Report of Fifth State Finance Commission of Tamil Nadu

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Constitution of SFCs in Tamil Nadu

- As mandated under Articles 243-I(1) and 243-Y(1) of the Constitution SFCs is constituted in Tamil Nadu once in 5 years.
- Five State Finance Commissions have so far been constituted right from 23.04.1994.
- 5th SFC constituted on 1st December 2014 for the award period 2017-2022.

Action Taken by Government on SFC Recommendations

SFC	Topic	Number of Recommendations					
		Total	Accepted	Not Accepted	Under Examination	Accepted in Principle	Others
I	Devolution	22	22	-	-	-	-
	Tax and related issues	195	93	97	2	-	3
	Others	196	-	1	-	129	66
	Total	**413**	**115**	**98**	**2**	**129**	**69**
II	Devolution	36	26	-	10	-	-
	Resource base	72	60	7	5	-	-
	Others	278	197	57	25	-	-
	Total	**386**	**283**	**64**	**40**	**-**	**-**
III	Devolution	22	5	8	-	7	2
	Resource base	117	46	44	-	12	15
	Grants-in-aid	5	2	-	-	-	3
	Others	64	38	83	52	15	28
	Total	**308**	**91**	**83**	**52**	**34**	**48**

Action Taken by Government on SFC Recommendations

SFC	Topic	Number of Recommendations					
		Total	Accepted	Not Accepted	Under Examination	Accepted in Principle	Others
IV	Devolution	19	18	-	-	-	1
	Resource base	66	59	3	1	1	2
	Others	45	35	4	4	2	-
	Total	**130**	**112**	**7**	**5**	**3**	**3**
						Accepted with Modification	
V	Devolution	**27**	**25**	**1**	**-**	**1**	**-**
	Resource base	**108**	**100**	**4**	**-**	**4**	**-**
	Others	**26**	**25**	**2**	**-**	**5**	**-**
	Total	**161**	**144**	**7**	**-**	**10**	**-**

Assessment of Finances of RLBs

- Ministry of Panchayati Raj on Status of Devolution
  - TN ranks 2nd in Financial Devolution
  - 11th in terms of Functional Devolution
- Devolution by tiers
  - 2nd for Village and Block Panchayats
  - 6th for District Panchayats
- Interesting findings in MIDS study on "Mapping Functions, Finances and Functionaries in Rural India"

Receipts and Expenditure of RLBS 2010-11 to 2014-15

- Receipts:
  - Tax – 5 per cent
  - Non-Tax – 7 per cent
  - SFC – 59 per cent
  - CFC – 9 per cent
  - Assigned/Pooled Assigned Revenue – 9 per cent
  - Others – 11 per cent
- Expenditure:
  - Salaries – 13 per cent
  - Capital Expenditure – 33 per cent
  - Others – 55 per cent
- Scheme receipts for VPs range between 67.38 per cent and 53.57 per cent
- Per VP total receipts ranged between Rs 44.89 lakh and Rs 76.47 lakh

Key recommendations on RLBs

House Tax

- GoTN to take up with GoI levy of service charges on Central Government properties
- Quinquennial revision of taxes to be statutorily ensured
- Adoption of technology and other measures to enhance collection
- Tribunals to decide appeals

Profession Tax

- Recommendation of 14th CFC to remove the Constitutional maximum limit on Profession Tax and to allow the Parliament by law to raise the maximum limit to Rs 12,000 reiterated.
- Improved co-ordination with CT, Labour Departments, EPFO and Professional SROs to identify more persons liable for tax

Tax Revenue of RLBs (Contd)

Advertisement Tax

- Power currently vested with the District Collectors to grant permission for erecting hoardings and displaying advertisement boards, may be delegated to Revenue Divisional Officers.
- Application for grant of permission should be accompanied by proof of payment of tax and fees into the account of the local body concerned.
- Local Bodies may be empowered to remove advertisements which have not received the requisite permission.

Non – Tax Revenue

Water Charges:

- VP's income:expenditure coverage ratio for Drinking Water supply was between 7.46 and 10.82 per cent between 2010-11 to 2014-15
- VPs should be encouraged to enhance water charges by including enhancement of water charges as one of the factors based on which allocations from the Capital Grant Fund/ Pooled Fund for Deficit RLBs would be considered.
- Water metering both for household supply and bulk supply by TWAD
- Bus Stand fees last revised in 2002 may be enhanced by 50 per cent.
- A special Country Planning Unit may be created at the district level to provide technical support for the grant of layout and building plan approvals in rural areas.
- Regularization of unapproved layouts based on certain norms should be expedited to ensure that local bodies receive revenue. However, necessary regulatory and legal measures must also be taken to ensure that the problem of unapproved layouts does not recur.

Assigned Revenue

- Pooling of assigned revenues must be done away with. (Recommendation not accepted)
- The assigned revenues should be distributed to the Local bodies based on the place where they actually accrue, after deduction cost of collection. (Not accepted)
- Levy of Surcharge on Stamp Duty on certain (i)Agreement (ii) Power of Attorney (iii) Release of benami right (iv) Release of right infavour of partners and(v) Settlement – recommendations of 3rd and 4th SFC reiterated.
- Surcharge on stamp duty should be levied on registration of "Construction Agreements" and "Settlement among Family Members"

Mines and Minerals

- Proportion of revenue from minor minerals to be shared with local bodies should be 60 percent to leave the government with an incentive to levy and collect this revenue more effectively and at higher rates
- 60 percent of the revenue from sand quarrying should be transferred to local bodies
- Local body share of minor mineral based revenue should be distributed in following proportion: 75 percent to the local body where the quarry is located and 25 percent to be distributed by the District Collector to the neighboring local bodies impacted by quarrying.

Peri Urban Panchayats

- Tamil Nadu Panchayats Act 1994 be suitably amended,
- To classify Peri Urban Villages based on location close to Urban centres and population
- To enable levy of House tax at rates on par with adjacent Urban Local Bodies
- To enable levy of Vacant Land Tax

Entertainment Tax Compensation

- State Government should compensate Local Bodies for loss of Entertainment Tax revenue in case a separate legislation enabling local bodies to collect Entertainment Tax is not passed.
- This compensation should extend to 90 per cent of the State GST collected on Entertainment Services and be distributed on the destination principle
- Not accepted by Government, as it was decided to enact legislation to enable LBs to collect Entertainment Tax

Accounts and Audit

- Government should enable treasury based operations of local body accounts instead of bank based operations through the Central Plan Scheme Monitoring System (CPSMS) and the Integrated Financial and Human Resources Management System being implemented in Tamil Nadu
- This would improve accountability in local bodies and also ensure more efficient use of fiscal resources
- Recommendation not accepted by Government as it may curtail the freedom available to local bodies and since VPs may find it physically difficult to operate treasury accounts.

SCHEME OF DEVOLUTION

First SFC

Devolution was divided into Two pools	
Pool A	• Taxes which belong local bodies but collected by Government – surcharge on stamp duty, local cess and local cess surcharge and entertainment tax – to be devolved to local bodies (Assigned Revenue). • 90% devolved, 10% retained by Government as cost of collection (1997-98 - Rs 380 crores)
Pool B	•States Own Tax Revenue to be apportioned to local bodies: 8% in 1997-98; 9% in 1998-99; 10 % in 1999-2000; 11% in 2000-01 and 12% in 2001-02. (1997-98 – Rs 620 crores) •Government accepted devolution of 8% of SOTR for whole award period

Second SFC

Pool A	Assigned Revenue – to be shared with the local bodies
Pool B	Share of Net SOTR to local bodies: •8 % in 2002-03 and 2003-04 •9 % in 2004-05 and 2005-06 and •10% in 2006-07 • Government accepted devolution of 8% for award period
Recommended sharing of 5% of States's share of Central Taxes with local bodies, which was not accepted by Government.	

Third SFC

Pool A	• Assigned Revenue – to be shared with local bodies • Government decided to pool assigned revenue for rural local bodies at State level
Pool B	• Net SOTR – 10 % to be shared with local bodies. • Government accepted the recommendation with modifications – 9% in 2007-8 & 2008-9; 9.5% in 2009 -10; and 10% in 2010-11 & 2011-12
Pool C	•Specific purpose grants for local bodies of 0.5 to 1% of SOTR

Fourth SFC

Pool A	• Assigned Revenue – recommended transfer without diversion to State level pools for infrastructure creation in local bodies • Not Accepted
Pool B	• Sharing from net SOTR recommended at 10 %. • Accepted by Government.

Fifth SFC – Vertical Devolution

Fifth SFC recommended that the existing overall vertical devolution proportion of **10 per cent** of the net State's Own Tax Revenue (SOTR) be retained for the award period

Allocation between RLBs and ULBs

SFC	% of Pool B Fund to General Devolution for Equalization and Incentive Funds	Balance % of Pool B fund distributed between	
		RLB	ULB
I	15	60	40
II	13	58	42
III	-	58	42
IV	-	56	44
V	-	56	44

Horizontal Distribution Formula among RLBs

	Criterion	Weight
1.	Population as per 2011 Census	60 per cent
2.	Area	15 per cent
3.	Scheduled Caste/Tribe Population	15 per cent
4.	Per Capita Consumption Expenditure Distance	10 per cent
	Total	100 per cent

Distribution Between Different Tiers of RLBs

SFC	District Panchayats	Panchayat Unions	Village Panchayats
I	14% (as block grant)	43%	43%
II	To meet salary expenditure	40%	60%
III	8%	32%	60%
IV	8%	32%	60%
V	8%	37%	55%

What the Aggregate Numbers Hide

- Internal variations amongst RLBs and ULBs
  - Out of 12,524 VPs, only 1552 were in surplus for all five years, while 238 were deficit in all 5 years
  - Out of 385 Panchayat Unions, 140 surplus in all five years and 31 in deficit in all 5 years.
  - Corporations – 8 were in surplus in all 5 years, while one corporation was in deficit for 3 out of the 5 years
  - Municipalities - 97 were in surplus all 5 years and only 4 in deficit all 5 years
  - TPs – 426 in surplus all five years and 33 were in deficit in all 5 years
- Hence the 5th SFC considered special measures for chronically deficit LBs

Deductions from Devolution

- The practice of deducting funds from the devolution beyond the purposes and mechanisms recommended by the SFC should be eschewed
- Interception from devolution should be exercised only as a last resort measure and only to meet statutory dues, court ordered dues, loan dues, pension dues, and in exceptional cases, electricity and water supply related charges
- Interception of SFC devolution should be only to the extent of devolution due to that particular local body, without affecting the devolution flowing to other local bodies

Capital Grant Fund

- A ~~Capital Grant Fund may be established to replace the~~ Infrastructure Gap Filling Fund (IGFF), into which 20 per cent of the aggregate devolution intended for RLBs would be paid.
- Of this Fund, 20 per cent would be set apart for taking up projects which are deemed to be of importance of the State level.
- The balance 80 per cent would be distributed district wise, based on the formula adopted for horizontal distribution amongst District Panchayats.
- The allocation of these funds project wise would be decided by the District Planning Committee

Pooled Deficit Fund

- 10 per cent of the overall devolution intended for RLBs be constituted into a Pooled Fund for Deficit RLBs.
- 40 per cent of Fund, to be disbursed only amongst those Panchayat Unions and Village Panchayats which have been in deficit for at least 3 of the last 5 years based on formula.
- 40 per cent of the Fund to be allocated:
  - 20 per cent retained by the DRD and
  - 20 per cent distributed amongst District Collectors

  To provide grants to those Village Panchayats and Panchayat Unions who have special problems which cannot be addressed under any of the existing transfer mechanisms or schemes.
- 20 per cent of the Fund to TWAD Board as support for maintenance of CWSS

Total Devolution Amounts

Gross SOTR 2017-18: Rs.1,03,089.44 crore

Total fund flow to Rural and Urban Local Bodies:

2017-18: Rs. 10,532.39 crore

Award Period 2017-22: Rs.65,473.84 crore

Per Capita Devolution

SFC	Year	Average Per Capita Devolution during the award period (In Rs.)
I	1997-2002	140.26
II	2002-2007	240.68
III	2007-2012	588.49
IV	2012-2017	973.80
V	2017-2022	1818.63

Thank you

Recommendations of Fifth SFC

Total number	161
Fully accepted	144
Accepted with modifications	10
Not accepted	7

Chronology of Tamil Nadu State Finance Commissions

SFC	Award Period	Chair Person	Date of Constitution	Date of submission of Report	Date of submission of ATR by the Government of Tamil Nadu
I	1997-98 to 2001-02	R. Arumugham, IAS (R)	23.04.1994	29.11.1996	28.04.1997
II	2002-03 to 2006-07	Sukavaneshvar, IAS	01.12.1999	21.05.2001	08.05.2002
III	2007-08 to 2011-12	MA Gowrishankar, IAS	02.12.2004	30.09.2006	10.05.2007
IV	2012-13 to 2016-17	K. Phanindra Reddy, IAS	01.12.2009	29.09.2011	14.05.2013
V	2017-18 to 2021-22	S. Krishnan, IAS	01.12.2014	27.12.2016	24.03.2017

Terms of Reference of Successive SFCs

- TOR based on the provisions of Articles 243 (I) and 243 (Y) and relevant Local Bodies Acts.
- Commissions to make recommendations on the principles which should govern:
  - Distribution between State and Local Bodies of net proceeds of taxes, duties, tolls and fees leviable by State
  - Allocation between local bodies at all levels of their respective shares of such proceeds
  - Determination of taxes, duties, tolls and fees which may be assigned to, or appropriated by the local level governments
  - Grants-in-aid to local bodies from Consolidated Fund of the State
  - Measures needed to improve the financial position of local bodies

Additional Terms of Reference

2nd SFC was also requested to:

- Analyse repayment of loans extended by the Government to the local bodies
- Suggest measures and changes needed in the payment of pension to the retired employees of local bodies
- Assess the accountability of the local bodies in utilizing the resources raised or received from Central, State and other agencies

3rd SFC was also asked to focus on:

- Reclassification of local bodies other than Town Panchayats
- Functions of Grama Sabhas in Village Panchayats

No additional Terms of Reference for 4th and 5th State Finance Commissions

Fifth SFC - Methodology and Approach

- Evolving procedures for functioning of State Finance Commission
- Collecting data through questionnaires from
  - Rural and Urban Local Bodies
  - Elected Representatives
  - NGO's
  - District Collectors
  - Line Departments / Stake Holders
  - Heads of Departments governing Urban and Rural Local Bodies
- Maintenance and compilation of data from Local Bodies collected online through the Commission's website
- Interaction with elected representatives of Local Bodies and officials of Government Departments, NGOs and District Collectors
- State / National level seminars/workshops in co-ordination with institutions Field visits and visits to other states for adopting best practices.
- Engaging expertise for special / issue based studies
- Preparation of Report and submission to the Government.

Procedural Recommendations

- Follow up of past recommendations
- Establishing separate sections in RD & PR and MAWS Department to follow up
- Permanent SFC Cell
- Data collected by SFC to be taken up for further analysis by hosting on GoTN website

Analysis of ULB Finances

- Total receipts of ULBs in 2014-15 was Rs 15039 crore and expenditure was Rs 15,230 crore
- From 2010-11 to 2014-15 – ULBs had revenue surpluses and till 2013-14 they had overall surpluses
- Corporations ran a revenue deficit in 2014-15 and overall deficits in 2013-14 and 2014-15, while Municipalities and Town Panchayats were in surplus through out.
- Own Revenues (including assigned revenue) ranged between 36.43 and 40.98 per cent. Corporations ranged between 42.56 and 54.47 per cent.
- SFC devolution was 23.74 and 26.83 per cent of total revenue receipts (including scheme grants).
- Property tax was between 33 and 39 per cent of own revenue of ULBs. Profession tax was the second largest source
- Total non-tax revenue exceeded own tax revenue of ULBs in the period under review.

Analysis of ULB Finances 2

- Town Panchayats had the best performance in Property Tax current collection – ranging between 83.13 and 89.29 per cent
- Corporations' Property Tax collection ranged between 70.64 per cent and 77.34 per cent
- Per capita property tax demand ranged between Rs 3000 and 3084 in Corporations and Rs 1124 and 1377 for Municipalities and Rs 393 and 509 for Town Panchayats
- Tamil Nadu's Property tax to GSDP ratio in 2012 was 0.16 per cent, much lower than AP (0.4 per cent), Maharashtra (0.5 per cent), Karnataka (0.26 per cent) and Gujarat (0.20 per cent).

ULB Tax Rates and Revisions

- Target for property tax collection for ULBs should be fixed to reach 0.60 percent of GSDP by the last year of award period i.e., 2021-22. (Accepted with modification that target would be 0.25 per cent)
- GIS mapping of all ULBs to bring left out properties to assessment should be completed in all Municipalities and Corporations.
- Special drive to cover all Town Panchayats with GIS mapping during the award period with a special fund of Rs.35 crore recommended from devolution for TPs for this purpose.
- State Government should take up with Government of India necessary amendments to Article 285 of the Constitution to make Central Government buildings liable for property tax.
- In the interim, Government of India should make statutory provisions enabling levy of service charges to replace the executive instructions which have proved ineffective.

ULB Tax Rates and Revisions 2

- Differentiation regarding the methodology of tax calculation between the properties belonging to the period prior to 1993 and post 1993 should be done away with and all urban properties should be treated alike
- Area Based Property Assessment System should be introduced for the property tax.
- Value of the property should be determined based on the guideline value of the land and the value of the building, based on the built up area, type and quality of construction, number of floors and usage.
- Government should mandate the adoption of the new methodology during the next revision of property tax.
- Clarification on Section 81(A) to ensure that it is used as a mechanism to protect revenue

ULB Tax Rates and Revisions 3

- Betterment Levies should be implemented for urban infrastructure works undertaken by ULBs to ensure more effective land value capture on a sustainable basis, along the lines of the existing provisions under the Tamil Nadu Highways Act, 2001
- Entertainment Tax levied by local bodies permitted as per amended Entry 62 in State List as per 101st Constitution Amendment enabling GST.
- Government to take urgent action to legislate and permit Local Bodies to levy and collect Entertainment Tax

Horizontal Distribution Formula among ULBs

	Criterion	Weight
1.	Population as per 2011 Census	65 per cent
2.	Area	15 per cent
3.	Per Capita Consumption Expenditure Distance	10 per cent
4.	Proportion of Slum Population	10 per cent
	Total	100 per cent

Distribution Between Different Tiers of ULBs

SFC	Town Panchayats	Municipalities	Municipal Corporations
I	38%	31%	31%
II	35%	32%	33%
III	29%	41%	30%
IV	31%	29%	40%
V	31%	29%	40%

Capital Grant Fund and Pooled Fund for Deficit ULBs

- CGF recommended at 15 per cent of devolution to ULBs to replace IGFF of 7 per cent
- Distributed amongst the three tiers of ULBs and sanctions to be accorded as per guidelines issued by Government.
- Pooled Fund for Deficit ULBs recommended at 5 per cent of devolution to ULBs to replace the O & M Gap Filling Fund of 3 per cent.
  - 40 per cent to deficit ULBs
  - 40 per cent with HoDs for special grants with priority to clear pending water supply and electricity bills
  - 20 per cent to TWAD Board of CWSSs maintenance
- Pooled Fund for Deficit ULBs recommendation was not accepted and instead O&MGFF was continued with enhanced share of 5 per cent.

ULBs: Incentive Fund

- 5 per cent out of aggregate devolution intended for ULBs to be set apart for the incentive fund
- ULBs who have improved their Property Tax collection by more than 20 per cent eligible to receive incentive as a matching share of the collection in excess of 10 per cent growth
- Any undisbursed amount to lapse to Government
- Government accepted recommendation with modification that undisbursed amounts would be left with HoDs for provision of infrastructure and amenities

Criteria for Horizontal Distribution

First SFC

Criterion	Panchayat Union	VPs	TPs	Municipality	Corporation
Total Population	50%	50%	45%	45%	40%
SC & ST Population	25%	15%	20%	10%	10%
Financial Viability	25%	-	-	-	-
Per capita House Tax Collection Performance	-	15%	-	-	-
Core Civic Services Deficiency	-	20%	-	-	-
Per Capita Own Resources	-	-	15%	15%	15%
Per Capita Expenses on Core Services	-	-	20%	30%	35%
Total	**100%**	**100%**	**100%**	**100%**	**100%**

Second SFC

Criterion	Panchayat Union	VPs	TPs	Municipality	Corporation
Total Population	60%	60%	50%	50%	50%
SC & ST Population	10%	10%	10%	10%	10% (Slum population)
Agricultural Labourers	10%	10%	-	-	-
Area	10%	10%	-	-	-
Asset Maintenance	-	10%	20%	10%	10%
Resource gap on inverse per capita land revenue	10%	-	-	-	-
Per capita own income	-	-	20%	20%	20%
Salary and Pension expenses	-	-	-	10%	10%
Total	**100%**	**100%**	**100%**	**100%**	**100%**

Government did not accept the criteria recommended by 2nd SFC and determined following criteria

Total Population	40%
Women Population	40%
SC / ST Population including Slum Population	20%
Total	**100%**

Third SFC

Criterion	Panchayat Union	VPs	TPs	Municipality	Corporation
Total Population	32%	32%	32%	32%	32%
Women Population	32%	32%	32%	32%	32%
SC / ST Population and Slum Population	16%	16%	16%	16%	16%
Area	20%	20%	10%	10%	10%
Debt Burden	-	-	10%	10%	10%
Total	**100%**	**100%**	**100%**	**100%**	**100%**

Fourth SFC

Criterion	Panchayat Union	VPs	TPs	Municipality	Corporation
Total Population (2011 Census)	60%	60%	80%	80%	80%
SC / ST Population	20%	20%	-	-	-
Area	20%	20%	15%	15%	15%
Debt Outstanding	10%	10%	5%	5%	5%
Total	**100%**	**100%**	**100%**	**100%**	**100%**

Fifth SFC

Criterion	Panchayat Union	VPs	TPs	Municipality	Corporation
Total Population (2011 Census)	60%	60%	65%	65%	65%
SC / ST Population	15%	15%	-	-	-
Slum Population	-	-	10%	10%	10%
Area	15%	15%	15%	15%	15%
Per Capita consumption expenditure distance	10%	10%	10%	10%	10%
Total	**100%**	**100%**	**100%**	**100%**	**100%**