New India formula? – on the 15th Finance Commission

The 15th Finance Commission's job will be especially tricky in the time of GST

The Centre has moved swiftly to notify the presidential order setting up the Fifteenth Finance Commission, within five days of the Cabinet's approval. The constitutional body is tasked with recommending a fiscal road map and a sharing of resources between the Centre and the States. On Monday, former Revenue Secretary N.K. Singh, who has been appointed chairman of the Commission, held preliminary discussions on its "wide-ranging" terms of reference and decided to hold expeditious consultations with stakeholders at all administrative levels as well as with political parties. Think tanks and academics will be consulted. The Commission has less than two years to complete its deliberations and submit its report by October 2019, giving the government a little over a quarter to consider and implement its recommendations for the period from April 2020 to March 2025. Accepting the 14th Finance Commission's recommendation to raise the States' share in the divisible pool of taxes to 42% from the previous 32% level, Prime Minister Narendra Modi had told Chief Ministers that although this meant less money at the Centre's disposal, his government had decided to strengthen the States' capacity to move away from a 'one-size-fits-all' approach. While Mr. Modi's disdain for Central planning is well-known, the terms of reference for this Commission seem to suggest that the record hike in the tax transfer rate to States is pinching.

The Centre has urged the Commission to finalise its tax-devolution formula after factoring in the impact on the Union's fiscal situation, keeping in mind "the continuing imperative of the national development programme including New India – 2022". Taken together with its need for resources for essential spending in areas such as defence, security, infrastructure and climate change, the Centre seems to be seeking a rollback of the 42% share for States. The government's top brass has repeatedly asserted the need for revenue to maintain public spending in the face of flak for high petroleum taxes. But a reduction from the 42% rate could dent States' faith in the Centre's claims of cooperative federalism. The rollout of the goods and services tax, which marks a new chapter in tax administration with both the Centre and States working together through the GST Council, makes the challenge trickier. The Centre is committed to compensating States for any revenue losses arising out of GST implementation till June 2022, thus covering nearly half the period for which the Commission is to recommend a formula. Its mandate includes formulating performance-linked incentives for States on a range of desirable outcomes such as attaining a replacement rate in population growth, deepening the GST net and improving the ease of doing business. Devising a fiscal nudge for development goals sounds attractive, though the challenge would lie in quantifying the good from the ugly — especially when one has to reward a State for showing 'control or lack of it in incurring expenditure on populist measures'.

Source: xaam.in