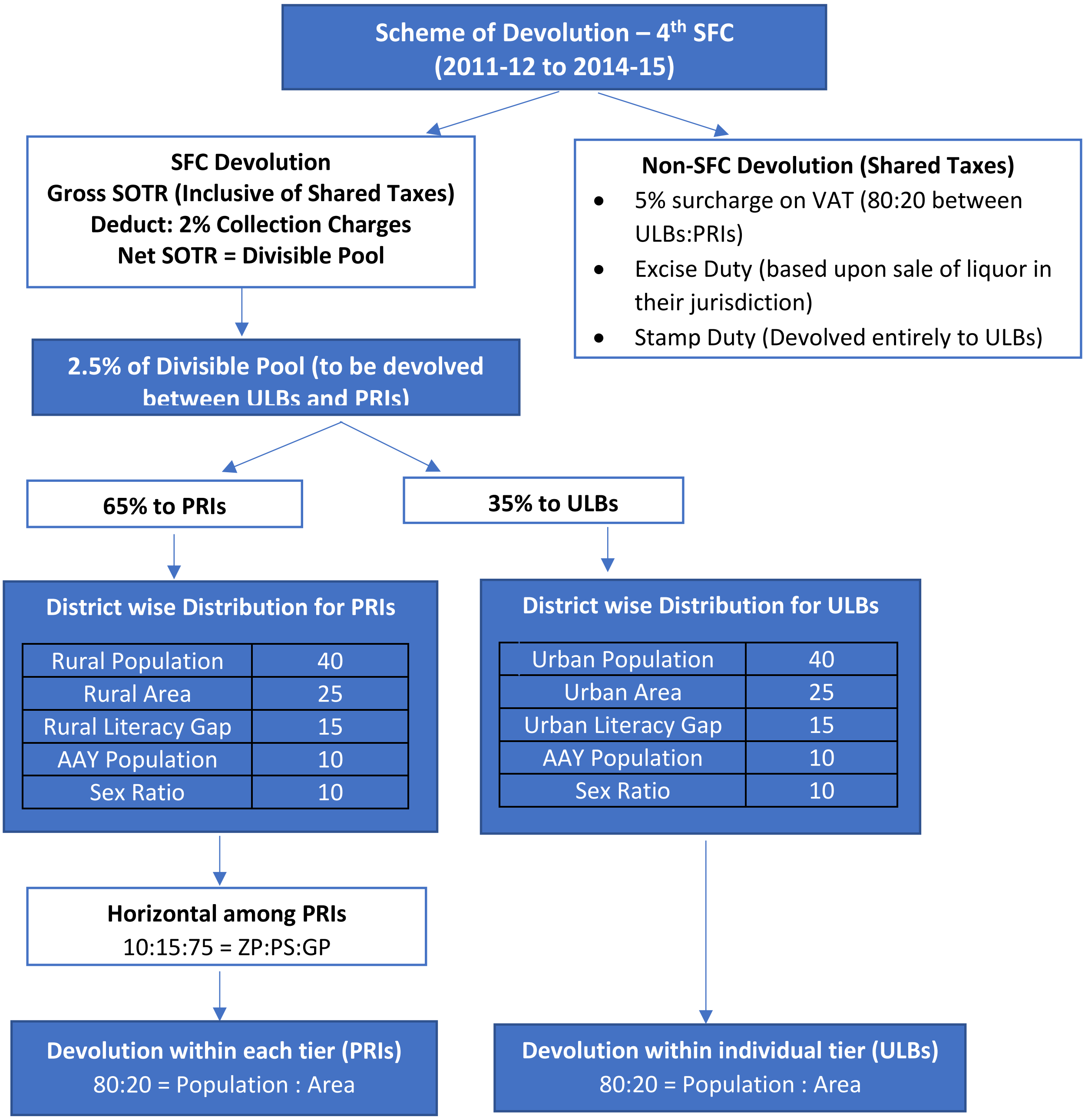
10% of the annual entitlement of PRIs and ULBs

- 50% of annual accruals allocated to those LBs that show better revenue performance measured in terms of at least 10% higher growth rate in their own tax and non-tax revenue over preceding year. Also minimum recovery of 60% of total annual demand from own-tax and non-tax revenue with 5% increase every year.
- 50% to those LBs which show higher performance over the standard norms in respect of each core areas of performance (to be fixed by the state government)

Source: Report of the 3rd SFC

Figure 3a: Scheme of Devolution Recommended by 4th SFC (2011-12 to 2015-16)

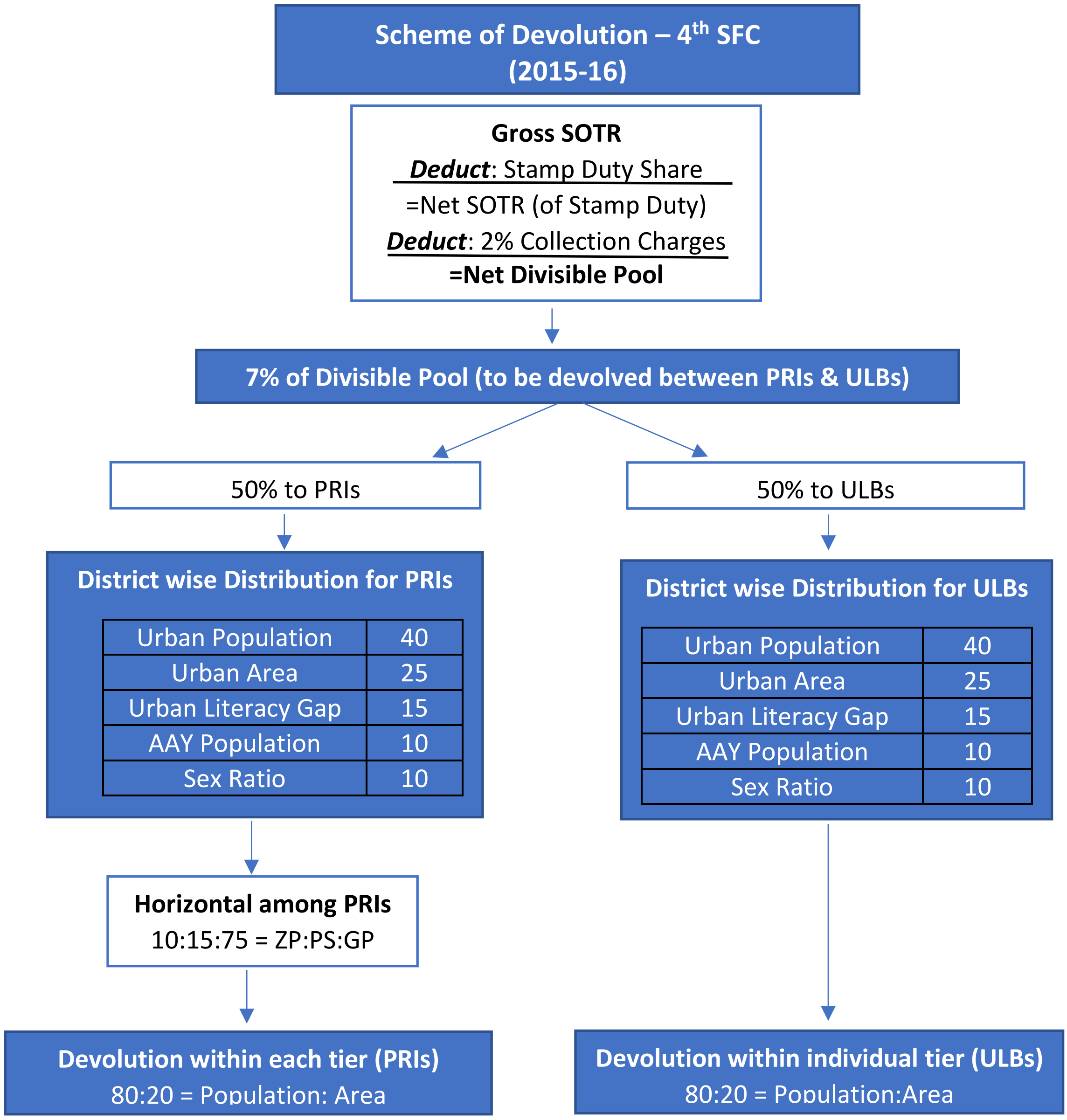
Step-1: For 2011-12 to 2014-15



Source: Report of the 4th SFC

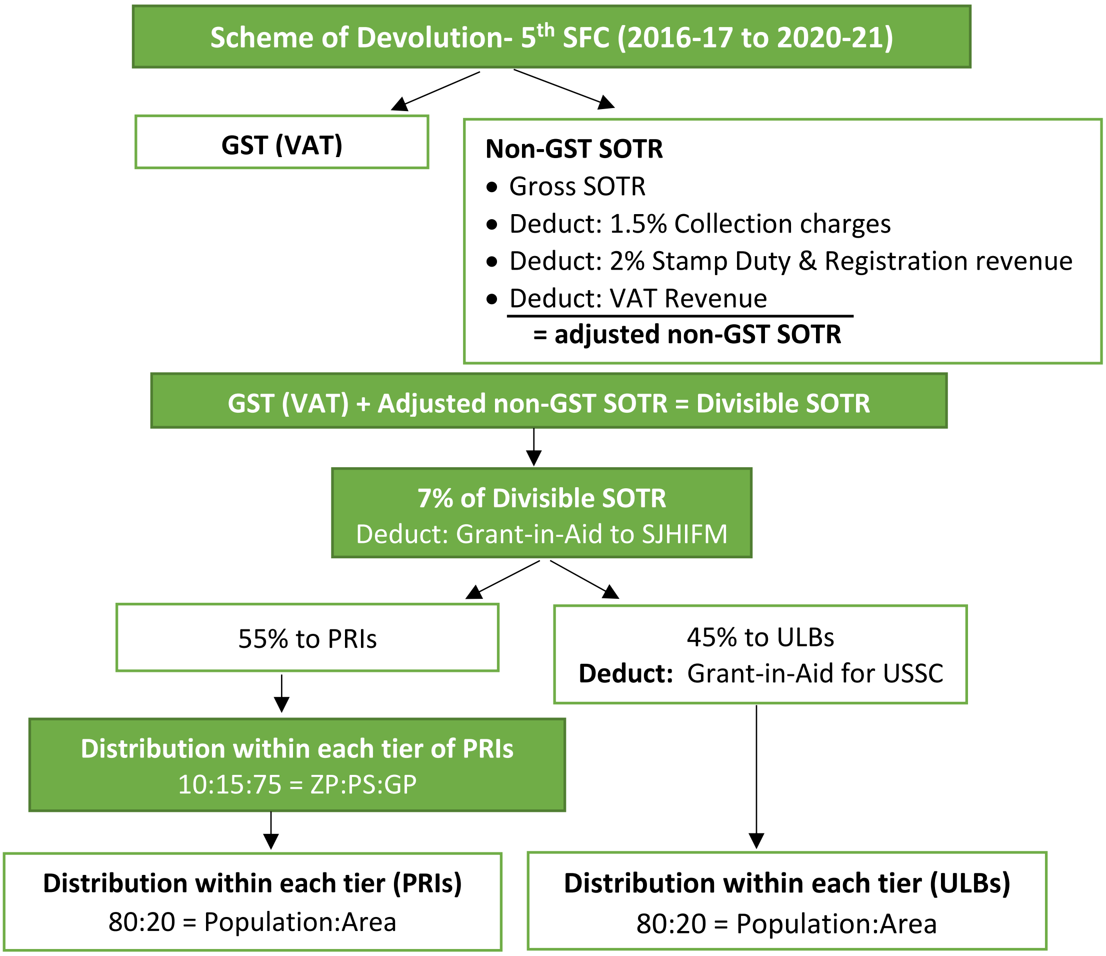
Figure 3b: Scheme of Devolution Recommended by 4th SFC (2011-12 to 2015-16)

Step-2: For 2015 – 16



Source: Report of the 4th SFC

Figure 4: Scheme of Devolution Recommended by 5th SFC (2016-17 to 2020-21)



Source: Report of the 5th SFC

5.3. Grants-in-aid

Grants are an important component of State Finance Commission transfers. They are meant to fill revenue gaps for the local bodies to enable them to discharge their expenditure responsibilities. SFCs in Haryana have been of the opinion that the major source of funds to local bodies should be tax-sharing and the role of grants should be purely supplementary.

Review of reports of all the five SFCs in Haryana reveal that with the exception of the 3rd SFC, all of them have recommended grants. The grants recommended by SFCs in Haryana and the action taken by the state government as per the explanatory memorandum presented in the State Legislature is presented in Table 9.

Table 9: Grants Recommended by SFCs in Haryana

SFC	Grants-in-Aid	Action Taken by the State Govt.
1st	• Grants for maintenance of community assets by RLBs (Rs. 10 lakh per block per year) and maintenance of PRI buildings (Rs. 1 lakh per block per year with a 10% increase every year). - Rs. 56.66 crore for the award period of the Commission • One-time Grant of Rs. 25 lakh for repair of ZP/PS buildings • Sanitation and Environmental Improvement Grant for RLBs of Rs. 10.17 crore for the award period of the SFC • Incentive grant to RLBs worth Rs. 1.67 crore per annum to be distributed on the basis of performance parameters • Development Grants for RLBs @ Rs. 50 per capita (1991 census) per annum along with a 10% step up each successive year • Grants to ULBs for Development purposes and future needs @ Rs. 50 per capita (1991 census) per annum along with a 10% step up each successive year, totaling to 74.92 crore for the award period	• Accepted for 2000-01, not implemented • Accepted and implemented for 2000-01. • However, as per the 4th SFC report it was not accepted • Accepted for 2000-01. • However, as per 3rd and 4th SFC reports it was accepted but not implemented • Accepted for 2000-01. • However, as per 3rd and 4th SFC report it was accepted but not implemented • Not Accepted • Not Accepted
2nd	• Grants for maintenance of community assets by RLBs (Rs. 10 lakh per block per annum) and maintenance of PRI buildings (Rs. 1 lakh per block per annum along with a 10% increase every year), totaling to 77.90 crore for the entire award period • One-time Grant of Rs. 25 lakh for repair of ZP/PS buildings • Incentive grants to RLBs in the form of cash awards worth Rs. 17.89 crore for the award period, based on their performance. The parameters to measure performance of each RLB to allocate incentive grants would be decided by state government • Sanitation and Environmental Improvement Grant for RLBs totaling to Rs. 30.23 crore for the entire award period • Grants to RLBs @ Rs. 25 per capita (2001 census) along with a 10% increase every year, for their development needs and meeting resource constraints. Total of Rs. 228.94 crore for the entire award period • Grants to ULBs @ Rs. 25 per capita (2001 census) per annum along with a 10% step-up every year, for all MCs (including Faridabad MC), for their development needs and meeting resource constraints totaling to 88.58 crore for the award period	• Government accepted Rs. 12.76 crore for 2005-06 • Not Accepted • Not Accepted • Not Accepted • Accepted devolution of Rs. 22.24 crore for 2004-05 • Partially Accepted
3rd	***Did not recommend any Grants***	
4th	• Grants for maintenance and upkeep of municipal roads and for Solid waste management totaling Rs. 57.85 crore • A Special one-time grant of Rs. 25 lakh for up-gradation and strengthening of fire services by ULBs. This includes training of	• Due to the delay in the submission of the report, recommendations of the 4th SFC were not accepted.

SFC	Grants-in-Aid	Action Taken by the State Govt.
	manpower, conducting public awareness programmes, building equipment etc. • Grants for capacity building and skill up-gradation of elected representatives of local bodies and other government officials. This grants consists of Rs. 15 crores to be provided to HIRD Nilokheri (6 crores), SCDTC Nilokheri (3 crores) and HIPA Gurgaon (6 crores) • Grant for setting up research units in three universities in Haryana, Kurukshetra University, MDU, Rohtak and GJU, Hissar (Rs. 25 lakhs eack) (Rs. 75 lakh) • Grant of Rs. 10 crore to be shared equally among the RLBs and ULBs for strengthening of data base • Grant of Rs. 20 crore to RLBs and ULBs for hiring qualified personnel to revamp the system of management of accounts and improve the auditing standards • Creation of Incentive Fund at district level with 10% annual entitlement of PRIs and ULBs to safeguard against adverse fiscal implications of unconditional transfers	
5th	• Special grant to Swarna Jayanti Haryana Institute for Fiscal Management to provide the SFCs with continuous support in terms of high-quality research on ULBs and RLBs schemes, services, capacity and finances (Rs. 70 crore) • Grants for establishing State Level Urban Shared Services Center (USSC) – (Rs. 250 crore)	• Accepted • Accepted with modification. The services of USSC should be utilised for both ULBs and RLBs.

Source: Reports of all the five SFCs and Action Taken Reports submitted by the State Government

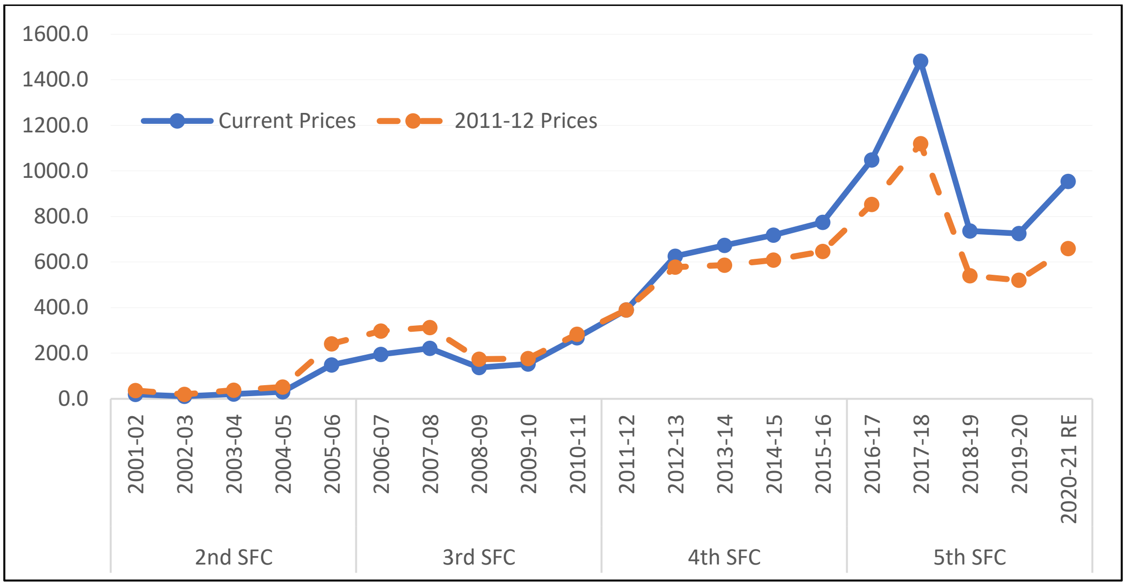
5.4. Quantifying Devolution to Local Bodies by SFCs in Haryana

Local bodies are required to provide various services like water supply, sanitation, solid waste management, drainage, public toilets, street lighting and maintenance of roads. As their own revenues are low and most of the central and state funds are tied in nature, the devolution from SFC is an important source of untied resources to them. Fig 5 presents actual per capita transfer of funds to local bodies in Haryana both in nominal and 2011-12 prices by the state government on the recommendations of the SFCs. We see that there has been a gradual increase in per capita actual devolution to local bodies in Haryana. The per capita devolution show an increase (at constant 2011-12 prices) from Rs. 297.57 in 2006-07 to Rs. 1119.77 in 2017-18 there after declining to about Rs. 659.20 in 2020-21RE. The average per capita devolution (at constant 2011-12 prices) during the award period of the Third SFC was Rs. 248.59 which increased to Rs. 561.90 during the award period of Fourth SFC[7], and further to

[7] The award period of the 4th SFC was from 2011-12 to 2015-16. As the recommendations of the 4th SFC were not accepted by the Government, the recommendations of the 3rd SFC were extended during the award period of the 4th SFC.

Rs. 735.45 during the award period of the Fifth SFC (Table 10). In 2021-22, the per capita devolution to local bodies, as per the budget estimates presented by the state government, works out to Rs. 747.48. The spike in actual devolution in 2017-18 is due to the release of one time arrears of surcharge on VAT to urban local bodies.

Figure 5: Per Capita Actual Devolution to Local Bodies in Haryana (Rs.)



Note: The award period of the Fourth SFC was from 2011-12 to 2015-16. As the recommendations of the 4th SFC was not accepted by the Government, the recommendations of the 3rd SFC was continued during the award period of the 4th SFC.
Source: Calculated using data given in the SFC Reports and information provided by the Finance Department, Government of Haryana.

Table 10: Average Per Capita Actual Devolution (at 2011-12 prices) (Rs.)

SFC (Award Period)	**Amount** *(Rs.)*
3rd SFC Award Period - 2006-07 to 2010-11	248.59
4th SFC Award Period - 2011-12 to 2015-16	561.90
5th SFC Award Period - 2016-17 to 2020-21	738.45
2021-22 BE	747.48

Source: Calculated using data given in the SFC Reports and information provided by the Finance Department, Government of Haryana.

6. Lessons from SFCs of Other States

Our Terms of reference requires us to suggest devolution criteria, quantum, and distribution method among the ULBs of different categories. Apart from reviewing the scheme of devolution adopted by the previous five SFCs of Haryana we have also examined the devolution scheme recommended by the latest SFCs in some of the other states in the country.

6.1. Scheme of Devolution Recommended by SFCs in Other States

6.1.1. Composition of the Divisible Pool

Examining the latest available SFC reports of 16 states, we find that with the exception of Himachal Pradesh, all of them have recommended global sharing of resources. While some of the SFCs have recommended sharing State own tax revenue (SOTR) net of cost of collection, other have netted out some of the state taxes from the SOTR in addition to cost of collection. SFCs in three states have recommended sharing own revenue receipts (i.e., state's own tax and own non-tax revenues) with the local bodies, while the 5th SFC of Himachal Pradesh adopted a gap filling approach wherein the funds to be devolved to the local bodies was derived/ calculated by including salaries of staff, honorarium of members, office expenses, TA/DA expenses etc. Table 11 presents how SFCs in other states have defined the divisible pool and the quantum of devolution recommended by them.

Table 11: Composition of Divisible Pool and Quantum of Devolution Recommended by SFCs in Other States

<table>
<tr><th>Share of Net Own Tax Revenue
(net of cost of collection only)</th><th>Share of Net Own Tax Revenue
(net of cost of collection and other taxes/ charges)</th><th>Share of Own Revenues receipts</th><th>No Specific Recommendation/ Criteria</th></tr>
<tr>
<td>• Assam (5th): 15.5% of net SOTR in 2015-16, 15% in 2016-17, 14.50% in 2017-18, 14% in 2018-19, and 13.5% in 2019-2020.
• Kerala (5th): 20% of net SOTR in 2016-17; for subsequent years it increases by 1% every year
• Odisha (5th): 10% of net SOTR.
• Punjab (5th): 4% of net SOTR.
• Rajasthan (5th): 8.5% of net SOTR excluding GST compensation.
• Sikkim (5th): 4.5% of net SOTR; 0.5% of net SOTR should be allocated for capacity building of PRIs and ULBs; 0.5% of net SOTR should be allocated for special support to most backward PRIs and ULBs.
• Uttarakhand (4th): 11% net SOTR.
• West Bengal (4th): 2.5% of net SOTR.</td>
<td>• Bihar (5th): 8.5% of State's net own tax revenue in 2015-16 and 9% in 2016-17 to 2019-20. Net of cost of collection and entertainment tax.
• Chhattisgarh (3rd): 9% of net tax revenues of the state, net of land revenue, tax on goods and passengers, other taxes on commodities and services and cost of collection
• Madhya Pradesh (4th): 1st interim report: 5% of the States net own tax revenue for 2015-16; 2nd & final interim report: 7.5 % of State's net own tax revenues (90%) for remaining 4 years.
• Tamil Nadu (5th): 10% of State's own tax revenue 2017-22. Net of Surcharge on stamp duty, cost of collection and other surcharges, if any</td>
<td>• Karnataka (4th): 48% of Non-loan net Own revenue receipt (NLNORR) inclusive of GST compensation but excludes 14th FC grants
• Maharashtra (4th): at least 40% of state's own tax and non-tax revenue
• Uttar Pradesh (4th): 15% of State's tax and non-tax revenues net of collection cost.</td>
<td>• Himachal Pradesh (5th): adopted a gap filling approach. Funds to be devolved derived by including salaries of staff, honorarium of members, office expenses, TA/DA expenses.</td>
</tr>
</table>

Source: SFC Reports of respective states.

6.1.2. Distribution among Rural and Urban Local Bodies

Having decided on the quantum of funds to be devolved to local bodies, the SFCs have used a variety of criteria to derive the share of PRIs and ULBs as evident from table 12. While some SFCs (Maharashtra and Punjab SFCs) have used rural-urban population shares as per 2011 census to decide on the shares of RLBs and ULBs, others (Sikkim and Rajasthan SFCs) have used projected population ratio during the award period of the Commission or projected population ratio in 2020 to determine such shares. Many of the SFCs have not used any criteria and recommended the sharing ratio in an ad hoc manner.

From table 12 one can see that the share of RLBs is dominant in most States except Uttar Pradesh and Uttarakhand. In Bihar, Rajasthan, Uttarakhand and West Bengal SFCs acknowledging the increase in urbanization have stressed on the need for devolving more funds to ULBs.

The 4th SFC of Uttar Pradesh adopted the same sharing ratio of 60:40 between ULBs and RLBs as that recommended by the 3rd SFC. The 3rd SFC in its report pointed out that both the 1st and 2nd SFCs of the state had adopted this sharing ratio and it did not want to change the ratio based on population as it would create lot of confusion in the system and result in financial crisis among the ULBs in the state. Furthermore, the 4th SFC pointed out that although the share of rural population in the state is much higher, the state government allocates lot of funds to RLBs under various schemes while the ULBs have to provide basic services to the population largely from its own sources. Hence, it is of the view that the share of ULBs should be 60 percent while the remaining 40 percent should go to RLBs.

Table 12: Distribution of Local Bodies Share between PRIs and ULBs by SFCs in Select States

	States	PRIs	ULBs	Remarks
1	Assam (5th)	--	--	Distribution based on population (80%); density (20%)
2	Bihar (5th)	70 60	30 40	70:30 in 2015-16 and 60:40 for remaining 4 years **No specific criteria** but resources need to be transferred to ULBs
3	Chhattisgarh (3rd)	76.8	23.2	Distribution based on population (2011 census)
4	Himachal Pradesh (5th)	--	--	**No specific criteria.** Adopted gap filling approach. Funds to be devolved derived by including salaries, honorarium, office and TA/DA expenses.
5	Karnataka (4th)	75	25	**Distribution based on 11 indicators** under 3 domains which are common to both rural & urban areas: (i) Demography (net increase in population, area, SC/ST population, Illiteracy), (ii) Decentralized Governance, (iii) Basic Household Amenities.
6	Kerala (5th)	--	--	Devolution comprises of General Purpose Fund, Maintenance Fund and Development Fund. Each Fund has its own distribution criteria
7	Madhya Pradesh (4th)	73	27	Distribution based 70% on population (census 2011), 15% on area and 15% on ST/SC population

	States	PRIs	ULBs	Remarks
8	Maharashtra (4th)	55	45	**Distribution based on population (census 2011)**
9	Odisha (5th)	75	25	The sharing ratio arrived at based on population (35%); density of population (35%); percentage of persons below poverty line (22%); SC/ST concentration (8%)
10	Punjab (5th)	--	--	**60% share of taxes distributed between PRIs & ULBs in the ratio 2011 population.** 40% share of taxes be distributed between PRIs & ULBs on the basis of and in proportion to gaps in projected revenue and expenditure during 2016-17 to 2020-21. While PRIs will have surplus and ULBs will be in deficit during 2016-17 to 2020-21, this 40% share will go to ULBs alone.
11	Rajasthan (5th)	70	30	**Distribution based projected rural-urban population as on 1 March 2020** & pressure of floating population in urban areas due to migration from rural areas on a daily/seasonal basis for education, employment, medical treatment, and for various other purposes.
12	Sikkim (5th)	70	30	**Distribution based on expected rural-urban population during 2020-25**
13	Tamil Nadu (5th)	56	44	The sharing ratio as per the needs (O&M and Capital), and Infrastructure creation in RLBs and ULBs
14	Uttar Pradesh (5th)	40	60	**No specific criteria**
15	Uttarakhand (4th)	45	55	**No specific criteria** but based on multiple factors like roles, responsibilities and committed liabilities of PRIs & ULBs and increase in urbanisation.
16	West Bengal (4th)	--	--	**No criteria**. From each year recommended devolution; funds for ULBs set aside based on estimated cost of providing services by them. The balance funds forms PRIs share.

Source: SFC Reports of respective states.

Further distribution of resources across different tiers of local governments – both rural and urban as recommended by SFCs is presented in Table 13. It is evident from the table that states have used a variety of indicators (assigning different weights) to distribute resources across different tiers of local governments. Some of the indicators used are Population, Area, SC/ST Population, Slum Population, Revenue Effort, index of infrastructure, number of BPL families, backwardness index etc.

Table 13: Distribution across Different Tiers of Local Government (Rural and Urban) (in %)

<table>
<tr><th rowspan="2"></th><th rowspan="2">States</th><th colspan="4">PRIs</th><th colspan="4">ULBs</th></tr>
<tr><th>ZP</th><th>PS</th><th>GP</th><th>Criteria/Description</th><th>Municipal Corporation</th><th>Municipalities</th><th>Nagar Panchayat</th><th>Criteria/Description</th></tr>
<tr><td>1</td><td>Assam (5th)</td><td>30</td><td>30</td><td>40</td><td>Stage 1: Allocation to PRIs in different districts in Normal Areas on the basis of a weighted average of (i) Population (50%), (ii) Geographical Area (25%) and (iii) Inverse Per Capita Rural District Domestic Product (25%).
Stage 2: share among the 3 tiers i.e., ZPs, APs and GPs shall be in the ratio of 30:30:40.
Stage 3: Share of AP and GP in a district determined on the basis of their respective 2011 census population.</td><td>--</td><td>--</td><td>--</td><td>Allocation based on Population (50%); Area (25%); index of infrastructure (12.5%); per capita tax collection (12.5%).</td></tr>
<tr><td>2</td><td>Bihar (5th)</td><td>20</td><td>10</td><td>70</td><td><table>
<tr><th rowspan="2">Criterion</th><th colspan="3">Weights (%)</th></tr>
<tr><th>ZP</th><th>BP</th><th>GP</th></tr>
<tr><td>Population</td><td>50</td><td>50</td><td rowspan="3">Each GP falling within a Block would get equal share of amount available to all GPs in that Block based on Block's UDI and Population</td></tr>
<tr><td>Area</td><td>10</td><td>0</td></tr>
<tr><td>Under Development Index</td><td>40</td><td>50</td></tr>
</table></td><td>--</td><td>--</td><td>--</td><td><table>
<tr><th rowspan="2">Criterion</th><th rowspan="2">Inter ULBs</th><th colspan="3">Weights (%)</th></tr>
<tr><th>MC</th><th>N Par</th><th>N Panc</th></tr>
<tr><td>Population</td><td>70%</td><td>1.5</td><td>1.3</td><td>1.0</td></tr>
<tr><td>Area</td><td>10%</td><td>1.0</td><td>1.0</td><td>1.0</td></tr>
<tr><td>No. of BPL families</td><td>20%</td><td>1.0</td><td>1.0</td><td>1.0</td></tr>
</table></td></tr>
</table>

<table>
<tr><th rowspan="2"></th><th rowspan="2">States</th><th colspan="4">PRIs</th><th colspan="4">ULBs</th></tr>
<tr><th>ZP</th><th>PS</th><th>GP</th><th>Criteria/Description</th><th>Municipal Corporation</th><th>Municipalities</th><th>Nagar Panchayat</th><th>Criteria/Description</th></tr>
<tr><td>3</td><td>Chhattisgarh (3rd)</td><td>5</td><td>15</td><td>80</td><td>Stage 1: Criteria for district wise allocation among PRIs is-<table><tr><td>Rural Population</td><td>60</td></tr><tr><td>Rural Area</td><td>15</td></tr><tr><td>SC/ST Population</td><td>10</td></tr><tr><td>Deprivation Index of SECC</td><td>10</td></tr><tr><td>Women Literacy</td><td>5</td></tr></table>Stage 2: Inter-se distribution among GPs:JPs:ZPs in the ratio 80:15:5
Stage 3: The shares of GPs and JPs would be divided on basis of population.</td><td></td><td></td><td></td><td>Criteria for allocation among ULBs is based on Urban Population (70%), Urban Area (20%) and Performance Grant of 14FC (10%)</td></tr>
<tr><td>4</td><td>Himachal Pradesh (5th)</td><td>--</td><td>--</td><td>--</td><td>No specific criteria</td><td>--</td><td>--</td><td>--</td><td>No specific criteria</td></tr>
<tr><td>5</td><td>Karnataka (4th)</td><td>38.61</td><td>53.64</td><td>7.76</td><td>Based on the average transfer of funds (for PRIs) for five years, i.e., 2012-13 to 2016-17 under all heads to each tier of PRIs.</td><td>--</td><td>--</td><td>--</td><td>Class-wise devolution among the ULBs is based on the following criteria-<table><tr><td>Population</td><td>40</td></tr><tr><td>Area</td><td>20</td></tr><tr><td>Level of Illiteracy</td><td>20</td></tr><tr><td>SC/ST Population</td><td>20</td></tr></table></td></tr>
<tr><td>6</td><td>Kerala (5th)</td><td>--</td><td>--</td><td>--</td><td>No specific criteria</td><td>--</td><td>--</td><td>--</td><td>No specific criteria.
However, distribution is based on different percentages of funds allocated for General Purpose (3.5%), Development Purpose (11%) and Maintenance Purpose (5.5%) for local bodies based on the projections of SOTR by Commission.</td></tr>
</table>

	States	PRIs				ULBs			
		ZP	PS	GP	Criteria/Description	Municipal Corporation	Municipalities	Nagar Panchayat	Criteria/Description
7	Madhya Pradesh (4th)	0	0	100	Based on population of GPs, classified into various class-sizes.	5+10*	40	45	No specific criteria
8	Maharashtra (4th)	30	20	50	No specific criteria	40	60	--	Distribution based on population
9	Odisha (5th)	10	20	70	The GPs were further grouped into 4 categories based on population size and the funds were devolved accordingly. Accounting for the developmental needs of the GPs, the SFC devolved an additional 25% of the funds in favour of GPs situated in Scheduled areas.				Inter-se devolution among ULBs is based on population
10	Punjab (5th)	--	--	--	80% share in tax revenue to be disbursed among all Panchayats in proportion to individual Panchayat's population as per 2011 census. Remaining 20% be given as additional grant for poor Panchayats. Payments to Panchayats be routed through ZPs. Both 80% and 20% of grants be transferred to ZPs in proportion to rural population of the district and population of poor Panchayats of the district respectively.	--	--	--	80% share in tax revenue be disbursed among ULBs in proportion to 2011 population of each ULB. Remaining 20% be given as additional allocation to poor ULBs, to be distributed in proportion to population. Poor ULB are those whose per capita tax income is lower than the average of per capita tax revenue of all ULBs.

<table>
<tr><th rowspan="2"></th><th rowspan="2">States</th><th colspan="4">PRIs</th><th colspan="4">ULBs</th></tr>
<tr><th>ZP</th><th>PS</th><th>GP</th><th>Criteria/Description</th><th>Municipal Corporation</th><th>Municipalities</th><th>Nagar Panchayat</th><th>Criteria/Description</th></tr>
<tr><td>11</td><td>Rajasthan (5th)</td><td>5</td><td>20</td><td>75</td><td>Stage 1: District-wise devolution among the RLBs is based on-
<table><tr><td>Population</td><td>40</td></tr><tr><td>Area</td><td>15</td></tr><tr><td>Child sex ratio</td><td>10</td></tr><tr><td>S.C. population</td><td>5</td></tr><tr><td>S.T. population</td><td>5</td></tr><tr><td>Infant Mortality Rate</td><td>5</td></tr><tr><td>Girls Education</td><td>5</td></tr><tr><td>Decline in Decadal Population Growth</td><td>5</td></tr><tr><td>Deprivation on 7 criteria as per SECC-2011</td><td>10</td></tr></table>Stage 2: Inter-se distribution among GPs:PSs:ZPs is in the ratio 75:20:5
Stage 3: Devolution to each GP is based on share of population of GP in total population of ZP; and devolution to each PS is based on share of population of PS in total population of ZP</td><td></td><td></td><td></td><td>For the ULBs, 70% of their share is to be distributed on the basis of population (55%) and area (15%). The remaining 20% is to be transferred to all municipalities on population basis and 10% to the municipalities in proportion to the per capita own income deviation from the highest per capita own income.</td></tr>
<tr><td>12</td><td>Tamil Nadu (5th)</td><td>8</td><td>37</td><td>55</td><td>Population as per 2011 Census (60%); Area (15%); SC/ST Population (15%); Per Capita Consumption Expenditure Distance (10%)</td><td>40</td><td>29</td><td>31</td><td>Sharing based on Population (Census 2011) (65%); Area (15%); Per Capita Consumption Expenditure Distance (10%); Proportion of Slum Population (10%)</td></tr>
<tr><td>13</td><td>Sikkim (5th)</td><td>35</td><td>--</td><td>65</td><td>Population figures of Census 2011</td><td>--</td><td>--</td><td>--</td><td>No specific criteria</td></tr>
</table>

	States	PRIs				ULBs			
		ZP	PS	GP	Criteria/Description	Municipal Corporation	Municipalities	Nagar Panchayat	Criteria/Description
14	Uttar Pradesh (4^{th})	15	10	75	(i) District-wise distribution based on population (50%); Area (10%); SC/ST population (10%); backwardness index (30%) (ii) PSs and GPs: Population (80%); SC/ST population (20%).	42	38	20	(i) Shares obtained on the basis of Population (90%); Area (10%) (ii) Inter-se distribution amongst each of the 3 tiers of ULBs based on Population (40%); Area (5%); SC/ST population (10%); Average per capita income of own resources (15%); backwardness index (access to wealth) (10%); Overall backwardness index (20%).
15	Uttarakhand (4^{th})	35	30	35	(i) Devolution to each tier of PRIs based on separate criteria based on Population, Area, Remoteness and Tax effort (ii) ZPs:KPs:GPs distribution based on Population (50:50:60), Area (20:30:20), Tax effort (15:00:00), Remoteness (15:20:20) respectively	40	45	15	(i) Devolution to each tier of PRIs based on separate criteria based on Population, Area, Tax effort and Centrality Index as a proxy for floating population (for NNs and NPPs only) (ii) NNs:NPPs:NPs distribution based on Population (50:60:60), Area (20:10:20), Tax effort (20:20:20), Centrality index (10:10:00) respectively
16	West Bengal (4^{th})	10	12	78	Focus on Developmental Activities. Horizontal distribution across PRIs on the basis of Index based on Population (50%), Area (10%), Backwardness (30%), proportion of Urban Population (10%) in rural areas to arrive at figures pertaining to horizontal devolution.	--	--	--	Proposed index for horizontal distribution across ULBs based on Population, Area and Backwardness (one-third weight to each of the criteria)

Note: * Madhya Pradesh: 10 percent funds goes to Municipal Corporation that have not received any funds under JNNURM and 5 percent to Municipal Corporations that received such funds; Here, BP stands for Block Panchayats, AP stands for Anchalik Panchayats, PU stands for Panchayat Unions and KP stands for Kshetra Panchayats.

6.2. Grants-in-Aid Recommended by SFCs in Other States

SFCs in other states have recommended a variety of grants to local bodies. The grants recommended by them are summarised in table 14.

Table 14: Grants Recommended by SFCs in Other States

	States	Grants-in-Aid
1	Assam (5th)	Recommended Special purpose grants.
2	Bihar (5th)	Grants to each ZP and PS, Municipal Corporations, Municipal Councils and Nagar Panchayats; Grants for capacity building in RLBs & ULBs. Ratio of Grant between the PRIs and ULBs would be 70:30 in 2015-16 and 60:40 in the subsequent years.
3	Chhattisgarh (3rd)	Recommended annual grants for GPs to strengthen basic services, for developing infrastructure and incentive grants for the installation of water purification plants. Also recommended special grant to GPs and Nagar Palikas where women are elected to more than 2/3rds of the total posts. Recommended cash awards for ULBs based on performance (additional revenue mobilisation, maintaining accounts including asset register and productive and timely use of funds) and on the level of services available in the field of sanitation, street lighting, solid waste management, disposal of wastewater and maintenance of public spaces.
4	Karnataka (4th)	Untied grants to PRIs (Development grants to ZPs and Statutory grants to TPs and GPs) including compensatory grants for the cut in grants by the FC-XV, Untied grants to ULBs for creation of capital assets and to meet expenditure on specific activities of ULBs, Performance grants to better performing LBs, and Establishment grants to newly formed PRIs & ULBs.
5	Madhya Pradesh (4th)	Recommended grant of Rs. 30/- per capita per annum for GPs (based on population census 2011) for maintenance and for works related to improvement of infrastructure, and an annual grant for Block and District Panchayats based on the estimates of the Government.
6	Maharashtra (4th)	The Commission earmarked an Incentive grant of 20% of the total divisible pool of the State for each year for horizontal distribution amongst RLBs and ULBs.
7	Odisha (5th)	Recommended specific purpose grants to both PRIs and ULBs pertaining to Solid Waste Management, Sanitation, drinking water, Capacity building etc. Also recommended earmarked incentive grants for both, GPs and ULBs. The grants was allocated to RLBs based on their performance on (a) revenue generation from their own source and (b) on performance of GPs on some social indicators like education, health etc. The ULBs which achieved a higher rate of growth from own source of revenue than the State's average growth rate were awarded via incentive grants.
8	Punjab (5th)	Recommended that apart from FC-XV grants to GPs, the other two levels of PRIs, i.e., PS and ZPs shall be given an annual grant of Rs. 1 crore. The Commission also recommended performance grants.
9	Rajasthan (5th)	Recommended incentive grants for ULBs and PRIs for registering an increase in their revenues and for timely audit of accounts

	States	Grants-in-Aid
10	Sikkim (5th)	Recommended that 0.5% of the net proceeds should be allocated as Special incentive grant for special support to a certain number of PRIs and ULBs which are constrained by topography as well as inaccessibility and other peculiarities.
11	Tamil Nadu (5th)	A Capital grant fund may be established to replace the IGFF, into which 20% of the aggregate devolution intended for RLBs. 10% of the overall devolution intended for RLBs be credited into a Pooled Fund for Deficit RLBs. 5% of the overall devolution intended for ULBs be impounded into a Pooled Fund for Deficit ULBs subsuming the Operation and Maintenance Gap Filling Fund.
12	Uttar Pradesh (4th)	No specific grants-in-aid recommended by the Commission.
13	Uttarakhand (4th)	Recommended Grants-in-aid to the 25 newly created NPs and 3 newly created NNPs not included in the horizontal share formula of ULBs. Commission recommended Grant-in-aid to each of the three non-elected Panchayats – Badrinath, Kedarnath and Gangotri on annual basis. Recommended other Grants-in-aid to ULBs for developmental needs in the State.
14	West Bengal (4th)	Commission was of the opinion that the idea of an Incentive fund should continue to enthuse the performance of the LBs and, therefore, recommended that 4% of the grant be earmarked as Performance grant from the 2nd year i.e., 2016-17.

Source: SFC Reports of respective states.

7. Survey of Urban Local Bodies – Interaction with Officials of ULBs, Finance Department and Directorate of Urban Local Bodies

The terms of reference of the study required visiting some of the ULBs in Haryana for interaction with the officials to understand the issues faced by them with respect to the flow of SFCs funds to them; are they receiving SFC funds regularly; are these funds untied or they have been tied to some scheme of the government etc. A detailed questionnaire was prepared (see Annexure) and was shared with the selected ULBs prior to visiting them through the Directorate of Urban Local Bodies and the State Finance Commission.

A total of 6 ULBs (2 Municipal Corporations, 2 Municipal Councils and 2 Municipal Committees) were selected for survey – one from each of the six Administrative divisions of Haryana in consultation with the Commission. The list of ULBs selected for survey is presented in table 2 while Fig-1 shows their location in Haryana.

The findings from the survey and our recommendations are as follows:

1) ***Availability of SFC funds (both quantum and frequency) is not known to the ULBs at the beginning of a financial year***. As a result, they are unable to plan for both their expenditure as well as developmental activities in their area.

Recommendation: It is recommended that at the time of the preparation of annual budget or before the start of the fiscal year, the ULBs should be informed about the SFC funds that are likely to be transferred to them (i.e., an indicative amount may be communicated to them) in the fiscal year for which the budget is being prepared. This will enable them to plan better the developmental works and other activities.

2) **There are no conditionalities, other than those recommended by the SFCs, imposed by the Finance Department of the Directorate of Urban Local Bodies for the utilization of SFC funds, nor are the SFC funds subsumed under any State/Central schemes in Haryana**.

   Recommendation: This is a good practice and the Commission must emphasize that this practice should continue in the future also.

3) **SFC funds are spent on developmental activities** like solid waste management, provision of clean sanitation facilities, construction of parks, maintenance of street lights etc. The letter from the Directorate of Urban Local Bodies specifies how these funds are to be spent. However, from 2020-21 onwards the ULBs were directed to spend the SFC funds for payment of salaries, pensions and to cover other establishment costs on account of covid pandemic. This was appreciated by all the surveyed ULBs, however, in the absence of adequate sources of own revenues, especially in case of Municipal Councils and Committees development works have suffered.

   Comments by DULB: DULB had obtained approval for using SFC funds towards payment of salaries, pension and meeting establishment costs of ULBs for 2020-21 and 2021-22 (i.e., the period of pandemic). They feel that this has resulted in an increase in dependence of ULBs on state transfers. With the economy gradually recovering, ULBs need to find ways to raise funds to meet their developmental needs

   Recommendation: While the government is doing its best to address the pandemic and ensuring availability of funds for meeting the salary needs of the ULB staff and other establishment expenses, development woks have suffered for want of funds. ***There is a need to create an earmarked fund (at the state/department level) for addressing such contingencies in future from which local bodies could be supported in times of such exigencies***.

   Further, given low own revenue base of councils and committees, and that CFC funds cannot be used for payment of salaries and meeting establishment expenditures, ***the Commission may consider allowing a certain percent (say 20-30 percent) of its devolution to be spent for meeting such expenditures provided the Councils and Committees show an improvement (say, improvement of 10 percent every year over the audited numbers) in their own revenue/tax collection***.

4) ***Monitoring***: There exists a robust mechanism which ensures the effective and efficient utilization of the funds devolved by the SFC. Each installment is released after the receipt of the Utilization certificate for the previous installment. The projects undertaken by the

local bodies need prior approvals, both at the administrative level as well as the technical level. The limits of each authority are clearly defined and are known to the ULB officials. However, the system is not foolproof as has been pointed out by some of the officials.

Recommendation: Although the monitoring mechanism is clearly specified for all the activities, there is a need to enforce it strictly with stringent checks and balances.

5) **Computerization/Digitization**: While there is some progress on the digitization front, most of the councils still maintain their accounts on paper.

   Recommendation: There is a need for greater digitization/computerization especially at the council and committee level. It is important from the perspective of availing 15th FC local body grants.

6) ***Training***: The officials complained about the lack of training of staff at all levels in the ULBs. There has been no induction training for most of the ULB employees at all levels. This leads to inefficiencies in the working of the ULBs.

   Comments by DULB: It was acknowledged that there is a need for training of employees of ULBs. They are of the view that if any ULB feels the need for training they should write to DULB.

   Recommendation: There is a need for training (including induction training) of ULB staff at all levels on a regular basis. It is recommended that there must be a mandatory training of all the ULB employees on a regular basis.

7) ***There is a shortage of manpower in ULBs with several sanctioned posts lying vacant***.

   Comments by DULB: ULBs have limited manpower, often not equipped to deal with the challenges of the job. There is a need to restructure and augment the current manpower by filling vacant posts and at the same time undertake capacity building of the existing personnel.

   Recommendation: It is recommended that the government should fill up these posts so that the reliance on contractual staff can be minimized. Further, there is a need to restructure the entire administrative set-up routinely to check for posts that may have become redundant and create new ones as per the demands of the ULBs.

8) ***There is a lack of awareness about the SFC and its role etc. among the elected representatives at the ULBs***.

   Recommendation: Given their role in the functioning of the local bodies, it is recommended that there is a need to educate the elected representative of ULBs about SFCs and its role in strengthening local governments, about their role as elected representatives through an induction training (to be conducted after the local body elections). They should also be made aware of the various programmes/schemes of the government that are currently in operation from time to time through regular trainings/workshops.

9) In comparison to municipal corporations, ***committees and councils have limited scope for raising revenues***. However, their expenditure requirements are much higher relative to their revenue generating capacity. As a result their dependence on the transfers from higher level of governments (both state and union government) is much higher.

Comments by DULB: ULBs do suffer from lack of resources to generate revenues resulting in insufficiency of funds. They suffer on account of (a) quality of resources at their disposal and (b) the scope of expanding their revenue by levying additional taxes.

Recommendation: There is a need to devolve relatively more funds from the State Finance Commission to the ULBs, especially to the Municipal Councils and Municipal Committees as their own source of revenues are limited. They are constrained in terms of their relative ability to raise revenues from their own sources of funds as there is limited scope to levy additional taxes.

10) With rapid urbanisation the urban boundaries of the ULBs have expanded and they have to provide services in such peri-urban areas also. It was pointed out by many ULBs that while deciding the share of individual ULBs more weightage be given to Area. They felt that the share of Area be increased to 30 percent at least from the current weight of 20 percent and the weight of Population be reduced to 70 percent from the current 80 percent.

Discussion with the Department of Finance, Government of Haryana: It was pointed out that the funds released to local bodies based on the recommendations of the SFC do not carry any additional conditions and are not subsumed under any of the schemes launched by the state government. The Finance department has not put any additional conditions/guidelines in the release and utilisation of SFC funds by local bodies. A single order is issued by the Finance Department for the release of funds to local bodies. The provision is made under the budget heads 2215 and 2216 for RLBs and ULBs respectively. This amount is then transferred to the DULB who works out the share of each of the ULBs and release the funds quarterly. The Finance Department does not have any role in the disbursal of funds to the individual ULBs.

It was further pointed out that the 5^{th} SFC recommended devolving 7 percent of the Net SOTR to the local bodies. The amount to be transferred to the local bodies every year is calculated based on the budget estimates for that year. Adjustments are made once the Revised Estimates become available and again when the Actuals numbers are known. ***Given the actual numbers would be very different from the Budget or Revised Estimates, the hon'ble CM had directed the Finance Department for using actual data and not the budget or revised estimates for calculating the funds to be transferred to local bodies. In other words, the funds to be transferred to local bodies in period t is calculated using figures of net State's Own Tax revenue in period (t-2) i.e., using audited number/Actuals of net SOTR.***

Discussion with the Directorate of Urban Local Bodies (DULB), Government of Haryana:
Our interaction with the DULB can be summarised as follows:

a) ULBs need to work towards strengthening their own sources of revenue. DULB had worked on obtaining an exclusive approval to use the funds devolved by the SFC in the past 2 years (i.e., during the period of the pandemic) to cover salaries and establishment costs of the ULBs. However, this has increased their dependence. Now that the economy is on the road to recovery, ULBs need to find ways to raise funds to meet their developmental needs.

b) Funds are disbursed as per the submission of Utilization Certificate by the ULBs. Subsequent installments are contingent on the demand raised by the ULB.

c) It was acknowledged that there is a need to train the employees at the ULBs. They are of the view that if any ULB feels that there is a need for training, they should write to DULB or HIPA for scheduling the same.

d) ULBs do suffer from lack of resources to generate revenues resulting in insufficiency of funds. They suffer on both accounts - in terms of the quality of resources at their disposal and the scope of expanding their revenue by levying additional taxes.

e) ULBs have limited manpower, often not equipped to deal with the challenges of the job. Therefore, there is a need to restructure and augment the current manpower by filling vacant posts and at the same time undertake capacity building of the existing personnel.

8. Fifteenth Finance Commission Local Body Grants to Haryana (2021-22 to 2025-26)

The Fifteenth Finance Commission in its report for the period 2021-22 to 2025-26 recommended grants of Rs. 4,36,361 crore for local governments. Of the total local body grants, Rs. 8,000 crore is performance-based grants meant for incubation of new cities and Rs. 450 crore is for shared municipal services[8]. In view of the current pandemic, the Commission has provided a grant of Rs. 70,051 crore to strengthen and plug the critical gaps in the health care system at the primary health care level. This grant is to be channelized through the local governments.

The remaining grant of Rs. 3,57,860 crores is to be distributed among rural and urban local bodies. The distribution between rural and urban local bodies is in the ratio of 67:33 in 2021-22 and 2022- 23; 66:34 in 2023-24 and 2024-25; and 65:35 in 2025-26. The Commission recommended Rs. 2,36,805 crore for duly constituted rural local bodies and Rs.1,21,055 for urban local bodies for the period 2021-26. The year-wise details of different components of

[8] Ministry of Housing and Urban Affairs (MoH&UA) in consultation and with the concurrence of Department of Expenditure, Ministry of Finance will issue separate guidelines/modalities for operationalizing/implementing the recommendations on Shared Municipal Services grants and incubation of new cities.

grants to local bodies is presented in table 15.

Table 15: Grants to Local Governments

(Rs. crore)

	Local Body Grants	2021-22	2022-23	2023-24	2024-25	2025-26	2021-26
1	Total grants for RLBs & ULBs (a+b)	80207	82613	85091	89997	90003	**427911**
a)	Grants for primary health sector	13192	13192	13851	14544	15272	**70051**
b)	Other grants to be disbursed among local bodies excluding (a) [(i) + (ii)]	67015	69421	71240	75453	74731	**357860**
(i)	Grants for RLBs	44901	46513	47018	49800	48573	**236805**
(ii)	Grants for ULBs	22114	22908	24222	25653	26158	**121055**
2	Grants for incubation of new cities	--	2000	2000	2000	2000	**8000**
3	Grants for shared municipal services	90	90	90	90	90	**450**
4	**Total Local Body Grants (1+2+3)**	**80297**	**84703**	**87181**	**92087**	**92093**	**436361**

Source: Report of the Fifteenth Finance Commission

8.1. Grants for Rural Local Bodies in Haryana

A total of Rs. 2,36,805 crore is recommended for duly constituted rural local bodies for the period 2021-22 to 2025-26. The inter se distribution amongst the States is based on a weight of 90 percent on population (2011 census population) and 10 percent on the area of the states. Using the above inter se distribution criteria, rural local bodies' share in Haryana works out to 2.08 percent. Multiplying total grants to rural local bodies for each of the year as given in table 15 by Haryana's share of RLBs, we get year-wise total grants for RLBs for the state (table 16).

Table 16: Calculation of RLB grants for Haryana

	2021-22	2022-23	2023-24	2024-25	2025-26	2021-26
Total Grants for RLBs (Rs. crore)	44901	46513	47018	49800	48573	236805
Haryana's local body share (%) as calculated by 15th FC	2.08	2.08	2.08	2.08	2.08	--
RLB grants for Haryana (Rs. crore) = *(Total Grants for RLBs)*(HR's share)*	935	968	979	1036	1011	4929

Source: Report of the Fifteenth Finance Commission

All the three tiers of panchayats – village, block and district – shall receive the grants meant for RLBs. The inter se distribution among the three tiers should be done by the State Government on the basis of the accepted recommendations of the latest SFC and in conformity with the following bands of

(a) not less than 70 per cent and not more than 85 per cent for Gram Panchayats,

(b) not less than 10 per cent and not more than 25 per cent for Block Panchayats and

(c) not less than 5 per cent and not more than 15 per cent for Zilla Panchayats, subject to the shares adding up to 100 per cent.

In the event of SFC recommendations not being available, the inter se distribution within the tiers is to be decided by the State Government within the bands indicated above.

Once the State-level grants are earmarked for each tier, the intra-tier distribution among the relevant entities across the State should be on the basis of population and area in the ratio of 90:10 or as per the accepted recommendations of the latest SFC.

Entry-level Condition for availing the grants for RLBs: To avail the local body grants, the Commission had recommended entry level conditions.

The Commission recommended the online availability of both, the provisional accounts of the previous year and the audited accounts of the year before previous as an entry level condition to avail the grants.

1) **For 2021-22 and 2022-23**: In the first two years of the award period of the Commission, States need to ensure that at least 25 percent of the rural local bodies have both their provisional accounts for the previous year and audited accounts for the year before the previous available online in the public domain in order for them to avail the full grants in that year.
2) **For 2023-24, 2024-25 and 2025-26**: From the third year (i.e., 2023-24) onwards, States will receive total grants due to rural local bodies having both provisional accounts of the previous year and audited accounts for the year before previous and making these available online. For example, if for a particular State only 35 percent of rural local bodies have both provisional accounts for the year 2022-23 and audited accounts for the year 2021-22 and these are available online in 2023-24, then in 2023-24, the State will receive total amount due to these 35 percent of rural local bodies for the year 2023-24.

The Commission further recommended that States which have not constituted their SFCs must constitute SFCs, act upon their recommendations and lay the explanatory memorandum as to the action taken thereon before the State legislature on or before March 2024. After March 2024, no grants should be released to a State that has not complied with the Constitutional provisions in respect of the SFC and these conditions. The Ministry of Panchayati Raj (MoPR) will certify the compliance of all Constitutional provisions by a State in this respect before the release of their share of grants for2024-25 and 2025-26.

The total grants to rural local bodies are further subdivided into

A. Basic Grant - RLBs

- 40 percent of the total grants to be disbursed to rural local bodies shall be untied and can be used by them for felt needs under the twenty-nine subjects enshrined in the Eleventh Schedule, except for salaries and other establishment costs. The expenditure required for auditing of accounts by external agencies approved by the State Government, however, maybe borne from this grant.

B. Tied Grants for National Priorities - RLBs

- 30 percent of the total grants to be disbursed to rural local bodies shall be earmarked for drinking water, rainwater harvesting and water recycling.

- 30 percent of the total grants to be disbursed to rural local bodies shall be earmarked for sanitation and maintenance of ODF status, and this should include management and treatment of household waste, and human excreta and faecal sludge management in particular.

However, if any local body has fully saturated the needs of one category and does not require funds for that purpose, it can utilise the funds for the other category. For example, if a local body saturates its requirement for drinking water, it can utilise the funds for ODF and vice-versa. The respective village assembly/Gram Sabha shall certify this and it will be duly confirmed by the supervising authority of the panchayats or the State Government.

8.2. Grants for Urban Local Bodies in Haryana

In view of the country's differentiated urbanisation pattern, the Commission accorded differential treatment to urban agglomerations with more than one million population relative to other urban areas in the distribution of urban local body grants. Accordingly, urban areas are grouped into two broad categories for recommending grants to urban local bodies:

a) Category-I cities: urban agglomerations/cities with more than one million population and

b) Category-II cities: other than million-plus cities.

A total of Rs. 1,21,055 crore is recommended for urban local bodies for the period 2021-26. Inter-se distribution among states is on the basis of a weightage of 90 percent on population and 10 percent on area. Using this inter se distribution criteria, Haryana's share of local bodies works out to 2.08% (refer to Annex Table 7.3 of 15th FC Report). Multiplying total grants to ULBs for each of the year by Haryana's share of local bodies we get year-wise total grants for ULBs for the state (table 17). The urban local body grants are then to be further distributed among Category-I and Category- II cities in the state.

Table 17: Calculation of ULB grants for Haryana

	2021-22	2022-23	2023-24	2024-25	2025-26	2021-26
Total Grants for ULBs (Rs. crore)	22114	22908	24222	25653	26158	121055
Haryana's local body share (in %) as calculated by 15th FC	2.08	2.08	2.08	2.08	2.08	--
ULB grants for Haryana (Rs. crore) = *(Total Grants for RLBs)*(HR's share)*	461	477	504	534	544	2520

Source: Report of the Fifteenth Finance Commission

Entry-level Condition for availing the grants for ULBs: In order to be eligible for grants, the urban local bodies have to mandatorily prepare and make available online in the public domain (i) annual accounts of the previous year and (ii) duly audited accounts of the year before that. Such audited accounts should include the minimum of a) balance sheet; b) income and expenditure statement; c) cash flow statement; and d) schedules to balance sheet, income and expenditure statement and cash flow statement.

Further the provisional annual accounts of a particular year shall be available online in real time basis by 15 May of every subsequent year. For example, the online provisional annual accounts for the year 2020-21 shall be available by 15 May 2021.

1) **For 2021-22 and 2022-23**: In the first two years of the Commission's award period, states need to ensure that at least 25 percent of the urban local bodies have both their provisional accounts for the previous year and audited accounts for the year before that available online in the public domain in order for them to avail the full grants in that year.

   Additionally, the States are also expected to notify the floor rates of property tax and operationalize the relevant arrangements in 2021-22.

2) **For 2023-24, 2024-25 and 2025-26**: From the third year (i.e., 2023-24) onwards, States will receive total grants due to the urban local bodies having both provisional accounts of the previous year and audited accounts for the year before that and making these available online. For example, if for a particular State only 35 percent of urban local bodies have both provisional accounts for the year 2022-23 and audited accounts for the year 2021-22 and these are available online in 2023-24, then in 2023-24, the State will receive total amount due to these 35 percent of urban local bodies for the year 2023-24 only.

   The Commission had recommended that the provisional annual accounts of a particular year shall be available online in real time basis by 15 May of every subsequent year. In other words to online provisional annual accounts for the year 2020-21 shall be available by 15 May 2021. However, the operational guidelines require that for the years 2021-22 and 2022-23, the ULBs should make available the unaudited accounts of the previous year and audited accounts for the year before the previous by 15 August for availing the full grants. However, for the remaining three years i.e., from 2023-24 to 2025-26 that have to make these accounts available by 15 May each year

The condition of notifying the floor rates of property tax will apply for eligibility of grants from 2022-23. Once the floor is notified, the condition of growth in property tax collection being at least as much as the simple average growth rate of the State's own GSDP in the most recentfive years will be measured and taken into account from 2023-24 onwards.

For example, if Haryana has duly notified a floor to the property tax rates in 2021-22, it becomes eligible for getting the entire urban local body grants in 2022-23. But for 2023-24 and onwards it has to meet the second condition of improvement in property tax collection in tandem with the growth rate of the State's own GSDP as well. The growth rate to be achieved in property tax revenue in a particular year will be taken as the simple average of GSDP growth available for the most recent five years. Thus, to qualify under this conditionality in 2023-24, the average GSDP growth rate for the period 2017-18 to 2021-22 (provisional or final, whichever is available at the beginning of the year) will be used for calculating the growth in property taxes that has to be achieved in 2022-23. The State will become eligible for grants in 2023-24 only if the urban local bodies have met the condition of actual collections of property tax in tandem with the State's own GSDP growth.

Further, if, in 2023-24, only 25 per cent of the urban local bodies have met the second condition of consistent improvement in collection in tandem with the growth rate of State's own GSDP, then the State will receive the total amount due to these 25 per cent urban local bodies in 2023-24. If, in 2024-25, 35 per cent of the urban local bodies have met the condition of consistent improvement in collection in tandem with the growth rate of State's own GSDP, the State will then receive the cumulative amount due to these 35 per cent of the entitled urban local body grants in 2024-25. However, it may be noted that the State will receive no grant in any of the years, if it has not notified the minimum floor rate.

In addition to these entry level conditions for availing the local body grants for ULBs, the operational guidelines have added some more. These are

(i) Each state government and each Category-I city/town shall sign a tripartite MoU with MoH&UA to be placed in public domain including the ***www.city.finance.in*** portal. The MoU will contain baseline (i.e., as on 1 April 2021) service level benchmarks, annual targets/outcomes and incentive for achieving the targets for water supply, water conservation measures and solid waste management and sustaining outcomes for Swachh Bharat Mission. It will be one of the pre-conditions for determining eligibility for release of funds from 2021-22 onwards.

(ii) Linking of ULB account for the 15FC grant with PFMS or with any other e-governance system fully integrated with the PFMS will be a pre-condition for release of grant from 2022-23.

8.2.1. Grants for Million-Plus Cities (MPCs)/ Towns

The million-plus cities as categorized by the Commission are the Category-I cities that comprise 50 urban centers with million plus population. For these Category-I cities the Commission has recommended a grant of Rs.38196 crores over its five year award period in the form of a Million-Plus Challenge Fund (MCF) which would be linked to performance of these cities in improving their air quality (which is critical not only for the health and wee-being of those living in these cities but also for attracting investment) and meeting the service level benchmarks for urban drinking water supply (including rainwater recycling and recycling), sanitation and solid waste management.

One-third of the total MCF of each city is earmarked for achieving ambient air quality. The balance two-third of the city-wise MCF is earmarked for achieving service level benchmarks for drinking water (including rainwater harvesting and recycling) and solid waste management.

Faridabad is the only million-plus city in Haryana. The year-wise distribution of the total grants meant for Million-plus cities and those for Faridabad is presented in table 18.

Table 18: Grants for Million-Plus/Category-I Cities

(Rs. crore)

	2021-22	2022-23	2023-24	2024-25	2025-26	2021-26
Total Grants for Million-Plus Cities	**6978**	**7227**	**7643**	**8093**	**8255**	**38196**
a) Ambient Air Quality	2217	2299	2431	2571	2621	12139
b) Service Level Benchmark	4761	4928	5212	5522	5634	26057
MPC Grant for Faridabad, Haryana	**74**	**76**	**81**	**85**	**87**	**403**
a) Air quality	25	25	27	28	29	134
b) SWM and sanitation	49	51	54	57	58	269

Source: Report of the Fifteenth Finance Commission

For monitoring ambient air quality and disbursing grants to Million-Plus cities, the Ministry of Environment Forests and Climate Change (MoEF&CC) will be the nodal ministry. The Ministry will develop city-wise and year-wise targets on ambient air quality, based on measurable indicators and outcomes in consultation with respective State Governments and will recommend distribution of Ambient Air Quality grants to the eligible MPC/Urban Agglomerations (UAs). It will also recommend proportional distribution of undistributed portion of the grants to the performing MPCs/UAs. The guidelines for the same will be issued by the MoEF&CC.

For drinking water (including rainwater harvesting and recycling) and sanitation and solid waste management criteria under service level benchmarks, the Ministry of Housing and Urban Affairs (MoH&UA) shall be the nodal ministry for determining the eligible urban local bodies. According to the operational guidelines, the grants will be based on the performance of MPCs/UAs in (a) solid waste management, (b) quality water supply, (c) water conservation, (d) water recycling and (e) rejuvenation of water bodies. The grants will be distributed based on the marks obtained based on their performance in water supply and sanitation (there are 4 service level indicators) and in solid waste management (there are 4 service level indicators). The details are spelt out in the operational guidelines. The undistributed portion of the solid waste management grant of Category-I cities shall be distributed by MoH&UA to cities/UAs in Category-II (i.e., non-million plus cities) in proportion to their 2011 census population.

For availing grants the Million plus cities/UAs are required to publish annually all 28 Service level benchmarks and targets for the year online on the portal ***www.city.finance.in***. Moreover, they are also required to submit detailed report on the measures/projects undertaken along with the progress and milestones achieved for recycling and reuse of waste water, rejuvenation of water bodies and water supply.

8.2.2. Grants for Other Than Million-Plus Cities/ Towns

The 15th FC recommended a basic grant of Rs. 82,859 crore for a period of five years for non-million plus cities/Category-II cities/towns. The share of category-II cities in Haryana is Rs.

2117 crore spread over the five year award period of the Commission. Intra-city distribution of these grants shall be on the basis of recommendations of the latest SFC. In case the SFC recommendation is not available for distribution within a particular category, allocations should be based on population and area in the ratio of 90:10. Year-wise distribution is shown in table 19.

It has be mentioned in the operational guidelines that some cities and towns falling under Category-II cities may be part of some urban agglomeration, but they will still receive grants under Category-II cities component as for the Million Plus Cities Challenge fund would be an additionality.

Table 19: Grants for Non-Million-Plus Cities/Category-II Cities/Towns

(Rs. crore)

	2021-22	2022-23	2023-24	2024-25	2025-26	2021-26
Total Grants for Category-II Cities	15136	15681	16579	17560	17903	82859
Grants for Category-II Cities in Haryana	387	401	423	449	457	2117
• Untied Grants (40%)	155	160	169	180	183	847
• Tied Grants (60%)	232	241	254	269	274	1270

Source: Report of the Fifteenth Finance Commission

Untied Basic Grants: Of the basic grants recommended to other than Million-Plus cities, 40 percent (Rs. 847 crore) is untied and can be used by the urban local bodies for felt needs under the eighteen subjects enshrined in the Twelfth Schedule, except for salaries and other establishment costs.

Tied Grants: The remaining 60 percent of the grants (Rs. 1270 crore) are tied and are to be used for supporting and strengthening the delivery of basic services. These tied grants should be used for

- 30 percent to be disbursed to urban local bodies shall be earmarked for sanitation and solid waste management and attainment of star ratings as developed by MoH&UA. This should include management and treatment of household waste, in particular human excreta and faecal sludge.
- 30 percent of the total grants to be disbursed to urban local bodies shall be earmarked for drinking water, rainwater harvesting and water recycling.

However, if any urban local body has fully saturated the needs of one category and there is no requirement of funds for that purpose, it can utilize the funds for the other category. Such saturation will also be certified by the respective urban local body and duly confirmed by the supervising authority of municipalities in the State Government. The Commission also recommended that no further conditions or directions other than those already indicated by it should be imposed either by the Union or the State Governments, or any authority, for releasing the funds.

As per the operational guidelines, MoH&UA will recommend release of tied grants for both solid waste management and drinking water & waste water management system components based on information of publication of baseline data, annual targets till 2025-26 and annual achievements thereof, fund utilization under each component progress achieved during the year for attainment of star ratings in comparison with the baseline data on the ***city.finance.in*** portal. Although, achievement of target is not a mandatory condition for release of this grants, but those non-million plus cities that achieve the targets for previous years will be eligible for receiving the undistributed portion on grants meant for million plus cities, in proportion to their 2011 census population.

Grants to Cantonment Boards: Because of their similarity with municipalities, the 15th Finance Commission pointed out that State Governments, while deciding the share of basic grants among ULBs in non-Million-Plus cities, should allot grants on population basis for the Cantonment Boards falling within their territory and conditions applicable to other urban local bodies will also apply to the Cantonment Boards. ***As per the operational guidelines whenever population is used for distribution of grants, 2011 census population numbers should be used***. Haryana has one cantonment board, Ambala.

8.3. Timely Release of Grants

The grants for rural local bodies and non-Million-Plus cities shall be released in two equal instalments each year in June and October, after ascertaining the entry level benchmarks and other requirements recommended by Commission. However, as per the operational guidelines issues by the Department of Expenditure Ministry of Finance, for Category-I cities the grants will be released in one installment every year based on the recommendations of the nodal ministry and subject to fulfillment of the stipulated conditions.

The States shall transfer grants-in-aid to the local governments within ten working days of having received them from the Union Government. Any delay beyond ten working days shall require the State Governments to release the same with interest as per the effective rate of interest on market borrowings/State Development Loans (SDLs) for the previous year.

8.4. Grants for Health (to be channelized through Local Governments)

The Commission provided grants earmarked for the third tier for support to primary healthcare. It identified interventions that will directly lead to strengthening the primary health infrastructure and facilities in both rural and urban areas. These include (1) Support for diagnostic infrastructure to the primary healthcare facilities (in in sub centers, PHCs and urban PHCs), (2) Support to Block level public health unit, (3) Support for setting of Urban Health and Wellness Centers, (4) Support for necessary infrastructure to Building-less Sub centers, PHCs, CHCs, and (5) Provide support for necessary infrastructure for the conversion of rural PHCs and sub centres into Health and Wellness Centre.

A sum of Rs. 70,051 crore out of the grants for local governments have been earmarked by the Commission for the health sector at the rural and urban local body levels during its award period from 2021-22 to 2025-26. For the state of Haryana, the amount of health grant recommended by the Commission for rural and urban local bodies is Rs. 1617 crore. The component-wise health grant for Haryana is presented in table 20.

Table 20: Year-wise Health Grants through Local Bodies (Haryana)

(*Rs. crore*)

	2021-22	2022-23	2023-24	2024-25	2025-26	Total
Health Grant (i to vii)	**305.00**	**305.00**	**320.00**	**335.00**	**352.00**	**1617.00**
i) Support for Diagnostic Infrastructure to Primary Health Sub Centre	25.48	25.48	26.75	28.09	29.49	**135.29**
ii) Support for Diagnostic Infrastructure to PHCs	28.05	28.05	29.45	30.64	32.40	**148.59**
iii) Support for Urban Primary Health Centre(UPHCs)	7.01	7.01	7.36	7.73	8.12	**37.23**
iv) Financial Requirement for establishing Block Level Public Health Units	28.58	28.58	30.00	31.50	33.08	**151.74**
v) Grants for Urban Health and Wellness Centres (UHWCs)	139.33	139.33	146.30	153.62	161.30	**739.88**
vi) Grants for Building-less Sub-centres, PHCs, CHCs	29.51	29.51	30.97	32.53	34.15	**156.67**
vii) Financial requirement for conversion of Rural PHCs and SCs into Health and Wellness Centre	46.61	46.61	48.94	51.38	53.95	**247.49**

Source: Report of the Fifteenth Finance Commission

Note: Sum of components may not match with corresponding totals because of rounding off.

For Haryana the total local body grants recommended by the 15th Finance Commission works out to Rs. 9066 crore for the period 2021-26. The year-wise and component-wise break-up is presented in table 21.

Table 21: Year-wise grants to Local Bodies (Rural & Urban) in Haryana

(*Rs. crore*)

		2021-22	2022-23	2023-24	2024-25	2025-26	2021-26
1	**RLB**	**935.00**	**968.00**	**979.00**	**1036.00**	**1011.00**	**4929.00**
	(i) Untied Grant (40%)	374.00	387.00	392.00	414.00	404.00	1972.00
	(ii) Tied Grant (60%)	561.00	581.00	587.00	622.00	607.00	2957.00
2	**ULB (a+b)**	**461.00**	**477.00**	**504.00**	**534.00**	**544.00**	**2520.00**
	a) Category 1 (million plus cities)	74.00	76.00	81.00	85.00	87.00	403.00
	b) Category II (non-million plus cities)	387.00	401.00	423.00	449.00	457.00	2117.00
	(iii) Untied Grant (40%)	155.00	160.00	169.00	180.00	183.00	847.00
	(iv) Tied Grant (60%)	232.00	241.00	254.00	269.00	274.00	1270.00
3	**Health Grant** (i to vii)	**305.00**	**305.00**	**320.00**	**335.00**	**352.00**	**1617.00**
4	**Total Grants (1+2+3)**	**1701.00**	**1750.00**	**1803.00**	**1905.00**	**1907.00**	**9066.00**

Source: Report of the Fifteenth Finance Commission for 2021-26

Note: Sum of components may not match with corresponding totals because of rounding off.

Although 15FC has recommended a much higher quantum as local body grants but a large percentage of it is performance/conditional/tied grants. The share of untied local body grants recommended by the Commission is much lower than that recommended by 13FC and 14FC. In case of Haryana, the share of untied grants works out to 37.84 percent of aggregate local body grants meant for the state (excluding those for health and on the assumption that the entry level conditions are met). If one were to consider health grants as untied grants, the share of untied would increase to about 48.92 percent.

As per the information from the Finance Department, Government of Haryana, in the current fiscal year 2021-22 (till mid October 2021) Rs. 218 crores has been released to Haryana as part of the 15^{th} Finance Commission's ULB grants. This includes Rs. 24 crore for Faridabad which is the only Million-plus city in the state.

9. Discussion and Study Recommendations

SFCs in Haryana have been constituted on regular basis. The first SFC was constituted on 31 May 1994. The subsequent SFCs were constituted at regular five year intervals with the 6^{th} SFC being constituted on 22 September 2020. It is required to make recommendations for the five year period 2021-22 to 2025-26.

We find that the SFCs in Haryana have taken considerable time in submitting their report. With the exception of the Fifth SFC, all the other SFCs took around 34 months or more to submit their reports. In the case of the 2nd and 4th SFCs, almost the entire award period had passed by the time the report was submitted by the Commissions. The term of the Commissions were extended by the State Government by giving multiple extensions without considering the award period of the Commissions. ***It is recommended that while giving extension(s) to the Commission, the government should keep in mind the award period for which the Commission has to make its recommendations.***

One of the reasons for SFCs taking considerable amount of time to submit their report is non-availability of records of previous Commissions. Considerable time is lost in re-designing questionnaires and other information formats to collect primary and secondary data and information. ***It is recommended that a permanent SFC cell be set up in the Finance Department. The proposed SFC cell apart from overseeing the implementation of the recommendations of the SFC can act as the repository of data and information collected by SFCs. Whenever a new SFC is constituted it will have access to this database.***

Government of Haryana has taken about a year or less to table the Action Taken Report in the State Legislature, except in the case of the 1^{st} and 2^{nd} SFCs where time taken was 3 years and 5 months and 1 year and 4 months respectively. It is observed that in the case of all five SFCs of Haryana, the ATR was submitted after the commencement of the award period and in the case of 1st, 2nd and 4th SFCs it was submitted in the final year of the award period of the Commission implying that the entire 5 years of the award period was not available for implementing the recommendations of the Commission.

As regards the recommendations of the SFCs are concerned, the State government has largely accepted (with or without modifications) recommendations of the SFCs. However, none of the recommendations of the 4th SFC were accepted by the government on account of delayed submission of the report. The government continued to transfer resources to local bodies based on the recommendations of the 3rd SFC during 2010-11 to 2015-16 which was the award period of the 4th SFC.

Examination of the reports of the SFCs of Haryana and the Action Taken Reports tabled by the government we observe some discrepancies with regards to the status of acceptance and implementation of some of the recommendations of the SFCs. Whether the accepted recommendations have been implemented or not is also not known. Review of the reports of the SFCs of Haryana reveal that while certain recommendations have been accepted by the state government as per the ATR tabled before the legislative assembly, the subsequent SFC reports point out that these recommendations have not been implemented. ***To address these issues we recommend constitution of a Vidhan Sabha Committee for local bodies, which will review the status of the accepted recommendations from time to time and ensure that they are implemented. We also recommend that the state government submit every year the action taken report to the proposed Vidhan Sabha Committee for local bodies, updating the status of implementation of SFC's recommendations***.

There has been a gradual increase in per capita actual devolution to local bodies in Haryana. The per capita devolution show an increase (in real terms) from Rs. 297.57 in 2006-07 to Rs. 1119.77 in 2017-18 there after declining to about Rs. 659.20 in 2020-21RE. The average per capita devolution (at constant 2011-12 prices) during the award period of the Third SFC was Rs. 248.59 which increased to Rs. 561.90 during the award period of Fourth SFC[9], and further to Rs. 735.45 during the award period of the Fifth SFC. In 2021-22, the per capita devolution to local bodies, as per the budget estimates presented by the state government, works out to Rs. 747.48.

Recommendations based on Survey Findings*:* Availability of SFC funds (both quantum and frequency) is not known to the ULBs at the beginning of a financial year. ***It is recommended that at the time of preparation of annual budget or before the start of the fiscal year, the ULBs should be informed about the quantum SFC funds that are likely to be transferred to them (i.e., an indicative amount may be communicated to them) in the fiscal year for which the budget is being prepared.*** This will enable them to plan their developmental works and other activities.

There is a need for greater digitization/computerization especially at the council and committee level. It is important from the perspective of availing 15th FC local body grants.

[9] The award period of the Fourth SFC was from 2011-12 to 2015-16. As the recommendations of the 4th SFC was not accepted by the Government and the recommendations of the 3rd SFC was continued during this period of the 4th SFC.

Although the monitoring mechanism is clearly specified for all the activities, there is a need to enforce it strictly with stringent checks and balances.

Capacity building/Training of ULB staff: There is a need for training of the staff at all levels in the ULBs on a regular basis. It is recommended that there must be a mandatory training of all the ULB employees on a regular basis.

Capacity building of elected representatives: Given their role in the functioning of the local bodies, it is recommended that there is a need to educate the elected representative of ULBs about SFC and its role in strengthening local governments, about their role as elected representatives through an induction training (to be conducted after the local body elections). They should also be made aware of the various programmes/schemes of the government that are currently in operation from time to time through regular trainings/workshops.

Shortage of manpower in ULBs with several sanctioned posts lying vacant: It is recommended that the government should fill up vacant posts in the ULBs so that the reliance on contractual staff can be minimized. Further, there is a need to restructure the entire administrative set-up routinely to check for posts that may have become redundant and create new ones as per the demands of the ULBs.

There is a need to devolve relatively more funds from the State Finance Commission to the ULBs, especially to the Municipal Councils and Municipal Committees as their own source of revenues are limited. They are constrained in terms of their relative ability to raise revenues from their own sources of funds as there is limited scope to levy additional taxes.

Recommendations about the Scheme of Devolution: SFCs in Haryana have used two approaches for sharing revenues with local bodies (a) Sharing of specific taxes and duties (1st and 2nd SFCs, Haryana), and (b) Global sharing of state revenues (3rd, 4th and 5th SFCs Haryana). The global sharing of taxes has advantages as it increases transparency, objectivity, and certainty and shares the buoyancy of state taxes directly with the local bodies. This enables them to plan their priorities in advance as the divisible pool becomes consistent and predictable. ***We recommend that the 6th SFC should also consider using global sharing of resources in its devolution scheme, sharing a percentage of gross SOTR net of cost of collection with the local bodies.***

The 3rd SFC recommended sharing 4 percent of SOTR net of LADT, revenues from state excise and 1.25 percent towards collection cost with the local bodies. The 4th SFC recommended sharing 2.5 percent of SOTR (inclusive of shared taxes) net of 2 percent as cost of collections with the local bodies for the period 2011-12 to 2014-15 along with sharing proceeds from the shared taxes. However, for 2015-16 it recommended sharing 7 percent of SOTR net of Stamp Duty and 2 percent as cost of collections with the local bodies. The 5th SFC also recommended sharing 7 percent of divisible pool with the local bodies during its award period.

Local governments are entrusted with relatively large expenditure responsibilities, but are not delegated with adequate financial resources, and political (and administrative) power which affect their functioning. It is important that local governments be strengthened not only financially but also administratively so as to ensure their smooth functioning. Furthermore, the pandemic has disrupted State finances considerably and will adversely impact devolution to local governments. ***Recognizing the role played by local governments in addressing the pandemic, the Commission may consider recommending measures to strengthen them. We are of the view that the Commission should consider sharing 7.5 of the net SOTR during 2021-22 to 2023-24 with the local bodies and increasing it to 8 percent of net SOTR during 2024-25 and 2025-26. Net SOTR is defined as Gross SOTR minus 1.5 percent of SOTR as cost of collection[10]. The total transfers in inclusive of grants-in-aid recommended by the Commission.***

We further recommend that the funds to be transferred to local bodies in period t should be calculated using Actuals of net State's Own Tax revenue in period (t-2) to avoid multiple readjustments in the transfer if resources to local bodies. The Hon'ble CM has also directed the Finance Department of follow the same.

From the review of latest available SFC reports of other states we find that that they have used a variety of indicators including 2011 census population ratio, projected population ratio to derive the rural-urban share. SFC in many states acknowledging the increase in urbanization have stressed on the need for devolving more funds to ULBs***. In keeping with the growing urbanisation in Haryana we are of the view that the Commission may keep this sharing ratio same as that recommended by the 5th SFC. The recommended devolution may be shared between the RLBs and ULBs in the ratio of 50:50.***

As per the 2011 census, the ratio of population between Municipal Corporation, Municipal Council and Municipal Committee is 56.96:26.85:16.19. From our field survey we find that Councils and Committees have limited sources of own revenues and the scope for raising resources from other non-tax sources is also limited relative to the Municipal Corporations. Given their expenditure responsibilities they require higher transfers from the Commission. ***We suggest that further distribution of ULB share between Municipal Corporation, Municipal Council and Municipal Committees the Commission should done in the ratio of 50:30:20 between Corporations, Councils and Committees. Further distribution among individual tiers should be on the basis of Population and Area in the ratio of 75:25.***

The Fifteenth Finance Commission in its report for the period 2021-22 to 2025-26 recommended grants of Rs.4,36,361 crore for local governments. In view of the current pandemic, the Commission has provided a grant of Rs.70,051 crore to strengthen and plug the critical gaps in the health care system at the primary health care level. This grant is to be channelized through the local governments. The share for Haryana works out to Rs.9066 crore

[10] The average cost of collection for the period 2019-20 to 2021-22BE works out to 1.27 percent of SOTR.

for the award period of the Commission, of which Rs. 1617 crore is the quantum of health grant.

Although the 15th Finance Commission has recommended a much higher quantum as local body grants but a large percentage of it is performance/conditional/tied grants. The share of untied local body grants recommended by the 15th Finance Commission is much lower than that recommended by the 13th and 14th Finance Commissions. In case of Haryana, the share of untied grants works out to 37.84 percent of aggregate local body grants meant for the state (excluding those for health and on the assumption that the entry level conditions are met). If one were to consider health grants as untied grants, the share of untied would increase to about 48.92 percent.

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Annexure

Questionnaire

Study for the 6th SFC of Haryana

Devolution of funds to ULBs under State Finance Commissions in Haryana: A critical review

Name of the ULB:

Date of Survey:

Names of the Officers:

1) A) Are you aware how much funds (or share in % terms) will your ULBs will receive during the award period of a SFC?

   B) When do you get to know in any financial year how much funds your ULB is entitled to?

   C) Do you know in the beginning of the financial year how much funds your ULB is entitled to?

2) Quantum and Time of release of SFC grants (Information from 2011-12 onwards i.e., award period of the 4th and 5th SFCs) – please provide details including office orders of release of installments by the department.

3) Was there a different between the funds allocated and the funds actually received in any financial year? It yes please provide year-wise details from 2011-12 onwards?

4) What could be, in your opinion, the reasons for such difference in the funds allotted and those released (assuming that the entire allocated fund was not released).

5) A) Did the SFC impose any conditions in the release and utilization of the funds for ULBs? If yes, please provide details.

   B) Are you aware of any such conditionalities imposed by SFC in the release of funds?

6) Was the devolution of SFC funds untied or were there any conditions imposed by the Finance Department or Directorate of ULBs or any other department in the release and utilization of the 5th SFC devolution fund? Please provide details.

7) Was the nature of SFC transfers changed from untied or general purpose transfers to conditional or specific purpose grants/transfers? If yes, please provide details.

8) Whether SFC funds and its releases were clubbed or tied with any of the schemes of the State government? If yes, please provide details.

9) Whether SFC funds were subsumed into any other scheme of the government (state or central government)? If yes, please provide details.

10) Please provide your views on the Scheme of Devolution for ULBs that should be recommended/adopted by 6th SFC.

    a) Share of ULBs and RLBs

    b) Inter-se distribution between Corporations : Councils : Committees

    c) Criteria and weights for horizontal distribution among each tier of ULBs

    d) Any other issue

11) Any issue that you want the 6th SFC to address or consider while making their recommendations.

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