

EXPLANATORY MEMORANDUM AS TO THE ACTION TAKEN ON THE RECOMMENDATIONS MADE BY THE FIFTEENTH FINANCE COMMISSION IN ITS REPORT FOR FINANCIAL YEAR 2020-21 SUBMITTED TO THE PRESIDENT ON DECEMBER 5, 2019.

1. The Fifteenth Finance Commission (XV-FC) [Commission, henceforth] was constituted on 27th November 2017 by the President, vide Order number S.O. 3755(E) dated 27th November 2017. The Commission, vide S.O. No.4308 (E) dated 29th November, 2019, has been mandated to submit two reports i.e. a first report for financial year 2020-21 and a final report for the period 2021-22 to 2025-26. The date of submission of the final report is 30th October, 2020. The Commission submitted its first report covering the financial year 2020-21 to the President on 5th December 2019.
2. The Report of the Commission covering the financial year 2020-21 commencing from April 1, 2020, together with this Explanatory Memorandum on the action taken on the recommendations of the Commission, is being laid on the Table of the House, in pursuance of Article 281 of the Constitution. Summary of the main recommendations related to sharing of the Net proceeds of Union taxes between the Centre and the States, grants-in-aid of revenue of States under Art 275(1) of the Constitution, financing of relief expenditure, grants to local bodies and other recommendations are contained in this Memorandum. This Memorandum also contains the recommendations related to Sectoral Grants and Performance based indicators provided by the Commission in its report submitted on December 5th 2019.

Sharing of Union Taxes

3. The Commission has recommended that 41 per cent of the net proceeds of Union taxes should be shared with the States as against the present 42%. The Commission felt that, financial resources equivalent to 1% of the net proceeds of Union taxes should be retained with the Central Government for financing the requirements of the newly formed Union Territories of Jammu & Kashmir and Ladakh.

The Government has accepted the above recommendation of the Commission.

Grants-in-aid of Revenues of States under Article 275 of the Constitution

4. The Commission has recommended Grants-in-aid of revenues of States for revenue deficit, special grants, nutrition grants, local bodies and disaster management under Art 275 of the Constitution.

Revenue Deficit Grants

5. The Commission has recommended Post-Devolution Revenue Deficit Grants amounting to ₹74,340 crore for fourteen States in 2020-21. Of the total revenue deficit grants of ₹74,340 crore, ₹37,917 crore have been assigned to General States namely, Andhra Pradesh, Kerala, Punjab, Tamil Nadu, and West Bengal while ₹36,423 crore are assigned to North-Eastern and Hilly States namely Assam, Himachal Pradesh, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim, Tripura, and Uttarakhand. The details of the revenue deficit grants are contained in Chapter 4 of the Report.

The Government has accepted the above recommendations of the Commission

Special Grants

6. The Commission has recommended Special Grants aggregating to ₹6,764 cr in 2020-21. These grants have been provided to ensure that in FY 2020-21, no state receives in absolute terms less than what it received in FY 2019-20 on account of tax devolution and revenue deficit grants. The details of the revenue deficit grants are contained in Chapter 4 of the Report.

The Commission may be requested to reconsider the recommendation as it introduces a new principle.

Nutrition Grants

7. The Commission has recommended additional grants of ₹7,735 crores to States for nutrition in 2020-21. The Commission has recommended that the Nutrition grants should not be substituted for either the State share or Union share and are an additionality. The details of the revenue deficit grants and the manner of providing them are contained in Chapter 4 of the Report.

The Commission may review this recommendation as a part of its overall proposal of measurable performance-based incentives for States as per the ToR, in the main report

Local Bodies

8. The Commission has recommended grant for local bodies of all States amounting to ₹90,000 crore. The recommended allocation for rural local bodies (RLBs) and urban local bodies (ULBs) in 2020-21 are ₹60,750 crore and ₹29,250 crore respectively.
9. The Commission has recommended that the rural local body grants be given to all three tiers in the panchayats, i.e. village, block and district. The Commission has recommended that rural local body grants, totalling ₹60,750 crore shall have two components-basic and

10. tied. The ratio of basic grants to tied grants shall be 50:50. The Commission has recommended that the basic grants are untied and can be used by the local bodies for location-specific felt needs, except for salary or other establishment expenditure.

10. The Commission has recommended that State Governments should make allotment of grants for both Fifth and Sixth Schedule areas falling within their jurisdiction. The inter-se allocation should be determined based on the population to area in the ratio of 90:10. The bifurcation into basic and tied grants shall be applicable to the fifth and sixth schedule areas.

11. The Commission has recommended that urban local bodies be provided total grants of ₹29,250 cr. The Commission has recommended providing ₹9,229 crore for the Million-Plus cities and ₹20,021 crore for the other category of cities/towns. The Commission has recommended that States should make allotment of grants on population basis for the Cantonment Boards within their territories. The details of the composition and manner of providing these grants are contained in Chapter 5 of the Report.

The Government has accepted these recommendations of the Commission

Disaster-related Grants

12. The Commission has recommended that the total amount allocated to the States for SDRMF shall be ₹28,983 crore in 2020-21, of which the Union share is ₹22,184 crore. The Commission has recommended that the allocation for National Disaster Risk Management Fund (NDRMF) be ₹12,390 crore in 2020-21 based on the expenditure-based methodology. The recommendations of the Commission in respect of Disaster Risk Management, including the composition and the earmarked allocations within the SDRMF and the NDRMF, the details and conditionalities regarding release of these grants are contained in Chapter 6 of the Report.

The Government has accepted these recommendations of the Commission.

Sectoral Grants

13. The Report discusses the broad contours of sectoral grants and preparatory work to be undertaken by the State Government and different Ministries/Departments of the Union Government in regard to sectoral grants. The Commission has recommended that preparations be undertaken by the State Governments and the Ministries/Departments of the Central Government in respect of seven (7) different sectors. Contingent on their preparations, the Commission intends to provide sector-specific grants for health, pre-primary education, judiciary, rural connectivity, railways, statistics and police training and

housing. The recommendations of the Commission on the sectoral grants are contained in Chapter 4 of the Report.

The Government has accepted these recommendations of the Commission in-principle.

Performance-based incentives

14. The Commission in its report has advised the States to undertake preparatory action by establishing a credible implementation and monitoring system in 2020-21, after developing robust, monitorable outcome indicators for releasing the grants to eligible States in subsequent years. The concerned Ministries/Departments are required to define the State-wise baseline indices/score/data using the indices to monitor annual incremental changes and issue guidelines before May/June 2020. These recommendations on the preparatory work to be undertaken by the States and the Ministries / Departments are contained in Chapter 4 of the Report.

The Government has accepted these recommendations of the Commission in-principle.

Other recommendations

15. In addition to the above, the Commission has made other recommendations related to revenue and expenditure reforms, at the Central and the State levels, accounting and budgeting reforms, additional disclosures by the Central Government and the State and local bodies.

The Government will examine these recommendations of the Commission in due course.

Implementation

16. Orders on the recommendations under Art 270 and 275(1) of the Constitution relating to share in Union Taxes and duties and Grants-in-aid respectively will be issued after obtaining the approval of the President. Other recommendations of the Commission will be acted upon in due course.

New Delhi
January 30, 2020


NIRMALA SITHARAMAN
Minister of Finance