Polity & Governance · GS - II

Examine the evolving pattern of Centre-State financial relations in the context of planned development in India. How far have the recent reforms impacted the fiscal federalism in India?

EXAM YEAR	PAPER	SUBJECT
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MARKS	WORD LIMIT
15	~250 words

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Answer Hint

Planning Commission, Finance Commission, grants-in-aid, tax devolution, GST, GST Council, Centrally Sponsored Schemes, fiscal imbalance, cooperative federalism, 14th Finance Commission, 15th Finance Commission, 16th Finance Commission

Model Answer

Introduction

India's fiscal federalism has evolved from centrally planned development towards greater tax devolution and institutionalised cooperative mechanisms. Nevertheless, vertical and horizontal fiscal imbalances remain significant.

1. Evolution

During the planning era, the Planning Commission influenced resource allocation through Plan assistance, while the Finance Commission handled constitutional tax devolution and grants. This created substantial Union influence over State finances.

The abolition of the Planning Commission and creation of NITI Aayog shifted the framework towards cooperative federalism. The 14th Finance Commission increased States' share of divisible central taxes to 42%, strengthening

untied fiscal resources.

2. Impact of recent reforms

GST created a common indirect-tax framework and institutionalised the GST Council, where the Union and States jointly participate in tax decisions. A compensation mechanism was also established to protect States against revenue losses during the transition.

The 15th Finance Commission retained States' vertical share at 41% for 2021–26 after adjustment for the reorganisation of Jammu and Kashmir. The Finance Commission remains constitutionally responsible for recommending tax distribution and grants-in-aid.

However, States continue to face concerns regarding cesses and surcharges, conditional grants, GST-related loss of taxation autonomy and rising expenditure responsibilities.

Conclusion

Recent reforms have strengthened institutionalised fiscal federalism, but genuine cooperative federalism requires predictable transfers, greater consultation on centrally sponsored schemes and adequate fiscal autonomy for States.

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