# FINANCING OF RELIEF EXPENDITURE

6.1 Paragraph 9 of the President's Order requires us to review the policy and arrangements in regard to the financing of relief expenditure by the States affected by natural calamities. We have been called upon to suggest appropriate modifications in the existing arrangements, having regard, among other considerations, to the need for avoidance of wasteful expenditure. The President's Order also requires us to examine the feasibility of establishing a national insurance fund to which the State Governments may contribute a percentage of their revenue receipts. The mandate is much wider than in the past. Pending the detailed examination of all the inter-related matters we had recommended in our first report the extension of the scheme of the Eighth Finance Commission to 1989-90 with the amount of margin money revised and updated. We will now examine in this report the entire gamut of the issues referred to us in paragraph 9 of the said Order.

6.2. The existing policy and arrangements for meeting the relief expenditure are, by and large, based on the observations and recommendations of the successive Finance Commissions. All the Finance Commissions from the Second Commission onwards have accepted the concept of margin money which is built into the expenditure forecast of each State. The Seventh Finance Commission, for the first time, made a distinction between different calamities. It distinguished droughts from floods, cyclones and earthquakes. The distinction was made on the grounds of differences in the nature of the calamity and the consequent difference in the measures required for relief of distress. That Commission recognised the fact that the necessity for relief in the event of floods,cyclones and earthquakes was immediate and the needed action could brook no delay. The incidence of droughts, on the other hand, was something which could be foreseen and which also permitted certain margin of time for planning relief works. In fact, while a flood destroys, drought offers the opportunity of creating productive assets for the community through relief works, provided a shelf of development projects to be executed at the local level is kept prepared in advance. There is no loss of immovable property in drought even though there is considerable loss of production of food and fodder. Drought leads to erosion of employment and wages, migration of cattle, distress sales, malnutrition and serious diminution in the availability of drinking water. As against this, when floods, cyclones or earthquakes occur, there is loss of both human and cattle lives accompanied by damage to public and private property. Floods may cause damage to standing crops - they may even lead to salinity or sand-spilling in certain cases - but quite often, the next crop, invigorated by the deposit of fresh silt, is healthy and luxuriant. The Eigth Finance Commission considereded the damage caused by fire as well to be treated on the same footing as floods, cyclones and earthquakes.

6.3. The pattern of funding of the relief expenditure has been evolved over the years on the basis of the recommendations of the Finance Commissions. The margin money for each State was calculated by averaging the non-plan expenditure (excluding advance Plan assistance and expenditures of a Plan nature) booked over the years under the heads accommodating the relief expenditure. The Seventh Finance Commission, while fixing the margin money, took into consideration the fact that the expenditure on public works damaged by a natural calamity constituted a heavy burden on the finances of the States and, therefore, it included an element on this account too in the margin money. The expenditure on relief employment, however, was kept outside the purview of margin money. That Commission also improved by 15 per cent the average calculated for 9 years(1969-70 to 1977-78) to allow for the increase in price levels. The Seventh Commission stipulated that in the event of drought, the expenditure, over and above the margin money, should be met by the State out of the contribution from its Plan outlay. Normally, such a contribution was not supposed to exceed 5 per cent of the annual Plan outlay of the State. This contribution by the State was to be covered by release of "advance Plan assistance" by the Government of India adjustable within five years following the end of the drought. The assistance was released in the form of 70 per cent loan and 30 per cent grant to all non Special Category States, Assam and Jammu and Kashmir and 10 per cent loan and 90 per cent grant to Special Category States excluding Assam and Jammu and Kashmir. In those cases, however, where the drought was so severe that the expenditure could not be restricted to 5 per cent of the annual Plan of the States, the Seventh Finance Commission recommended that the expenditure should be taken as an indication of the special severity of the calamity which would justify the Central Government assisting the State to the full extent of the extra expenditure. This extra assistance was to be made available by the Central Government on more liberal terms i.e., half as grant and half as loan. As regards expenditure in excess of margin money on repairs and restoration of public works following floods, cyclones and earthquakes, the Central assistance was to be made available as non-plan grant not adjustable against the Plan. The non-plan grant was to be given to the extent of 75 per cent of the total approved ceiling of expenditure in excess of the margin money. The remaining 25 per cent was to be borne by the State. The Seventh Finance Commission had also observed that where a calamity was of "rare severity", the Central Government could extend assistance to the States concerned even beyond the schemes suggested by the Commission.

6.4. The Eighth Finance Commission recommended the continuance of the scheme suggested by the Seventh Finance Commission, increased the quantum of margin money for all States to Rs.240.75 crore per year and suggested that the margin money should be shared on a matching basis between the Centre and the States. That Commission further stipulated that the margin money should cover items of direct relief expenditure and expenditure on repairs and restoration of public assets. The expenditure on relief employment was disallowed, except to the extent where additional staff was specifically recruited for the purpose of relief operations.

6.5. Let us now examine the views of the States in the matter. Almost all the States felt that there were deficiencies in the present arrangements and pointed out the operational problems that the scheme gave rise to. Uttar Pradesh, Madhya Pradesh, Maharashtra, Manipur etc., would like the present distinction between droughts and floods to be done away with. All non-plan expenditure on drought relief in excess of the margin money is expected to be borne by the State Governments. The advance Plan assistance is available to accommodate Plan expenditure but this assistance is adjustable against future Plan assistance. This pattern of funding obviously cuts into the size of the Plan for subsequent years and poses problems of inter-sectoral adjustments. The States, therefore, by and large, do not relish the linkage of relief expenditure to the adjustment from Plan assistance which eventually reduces the size of the Plan. In their view, the entire expenditure should be met by the Central Government in the form of non-Plan grants. Further, State

Governments have argued that Central teams which visit the States after the calamity do not allow some items of expenditure on which expenses have already been incurred by the States and that they also do not have very clear idea about the norms for different items of expenditure on drought and flood relief. A number of suggestions have been made for increasing the level of expenditure. Bihar, Gujarat and Maharashtra have suggested increase in the quantum of cash doles given to the aged and the handicapped. Other suggestions include admissibility of overhead expenditure, purchase of capital equipment and payment to skilled workers with a view to creating permanent assets through employment generation programmes. Some of the States have also requested that they should be allowed a free hand in incurring expenditure on heads other than those approved by the Central teams with the stipulation that the total ceiling should not be exceeded. They have also suggested that the loans advanced by the Centre for financing the relief expenditure in the past and remaining outstanding should be written off.

**6.6.** The States have also referred to the current procedure for sanction of relief assistance by the Government of India which,according to them, is somewhat cumbersome and time consuming. In actual practice considerable time is taken before final indication is received about the quantum of assistance available from the Government of India. States argue that they are handicapped by the fact that they do not know at all as to why their claims for Central assistance are disallowed and why the size of the assistance is drastically curtailed relative to the demand put forth by them. The Central teams constituted at short notice and comprising officers drawn from different disciplines are said to have no effective means of checking the data personally and their recommendations which are usually endorsed by the High Level Committee on Relief are based mostly on impressions gathered during brief visits to some sites.

**6.7.** We feel that the present system in which any assistance in excess of the margin money is made conditional on the assessment of the Central team carried out at short notice would lead, by its very nature, to dissatification on the part of the States and at the same time induce them to make exaggerated claims. On the other hand, since the quantum of assistance is based on quick and rather cursory surveys, there could be substantial underassessment of the damage to be compensated for. We must,therefore, look for an alternative system.

**6.8.** The Sixth Finance Commission had a mandate under the President's Order to examine the feasibility of establishing a national fund somewhat similar to what has been assigned to us. That Commission gave careful thought to the pros and cons of the setting up of such a fund. It recognised the fact that the provision of relief was a sensitive issue and any fund set up outside the Government would find it difficult to deal successfully with issues having political implications. In the event of a wide-spread natural calamity the Central Government would come under strong pressure to go all out and provide assistance to the affected State. In such a situation,the availability or otherwise of resources in the national fund would cease to be relevant in determining the quantum of assistance. The concept of national fund would thus break down completely in the event of a major calamity. At the same time, the States would view the assistance from the national fund as legitimately due to them, at least, to the extent of their contribution. There was thus a risk of the fund being depleted even in the normal years, while in years of adversity, it might prove wholly inadequate. That Commission also felt that there were serious operational difficulties in the constitution of such a fund. The determination of the contribution of individual States to the fund would pose conceptual and practical problems. No formula, however carefully designed, would be acknowledged as fair by all the States. Some of the States would be called upon to contribute appreciably more to the pool than they were ever likely to draw from it. The question of States' contribution to the fund - the Commission felt - might become yet another irritant in Centre-State relations. The Sixth Finance Commission, therefore, came to the conclusion that the establishment of such a national fund was neither feasible nor desirable.

**6.9.** The feasibility of establishing a national insurance fund to which States may contribute a percentage of their revenue receipts has also been referred to us under the President's Order. In this connection we had discussions with the Life Insurance Corporation of India(LIC) and the General Insurance Corporation of India (GIC). These institutions operate a number of schemes which cover, wholly or partly, some of the items for which relief is provided. Both LIC and GIC were asked to examine the possibility of formulating a comprehensive umbrella scheme which could cover the whole range of natural calamities for which relief is currently admissible. The LIC indicated that it would be possible for them to cover only one item viz., ex-gratia payment to a bereaved family under the insurance scheme. It further mentioned that due to certain legal constraints it would not be possible for it to cover death attributable only to natural calamity. The insurance cover would include deaths ascribable to other factors as well. The insurance cover could be had under the group insurance scheme of the LIC covering groups of persons taken together under one master policy. It further stated that since a natural calamity might affect many categories of people in many geographical locations of the country, the only effective way was to cover the entire population of India within the age group of 18-60 years for an assured sum of Rs.1000 per person. The premium on such an insurance was tentatively estimated to cost Rs. 400 crore per annum and this we considered to be too colossal a sum for the limited benefits provided. In any case, it hardly bore any relation to the maximum expenditure of Rs.84.5 lakhs incurred by the States for the loss of life during any one year of the last five years. The proposal submitted by LIC was beset with other limitations as well. The scheme, by and large, covered only the principal bread-winner of the family and the population below 18 years and above 60 years was outside its purview. The LIC would also not be in a position to operate even a limited scheme of this nature entirely on its own strength. It would call for heavy dependence on the administrative machinery of the State without which the settlement of the claims was likely to get inordinately delayed. We felt,therefore, that the proposal submitted by LIC was unlikely to meet the purpose which we had in mind.

**6.10.** The General Insurance Corporation of India (GIC) also operates its business of general insurance on the principles of insurable interest and indemnity. Most of the items for which assistance is now being provided by the States do not lend themselves to the concept of general insurance as transacted by the GIC. Only a few of the items fall under the categories now being insured by the GIC. It was found that the items which the GIC was prepared to insure did not account for even 20 per cent of the total ceilings of expenditure approved for relief during the five year period 1982-87. In any case, both the LIC and the GIC do not have field organisations of their own down to the block and village levels which could take up the task of assessing losses and damages resulting from natural calamities. The insurance cover provided by them is also of a limited nature and the bulk of the items on which relief is being given today fall outside their purview.The LIC and GIC have further averred that given the magnitude of the problem, they could operate any such scheme, like the Crop Insurance Scheme, not as insurance bodies but as agents of the Government. In other words, government would have to provide budgetary support to meet any gap between the premium collected and claims paid. We found it difficult to evolve an appropriate insurance scheme which could be operated independently of the government. The formulation of an insurance scheme would hinge on determination of experience-rated premia for different types of risk whose incidence and intensity would vary widely from State to State and, indeed, from area to area within each State. There would be serious imponderables in working out the premium rates and getting the same accepted by all the States.

**6.11.** The source of calamity, by its very nature and magnitude, would pose problems which no agency, outside government, can tackle exclusively and in full measure. The process of assessing the loss by an external agency is bound to be a lot more complicated and time-consuming. It would largely defeat the purpose of providing timely succour to the people stricken by calamity. Besides, the greatest sufferers in a natural calamity are the poor and the have-nots at the bottom of the social and economic pyramid who have precious little to insure. Apart from this, it must be remembered that in the case of floods and cyclones, much of the damage is caused to public assets such as roads, embankments, bridges and government buildings. The States have to be helped to rebuild them. This liability to rebuild cannot easily be measured as an insurable risk, particularly when the physical conditions and the sources of risk vary vastly as between States. It would, therefore, seem that the concept of an insurance fund for disaster relief is not a viable one and a scheme based on the insurance concept will run into serious practial problems.

6.12. It is not possible to run away from the basic fact that the primary responsibility for providing relief to the persons affected by natural calamities is that of the government. No corporate body or agency independent of government can ever cope with the multitude of problems left by a natural calamity in its trail. The execution of the relief programme, therefore, cannot be delinked from governmental responsibility.

6.13. We, therefore, share the misgivings expressed by the Sixth Finance Commission in full measure. The majority of the States have also opposed the setting up of such a fund. Having heard the States and after having given serious thought to the entire gamut of inter-related issues we also feel that the establishment of a national insurance fund is not feasible.

6.14. It is seen that in the last ten years (1979 to 1989) the total of ceilings of expenditure allowed on relief on account of natural calamities comes to Rs. 7930 crore. While there has been a continuous increase in the ceilings of expenditure on account of relief, it is seen that no asset of any significance could be created within the parameters of the relief programmes both under floods and drought nor could any long- term corrective action be undertaken. The assets created were negligible as the scheme of financing of drought relief work did not allow for expenditure on material components or for employment of skilled staff to guide the unskilled workers who could create durable assets. It was mostly test relief type of work which was undertaken. Further, the scale of assistance allowed was not enough to meet the actual expenditure required for the restoration of the assets. No purpose was served by such assistance. The Commission feels that it would have been a more constructive approach if this money had been given as seed money to enable individuals or a group of people to get help from financial institutions and build pucca houses. A similar approach is also called for in the construction of the roads damanged by a natural calamity.

6.15. While formulating our recommendations on the financing of relief expenditure and suggesting a suitable scheme, we must keep in view certain basic considerations to ensure the success and viability of the scheme. The first concerns the level of assistance to be provided for. An analysis of the operation of the scheme during the recommendation period of the Eighth Finance Commission would clearly show that the ceiling for the margin money prescribed by the Eighth Commission proved to be quite inadequate for the levels of relief expenditure sanctioned by the Central Government in each year of the recommendation period. The total ceilings of expenditure approved by the Government of India during the five-year period 1984-89 were Rs.512.89, Rs.1006.32, Rs.1023.89, Rs.1658.92 and Rs.1084.29 crore, respectively, against the annual margin money of Rs.240.75 crore fixed by the Eighth Commission. This large difference between the margin money fixed and the actual ceilings of expenditure was due to the fact that the margin money was calculated excluding the expenditure incurred by the States on items of plan nature for which advance Plan assistance was given, whereas the actual ceilings of expenditure included also advance Plan assistance consisting of both grants and loans. The expenditure level allowed should be calculated in such a manner as to reflect the current realities as closely as possible. Second, the present system of assessment of the damage and the mechanism of giving Central assistance leads to delay in extending help and succour to the people affected by the natural calamities which should be avoided. Quickness of response should be a basic feature of the scheme. Third, we must take note of the fact that, quite often, the catalogue of demands presented by the States is inflated in character presumably under the impression that the claim, regardless of how realistically it has been formulated, would, in any case, be cut down heavily by the Government of India. The compulsions of public opinion in the State may also lead to such demands so that the State Governments could avoid being criticised for alleged underestimation of relief requirements. Any scheme of financing the relief expenditure, therefore, should contain a built-in mechanism to discourage such claims which are either not necessary or not fully supported by facts. Fourth, the scheme should be so designed as to ensure against profligacy and wastefulness. As observed by the previous Commissions, the big increase in expenditure in terms of approved ceilings from Rs.49.88 crore in 1974-75 to Rs.1084.29 crore in 1988-89 cannot be explained purely in terms of the growing severity of natural calamities. True, the environmental degradation, deforestation, climatic changes as a consequence of the greenhouse effect, rapid population growth forcing settlement and cultivation of marginal lands in the river beds and storm water channels have all contributed to the phenomenal growth in relief expenditure. At the same time, increased expenditure on relief diverts precious resources from investment in projects needed for the long term growth of the economy. The scheme should aim at providing incentives for economy in expenditure. Fifth, the States should be able to take care of the problems and expenses caused by the occurrence of the usual type of natural calamities of normal magnitude. That is, the money already provided in advance should be more or less sufficient for the purpose of relief expenditure except when there is a serious disaster. Keeping these considerations in mind and also taking into account the various suggestions made by the State Governments, we recommend as follows.

6.16 The present arrangement for financing relief expenditure should be replaced by a new one where greater autonomy, accountability and responsibility are placed upon the States and they are provided adequate means and wherewithal to carry out the same. Once this is done, the States would be expected to follow the path of self-reliance and would not have to look up to the Centre. This would also be in conformity with the views of previous Commissions and the constitutional position that the primary responsibility for relief is that of the States.

6.17. We propose to replace the present scheme involving the provision of margin money, preparation of States' memoranda, visits of Central teams, etc. by a scheme which is qualitatively different in the sense that generous funds are placed at the disposal of the States and they are expected to look after themselves in almost all situations. We have taken the average of actual ceiling of expenditure approved during the last ten years ending in 1988-89 and rounded it off to the nearest crore thus completely changing the concept of margin money followed hitherto. On this basis, the aggregate average for all the States, taken together, works out to Rs.804 crore. We, therefore, recommend that a total of Rs. 804 crore should be available each year to States as funds earmarked for relief on account of natural calamities. This amount does not represent just the margin money (both Centre's and States' shares) as understood so far but the average of ceilings of expenditures approved in the last ten years which include margin money, advance Plan assistance (grant and loan), special Central assistance (50:50 loan and grant) for relief of natural calamities and the State's own share of 25 per cent in flood relief. The Centre will be required to pay 75 per cent ( Rs. 603 crore) to a Calamity Relief Fund for all the States together for each year of the five year period covered by our report. The Statewise shares are shown in Annexure VI.1. The States would have to deal with natural calamities and manage their affairs without the need for any reference to or authorisation from the Centre within the amounts so provided. The other features of the scheme would be as under:

(I) A Calamity Relief Fund should be constituted for each state with the amount allocated to the State. This fund would have an existence separate from the general revenues of the State and contributions to this fund would be made by the Centre and the State concerned in the course of the year in equal quarterly instalments. The fund will be kept in a nationalised bank and administered by a Committee.

(II) Contribution to the fund would be made by the Government of India to the extent of 75 per cent in the form of non-Plan grant. The balance of 25 per cent shall be contributed by the State Government out of its own resources.

(iii) The fund would be operated under the control of a Committee headed by the Chief Secretary of the State. The Committee would consist of officials who are normally connected with relief work and experts in various fields in the State affected by natural calamities. The Committee will be nominated by the State Government.

(iv) The State Level Committee shall decide on all matters connected with the financing of the relief expenditure.

(v) Following the creation of this fund, it will be the responsibility of the State Governments to meet all expenditures arising out of natural calamities. The yearly additions to the fund as well as the accrual of interest thereon should be used to meet the requirements. No further Central assistance would be available for this purpose.

(vi) The money put into the fund in a year and remaining unspent in that year or in subsequent years would be available to the State at the end of the 5th year or thereafter for being used as a resource for the next Plan.

(vii) The State Level Committee will decide all the variations in the norms of assistance as it may not always be realistic to have one uniform norm throughout the country.

(viii) If it is found by the State Level Committee that in a particular year the amount required is more than the same available in the fund, it may draw 25 per cent of the funds due to them in the following year from the Centre to be adjusted against the dues of the subsequent year. The Central Govt. may, however, at its discretion, allow a higher percentage of advance from the State's entitlement in the next year.

(ix) The State Level Committee may keep the Union Ministry of Agriculture, informed of the amount of damages due to drought, floods, etc. as well as the broad details of the relief work undertaken.

(x) The present arrangements for coordinating relief work at the Centre in the Ministry of Agriculture may continue so that the assistance from Defence forces, Railways as also supply of seeds, etc., which may be required in times of natural calamities could be coordinated.

(xi) The Commission also recommends that all calamities such as drought, floods, cyclone, fire, etc., which have so far been covered by the relief schemes of the previous Commissions for purpose of relief assistance should continue to be covered in the present scheme also and the distinction between drought on the one hand, and floods, cyclone, fire, etc., on the other, be done away with.

(xii) The Centre should constitute an Expert Group to monitor the relief work done in the States utilising the Calamity Relief Fund. Acknowledged Experts in various relevant disciplines should be involved in this work of monitoring. The result of their work should be communicated to the State Government concerned. The Group may also give such advice as it deems appropriate to the States' agencies involved in relief work. We expect that the work of this Group and the reports it prepares would enable the next Finance Commission to review the working of the new scheme we have recommended.

6.18. During the period covered by our Report, if any region faces a calamity of such dimensions and severity as to warrant its handling at the national level, we are confident that the Centre will take appropriate action as the situation demands and incur the necessary expenditure.

## BHOPAL GAS LEAK TRAGEDY

6.19. We propose to deal with Bhopal Gas Leak Tragedy also in this Chapter although this tragedy was industrial and man-made and quite distinct from a natural calamity. This tragedy was by far the worst industrial disaster of its kind. We had observed in the first report that a crisis of this magnitude could not legitimately be construed as the exclusive responsibility of the State Government. The Supreme Court of India has since given its decision and pursuant to the same the Union Carbide Limited has deposited a sum of US $ 470 million with the Reserve Bank of India. We believe that the amount available from the Union Carbide Limited is dedicated entirely to the victims of the gas tragedy and the compensation money would not lend itself to any adjustment against the sum already spent or required to be spent in future for this purpose either by the Government of India or by the State Government. An assurance to this effect has also been given to the Supreme Court by the Government of India.

6.20. It would be worthwhile to remember in this context that the Government of India enacted a Bhopal Gas Leak Disaster (Processing of Claims) Act, 1985 under which the Central Government assumed the exclusive responsibility to represent all the victims and the claimants of the gas tragedy. The Government of India assumed the role of "parens parentis" on behalf of the victims of the tragedy. This adds considerably to the responsibility of the Government of India as regards its duties and obligations to the victims.

6.21. The Government of Madhya Pradesh had earlier submitted an "Action Plan" involving an amount of Rs. 371.29 crores likely to be spent on relief and rehabilitation during the period from 1988-89 to 1994-95. It is learnt that the size of the Action Plan, following its scrutiny by Government of India, has since been reduced to Rs. 163 crores. We, therefore, recommend:-

(a) that the entire amount of medium term loan of Rs. 91.62 crore given by the Government of India to the State Government, together with the interest thereon, should be written off. A special reference to this has been made later in the Chapter on Debt Relief.

(b) the future requirement of fund in the forecast period towards the relief and rehabilitation of the victims which has now been reduced to Rs. 163 crore should be met by the Government of India and the State Government in the ratio of 3:1. The share of the Government of India which works out to 75 per cent of the entire amount should be given to the State Government by way of outright grant. The balance of 25 per cent should be met by the State Government out of its own resources for which a suitable provision has been built into our assessment for Madhya Pradesh. The amount mentioned here is over and above the amount allocated to the State for financing its other relief expenditure.