1. Why a Constitutional Commitment to Federalism is Important

Why in News?

- With the end of fourteenth Finance Commission and start of the Fifteenth Finance commission, debates around India's federal fiscal architecture are gathering momentum.

Division of Powers:

- The Constitution of India has provided for a division of powers between the Central and state governments. Under the Seventh Schedule, there are three lists – **the Union, State and Concurrent.**
- The **Union List** has a range of subjects under which the Parliament may make laws. This includes defence, foreign affairs, railways, banking, among others.
- The **State List** lists subjects under which the legislature of a state may make laws. Public order, police, public health and sanitation; hospitals and dispensaries, betting and gambling are some of the subjects that come under the state.
- The **Concurrent List** includes subjects that give powers to both the Centre and state governments. Subjects like Education including technical education, medical education and universities, population control and family planning, protection of wildlife and animals, forests etc.

Finance Commission (FC) and role of FC on fiscal federalism:

- Finance Commission is a constitutional body under Article 280 created every five years to recommend the transfer of financial resources from the Centre to the States.
- The Commission also decides the principles on which grants-in-aid will be given to the States.

Debates around the role of the Finance Commission:

- First, whether the recommendations of the Fourteenth Finance Commission on devolution of taxes to states would be protected.
- Secondly, would the purview of the Fifteenth FC be expanded?
- How the effects of the GST regime will be factored in, among others.
- These debates are further being expanded to include subjects which have never been under the purview of the FC traditionally.
- Recently, Bibek Debroy economic advisory council to PM says that, "the present CSS (centrally-sponsored schemes) basket has an expiry date of March 31, 2020, which is co-terminus with recommendations of the 14th Finance Commission."

- The second point he suggests is even more questionable – a re-look at the Seventh Schedule in context of restructuring and rationalisation of CSS.

Mandate of the Finance Commission:

- First, the mandate of the Finance Commission never included giving recommendations on resource transfers under the CSS. Presenting the CSS as being co-terminus with the Finance Commission is a flawed understanding of the transfers from Union to states.
- There are two kinds of transfers by the Union government – **general purpose and specific purpose.** The transfers made on the recommendations of the FC (which is formed every five years) are **general-purpose transfers,** which have mostly been untied.
- Apart from these, the Union government **through various ministries gives specific purpose grants,** which include Centrally Sponsored Schemes (CSSs) and central sector (CS) schemes. These transfers are tied, i.e. they are for specific schemes designed by ministries at the Centre.
- This implies that these schemes by design are outside the ambit of FC, unless specifically mandated by the Union government to the FC. Thus, there can't be an automatic expiry date for these schemes, unless desired by the Union government.
- Secondly, re-look at "the Constitution's Seventh Schedule, which differentiates between spending by the Centre and states." The argument put forth is "if the Union government should contribute to health because it is nationally important, why should states not contribute for defence?"
- The argument is problematic; it overlooks the roles of different tiers of government in a federal structure. Here there are two things.
- Firstly, **Article 246 adopts a threefold distribution of legislative power between the Union and the states.** The subject-wise distribution of this power is given in the three lists of the Seventh Schedule of the constitution – Union (List I), state (List II) and concurrent (List III). This implies that the states too have a large expenditure function.
- However, the **revenue mobilisation power of the Union is more compared** to the states. To correct this vertical imbalance, resource transfer is necessary. At the same time, there are differences in the level of development across states.
- The quality of life (in terms of access to education, health, employment) is relatively poor in low-income states and their revenue raising abilities are also limited.

- To ensure equity and certain minimum standards of public service, specific purpose transfers (such as for health and education) by the Union become necessary.
- Thus, by spending on these essential services, the Union government is trying to enable state governments to undertake expenditure on these services, which might otherwise not be prioritised either due to a resource crunch in poor states or other concerns taking precedence.
- Another issue is that **the power to legislate on a subject matter is closely linked to the power to spend on those matters.** Since the Union government has exclusive power to legislate on defence matters (List I), with no interference from the state governments, it is mandated to spend on it.
- Similarly, the Union government has exclusive power on issues related to foreign affairs, railways, atomic energy, income tax, customs duties, etc.
- At the same time, items in the state list are mostly related to socio-economic services, such as public health, sanitation, agriculture, etc. These items are better handled by the state government due to its proximity to the people.

Conclusion:

- Re-looking at the Seventh Schedule would then involve renegotiating legislative power on all the matters enlisted, which has the potential to shake the balance of power that now exists between the Union and states.
- However, changing the Seventh Schedule for deciding expenditure priorities of the Union government wouldn't be a prudent idea and certainly encroaches on the state's Autonomy.