CENTRE STATE FINANCIAL RELATIONS IN TAMIL NADU

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ABSTRACT

The important and elastic revenue sources are mostly assigned to the Union Government and the major expenditure obligations are assigned to State governments. To enable the States to carry out their expenditure responsibilities, the Finance Commission is assigned the task of recommending the transfer of resources from the Centre to the States. The share of central transfers in aggregate expenditure of the State governments has varied between 35 per cent and 45 per cent. This clearly brings out the heavy dependence of the State governments on the Centre. The present paper is an attempt to know the financial relation of Tamil Nadu state with Centre from 12th finance commission period (2005-06 to 2018-19).

KEY WORDS: *Central Transfers, Devolution of Taxes, Tax Revenue, Tax Buoyancy*

INTRODUCTION

The distribution of powers defines the financial relations between the Central and the state Governments in a federal system. In India, Centre-State financial relations relate to the sharing of expenditure responsibilities and distribution of power in collection of revenue between the Centre and the States. Indian State governments are accounting for three fourths of the aggregate social expenditure and more than one-half of the aggregate expenditure on economic services but mobilizing about only one-third of the total tax revenue. That is, in India, the substantial and elastic revenue sources are assigned to the Union Government while the major expenditure responsibilities are assigned to State governments which create vertical fiscal imbalance between the Centre and the States. There is lot of disparities in the economic development on account of different factor endowments which creates Horizontal Fiscal imbalance among the States.

To address these imbalances the Constitution provides for the establishment of a Finance Commission under Article 280. Finance Commission is to be constituted by the President for every 5 years to make recommendations on transfer of resources from Centre to States in the form of Share in Central taxes and grants. Resources from the Centre to the States have increased continuously over the period of time. The share of these transfers in aggregate expenditure of the State governments has varied between 35 per cent and 45 per cent. This clearly brings out the heavy dependence of the State governments on the Centre. Given this background, an attempt was made to know the financial relation of Tamil Nadu state with Centre during the last three finance commission periods (2005-2010, 2010-2015 and 2015-2020). Since the data are available only up to 2018-19 it restricted the analysis to 2018-19.

Objectives

- To analyze the growth trend of Central Transfers in Tamil Nadu.
- To understand the growth pattern of components of Central Transfers in Tamil Nadu
- To examine the share of different taxes in Central tax revenue shares.

- To analyze buoyancy of total revenue from state taxes.

Hypothesis

- There is no significant difference in the Tax Buoyancy between 13th and 14th Finance Commission period.

Methodology

Secondary data form the basis of this study. The data were obtained mainly from Reserve Bank of India (RBI) data base, Statistical Hand Book of Tamil Nadu, and Economic Survey. Growth rate have been worked out to know the growth pattern of central transfers and share of central taxes to Tamil Nadu. Simple percentage was computed to know the share of devolution of central taxes and grants-in-aid in total central transfers. Tax buoyancy was calculated to measure the responsiveness of tax yield to any change in the state income with the help of formula $\frac{\Delta Y}{Y} \Big/ \frac{\Delta X}{X}$ (Where Y is tax revenue and X is state income)

Results and Discussion

The growth pattern of central assistance received by the state Tamil Nadu during the Twelfth, Thirteenth and Fourteenth Finance Commission period is presented in the following table.

Table:1 Growth Trend of Central Transfers to Tamil Nadu

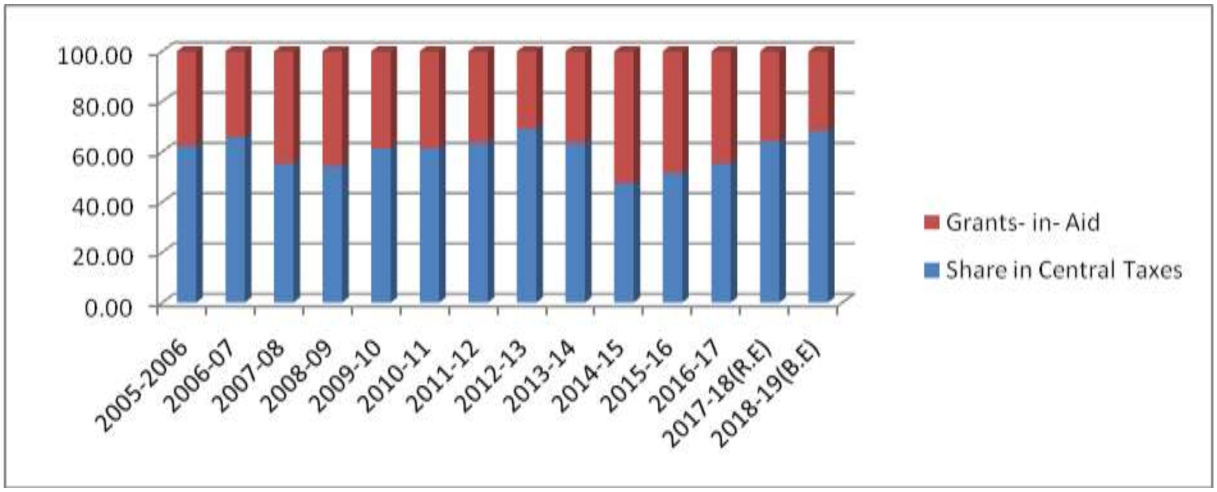
Year	Total Central Transfer (Rs. In Lakhs)	Growth Rate (%)	Central Transfer as percentage of Total Revenue
2005-06	803321	16.66	23.65
2006-07	971951	20.99	23.76
2007-08	1459704	50.18	30.72
2008-09	1564581	7.18	28.42
2009-10	1427041	-8.79	25.55
2010-11	1775399	24.41	25.30
2011-12	2000126	12.66	23.48
2012-13	2101917	5.09	21.27
2013-14	2497504	18.82	23.12
2014-15	3541330	41.79	28.93
2015-16	3961348	11.86	30.71
2016-17	4437596	12.02	31.64
2017-18(R.E)	5377832	21.19	33.75

2018-19(B.E)	6501706	20.90	41.72

Source: Budget Documents of State Government, Growth Rate & Central Transfer as percentage of Total Revenue - Calculated

The revenue received from the Central Government in the form of share in taxes and grants-in-aid have increased in Tamil Nadu in all the years except 2009-2010. Therefore the annual growth rate is negative in the year 2009-2010. Though the absolute amount has increased in 2018-19 when compared with the starting year of analysis period, lot of fluctuations can be seen between the years. Regarding the share of central transfers to total revenue of Tamil Nadu, it forms nearly 42 percentage in 2018-19(B.E) whereas in the year 2005-06, it formed 24 percentage.

Fig 1: Components of Central Transfers (in %)



Share in Central taxes is the important component of Central Transfers. In Tamil Nadu, the share of tax devolution in the total transfers varied from 47.51 per cent to 69.08 per cent during the last three FC periods. In the total resource transfers recommended by the Finance Commission-XIV, tax devolution accounted for an average of 59.78 per cent as compared to the average of 61.02 per cent share during FC-XIII period.

Table 2: Growth Rate of Devolution of Central Taxes and its Share to Tax Revenue, Total Revenue in Tamil Nadu

Year	Share in Central Taxes (Rs. In Lakhs)	Growth Rate (%)	Central Tax Share as Percentage of Tax Revenue	Central Tax Share as Percentage of Total Revenue
2005-06	501274	18.33	17.69	14.76
2006-07	639386	27.55	18.71	15.63
2007-08	806527	26.14	21.40	16.97
2008-09	851080	5.52	20.17	15.46
2009-10	875619	2.88	19.33	15.68
2010-11	1091397	24.64	18.59	15.55

2011-12	1271495	16.5	17.60	14.92
2012-13	1451969	14.19	16.93	14.69
2013-14	1585276	9.18	17.70	14.67
2014-15	1682403	6.13	17.62	13.74
2015-16	2035386	20.98	20.19	15.78
2016-17	2453776	20.56	22.21	17.50
2017-18(R.E)	3451372	40.66	27.22	21.66
2018-19(B.E)	4439019	28.62	35.29	28.49

Source: Budget Documents of State Government, Growth Rate & Share - Calculated

Growth rate of share in central taxes received by the state Tamil Nadu is high during the 14th Finance Commission period when compared with 12th and 13th Finance Commission period. Share in central taxes as percentage of tax revenue of Tamil Nadu is also high in the 14th Finance Commission period. Likewise, its percentage share to total revenue of Tamil Nadu is also high in the last Finance Commission period.

Prior to 2000, Central Government shared only Income Tax and Union Excise Duty with State Governments. From the year 2000, all central taxes are shared with state governments, i.e., Income Tax, Excise Duty, Corporation Tax, Customs Duty, Service Duty, Estate Duty, Wealth Tax, Taxes on Employment and Duties on Commodities and Services. The following table reveals the percentage share of various taxes to total share in central taxes.

Table 3 : Share in Central Taxes- Components (%)

Year	Income Tax	Excise Duty	Corporation Tax	Customs Duty	Service Duty	Others	Total
2006-07	18.95	20.71	31.21	19.50	9.59	0.03	100
2007-08	21.30	18.04	31.74	18.90	9.98	0.03	100
2008-09	20.59	16.67	31.73	19.12	10.80	1.09	100
2009-10	22.92	11.27	41.15	14.00	10.56	0.09	100
2010-11	20.66	12.72	39.09	17.49	9.97	0.08	100
2011-12	19.99	11.22	39.36	17.34	11.93	0.15	100
2012-13	21.51	11.29	35.92	16.62	14.60	0.06	100
2013-14	22.15	11.52	33.63	16.32	16.29	0.09	100
2014-15	24.94	9.13	34.92	16.17	14.74	0.10	100
2015-16	21.63	13.50	31.34	16.05	17.37	0.10	100
2016-17	22.27	16.79	32.04	12.73	16.09	0.07	100

Source: Calculated

The state Tamil Nadu receives one third of central tax proceeds from Corporation Tax. The second important component is Income Tax which is followed by Service Tax, Excise Duty and Custom Duty.

But after the introduction of Goods and Service Tax, which is an indirect tax reform measure introduced in July 2017 to ease the complex multiple indirect tax regime in India, tax revenue from IGST (30.48%) becomes the major component of share in central taxes. It is followed by CGST (22.99%), Corporation Tax (20.61%) and Income Tax (17.86%) in the year 2018-19.

Table: 4- Tax Buoyancy during XII, XIII and XIV Finance Commission period

Finance Commission	Tax Buoyancy
XII	0.68
XIII	0.77
XIV	0.64

Tax buoyancy is an indicator to measure efficiency in revenue mobilization in response to growth in GDP. If it is greater than 1, it indicates more than proportionate response of the revenue to rise in GDP. During the last three finance commission period, tax buoyancy in Tamil Nadu is less than one which indicates that less than proportionate response of the revenue to rise in GDP. Moreover, there is no significant difference in the tax buoyancy among the last three finance commission periods.

Conclusion

The analysis of Tamil Nadu finances has clearly shown that Central Government assistance in the form of share in tax and grants in aid have increased enormously over the period in the study. During this period, the relative importance of distribution of central tax proceeds has also increased. It is an undeniable fact that the Centre has been assigned larger powers than the state governments. Therefore, Central government may allow states to collect more revenue for achieving vertical balance. To remove disparities among the states, i.e., to solve horizontal imbalance problem, more grants should be given on the basis of necessity and not on the basis of political alliance and bargaining power of the state governments. That is, objectivity and impartiality should be there while providing grants. Both the centre and the state governments should exercise restraint in undertaking unwarranted expenditure commitments.

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