The Eleventh Finance Commission

2.39 The Eleventh Finance Commission (EFC) was constituted by the President on July 3, 1998 to give recommendations on specified aspect of Centre-State fiscal relations during 2000-2005. The Commission submitted its Report covering all aspects of its original mandate on 7th July, 2000. The EFC had earlier submitted an interim report on the 15th January,2000, for making provisional arrangement for 2000-2001. The Commission was also asked to "draw a monitorable fiscal reforms programme aimed at reduction of revenue deficit of the States and recommend the manner in which the grants to the States to cover the assessed deficit in their non-plan revenue account may be linked to progress in implementing the programme". Accordingly, the EFC submitted a supplementary report on 30th August, 2000. In the Main Report submitted on 7th July, 2000, the EFC recommended revenue deficit grants of Rs.35359 crore for 15 States during 2000-2005. The remaining 10 States were revenue surplus in the EFC's assessment. Since only 15 States were assessed to be in revenue deficit, the fiscal reforms programme should have normally covered only the 15 States assessed to be in non-plan revenue deficit. Instead, in the Supplementary Report submitted on 30th August, 2000, the majority view in the EFC has recommended monitorable fiscal reforms programmes for all States. The EFC's major recommendations in their three Reports accepted by the Government are given in Box 2.4.

BOX 2.4

Major Recommendations of the Eleventh Finance Commission (EFC)

The major recommendations of EFC accepted by the Government are summarised below:

- A lumpsum provision of Rs. 11,000 crore in the Central Budget 2000-01 for revenue deficit grants to States.
- For the period of five years commencing from Arpil 1, 2000, the total share of the States in the net proceeds of Union taxes and duties would be 29.5 per cent.
- Grants totalling to Rs.4,972.63 crore be given towards upgradation of standards of administration and specific grants to certain States for special problems for the five years commencing from April 1, 2000.
- Grants totaling Rs.10,000 crore for local bodies during 2000-05, to be utilised (except the amount earmarked for maintenance of accounts and audit and for development of database) for maintenance of civic services (excluding payment of salaries and wages). Of this, Rs.1600 crore per annum is for rural local bodies and Rs.400 crore per annum is for urban local bodies.
- Continuance of the existing scheme of Calamity Relief Funds in States with an aggregate size of Rs.11007.59 crore during 2000-05. This includes the Centre's share of Rs.8255.69 crore, and the States' share of Rs.2751.90 crore. Discontinuation of the existing National Fund for Calamity Relief. The Central assistance to the States in national calamities should be financed by levy of a special surcharge on the cental taxes for a limited period and to be kept in a separate fund, to be known as National Calamity Contingency Fund, created in the Public Account of the Government of India.
- In deciding the total quantum of devolution of share in Central taxes/duties to States and grants-in-aid to States, tax devolution and Plan/non-Plan grants from the Centre to the States should not exceed 37.5 per cent of total Centre's revenues, both tax and non-tax.
- Grants-in-Aid under Article 275 (1) of the Constitution, amounting to Rs.35359 crore during 2000-2005 to be provided to such States (15 States) which will have deficit non-plan revenue account even after the devolution of central tax revenues, equal to the amount of deficits assessed during the period 2000-2005.
- In its Supplimentary Report, the majority view has recommended monitorable fiscal reforms programmes for all States. Fifteen per cent of the revenue deficit grants meant for 15 States during 2000-05 and a matching contribution by Central Government be credited into an Incentive Fund from which fiscal performance based grants should be made available to all 25 States. Total amount of the Fund comprising both parts is recommended at Rs.10607.72 crore for a five year period to be apportioned at the rate of Rs.2121.54 crore per annum. The grants for specific purposes like upgradation, special problems and local bodies, which remain unutilised due to non-observance of conditionalities attached to the release of these grants may also be credited to the Incentive Fund during 2004-05.
- For the purpose of drawing up State-specific monitorable fiscal reforms programmes, a monitorable fiscal reforms programme aimed at reduction of revenue deficit of the States is envisaged.
- A group designated as Monitoring Agency may be constituted by the Government of India for drawing up State-Specific monitorable fiscal reforms programmes for all States in the context of the broad parameters suggested by the EFC and as accepted by Government of India.
- Eighty five per cent of the revenue deficit grant recommended by the EFC and accepted by the Government of India may be released to the relevant States without linking it to performance under the monitorable fiscal reforms programme. Only 15 per cent of the revenue deficit grant to which a State is entitled may be withheld and linked with the progress in performance.
- The Monitorable programme should give equal weight to the raising of revenue and control of expenditure.
- The incentive component is to be provided to all the States. The initial eligibility of the States has been worked out on the basis of the population as per the 1971 Census. The amount will be available to a State in proportion to the level of performance in the implementation of the monitorable fiscal reforms programmes for each year.
- If any State is unable to get the full amount initially earmarked for it in any year, such amount will not lapse but will continue to be available in subsequent years to the same State. During the first four years, no amount of this Fund earmarked for assistance/incentive to a State, would be transferred to another State. However, if any State is not able to draw the amount indicated on the basis of the performance of the first four years, the amount undisbursed to a State would form part of the common pool and would be distributed to the performing States in the fifth year on a pro-rata basis in addition to the amounts to which they are initially entitled. The same would apply to the undrawn amount of the withheld portion of the grants to cover non-plan revenue deficit. Every State irrespective of the assessed deficit or not would be entitled to get the assistance on a pro-rata basis related to performance from the additions to the Fund. This additional entitlement can go up to 100 per cent of their initial eligibility indicated for the State concerned.
- The withheld amount of grants releasable in 2004-05 may be released to the concerned assessed State on the basis of a review of their performance. In case any amount remains unreleased to a State, it would be added to the Fund and would be available to the remaining States. The balance amount in the Fund at the end of 2005-06 will lapse to the Central Government.
- In addition to the incentives for better performance, Central Government may also consider the fiscal reforms programmes linked assistance by way of extended ways and means advance and additional open market borrowings. The scope and dimension of such facilities should be drawn up by the Central Government bearing in mind the Centre's fiscal position and the macro-economic implications of this facility. This facility should also be extended to all State linked to monitorable fiscal reforms programme.
- The disbursements from the Incentive Fund as well as the progress in utilisation of the grants recommended by the EFC in the Main Report will be subject to review by the 12th Finance Commission.