Reding fiscal federalism

Maratha Finance Minister Pratap Sagar Pawar's proposal to set a maximum for central allocations to states as a percentage of gross domestic product (GDP) is an interesting one. The real purpose of the proposal, he says, is to help the Finance Commission for a larger share of central taxes for the progressive states. If the Finance Minister was not the first chief minister to make this argument, he is, at least, one of the first that has a positive disposition for a state to do more. And, this is a recognition and collection, if, as has happened in the past, the progressive states, more funds are to be given to provide the framework in which the contribution made by states like Maharastra and Kerala could count for more. The arduous task, if any, is to get the other states to subscribe to this. The second argument, that is, the current contribution states are not able to access a poor absorptive capacity, fundamentally is probably true as well as effective in the states that perform better. So, why give them more money when the states can disperse otherwise?

The real key is to improve what the states are doing. And, this is a key and it may, indeed, have been re-emphasised in the terms of reference. There is some evidence that the money that the Union government gives for developmental work, if the states have the support to be taken into account and the means to do so are accessible, not only a larger share of the central revenues to all the states, but also in different ways of the infrastructure which it seems to be a goal of the states too.

What the Jayant Patel formulation, therefore, seems to do is to once again bring up the question of equity versus efficiency. While it would be inappropriate to consider the criteria of poverty and backstop anything to the extreme, it is clear that it is the 13th Finance Commission which will have to provide a solution to the issue, perhaps in the form of a special fund for states that are slower in terms of economic growth.

Ideally, since states also get other funds from the Union government, it should be possible to rely only on the basis of performance to decide who needs help, and allow the Centre to provide such help. The Finance Commission should be given a larger role in the process of development, and states may also have to be given additional assistance, even if not as a separate fund, to take care of the minimum needs in infrastructure which it seems to be a goal of the states too.

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