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Trends and Perspectives of Urban Public Finance in Select Countries and India

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Abstract

Urban Local Government Finances have received lesser attention in public finance literature. This paper attempts to provide an outline of urban public finances in select countries of the West in comparison to that in India. In advanced countries like the European nations and America, the systems of public finances are well structured and the roots of the same are well laid down within the administrative structures – particularly with respect to the unitary or federal structures. However, there is wider range of financial structures – both revenue and expenditure - that can be seen in these countries. India's local government fiscal structure has changed after the 74th Constitutional Amendment Act in 1992. The renewed focus on urban areas as growth engines, thereafter, has to find its base on stronger revenue base and financial management. Local government finances of cities – both on revenue and expenditure side - still present a weak base and loose foundations in comparison to those that of other countries and, therefore, point to reforms in these institutions.

Key Words: Urban Public Finances, Local government, Tax base, Revenue and expenditure.

1. Introduction

Public Finance is a specialised subject concerning public policy wherein principles of finance, policy and economics are often applied with respect to the finances of governments – primarily central (or, federal) and provincial (or, state) governments. Given the importance of these two tiers of governments, in terms of both power and finances, the enquiry of public finance has primarily confined to finances of these governments and inter-flows together with institutional aspects and so is the research on theory and practice (Musgrave and Musgrave 1989). Local Government Finance, a sub-stream of public finance, pertains to the finances of local governments (in both rural and urban areas) in relation to the upper tiers of governments i.e., federal and state governments.

The finances of Urban Local Bodies (ULBs) have been assuming much greater importance with the urban areas increasingly becoming important in

terms of not only population share but also economic wealth¹, and with which we concern in this paper. With the municipalities/municipal corporations acting as centres of government in urban areas, urban local government finance is also referred to, some times, as municipal finance in India. However, the performance (both physical and financial) of urban local governments may vary between the municipalities (of cities) and municipal corporations (of larger urban agglomerations) as well as amongst themselves.

Finances of ULBs or Urban Public Finance broadly relates to the evolution and structure of finances of local governments, and the array of fiscal relations of local governments (Bahl and Linn 1992). However, given the existence of ULBs in the tiered structure of government and their interface with the citizens, the inquiry of urban public finance also includes the dimensions like institutional arrangements of decision making and fiscal management, reforms and accountability, transparency and gap-financing (Bhatia 2003). Therefore, urban public finance systems vary across the countries substantially due to a variety of public finance structures and political/ institutional set-ups. For example, the revenue generation powers and expenditure responsibilities should be an integrated package which varies to suit the different circumstances. Likewise, inter-governmental transfers provide a spectrum of varieties of fiscal arrangements across the countries: whereas well designed packages and arrangements can enable local governments to function effectively, unsuitable arrangements may hamper their performance to a good extent.

Given the variation of fiscal and institutional arrangements across the countries, it is useful to understand the way they are organised in order to get a perspective and then look at them in the Indian context, which is what attempted in this paper. Across the countries, there are differences in the political structures of government that can be distinguished as unitary and federal systems. Unitary systems have one central government and several local governments, between which the powers of decision making and finances are distributed; whereas federal systems have another tier of states/ provinces with which the central/ federal government shares its power of decision making, finances and other resources. The fiscal relations between local and provincial (and, provincial and state) can be better understood through a review of the assigned functions, which is provided in the next section. In the section that follows, we present the structure of local government finances in a few select countries: Australia, Canada, Denmark, Germany and the United States of America. In this section, we provide an overall analysis of the patterns found in the local government revenues and expenditures and the transfer arrangements in the select countries. In the final section, we will carefully examine the similar arrangements in the context of India, which can be broadly compared with the description made in the earlier section.

¹ In the developed economies, cities typically contribute to 90% of population and an equivalent proportion of the economic activity; in India, urban population assumes roughly 30% of the total population and it is estimated that they contribute to about 60% of the country's GDP.

2. Patterns of Municipal Functions/Responsibilities in Select Countries

Although the responsibilities of municipal bodies differ between countries, some common patterns can be found. Bahl and Linn (1992) documents some international experiences in this regard, based on data pertaining to various years between 1960 and 1982. These cover cities entrusted with extensive, moderate and little responsibilities by the higher levels of government. As can be seen from the Tables 1, 2 and 3, the most common functions of municipal governments internationally are: street cleaning and lighting, refuse collection, parks and recreation, markets and abattoirs, cemeteries, fire protection, and minor public disease prevention services. In Municipalities having extensive and moderate responsibilities, water supply, sewerage and drainage, and roads are also common. Mass transportation - rail-based, in particular - is rarely a function of Municipalities. Primary education appears to be a common function only in cities entrusted with extensive service responsibilities.

Table 1: Local Public Responsibility for Services in Selected Cities with Extensive Responsibility (No. of Sample Cities* = 12)

	Primary Responsibility	No. of Cities with Secondary Responsibility	No Responsibility
<i>Public Utilities</i>			
Water Supply	12	-	-
Sewerage & Drainage	12	-	-
Electricity	5	-	7
Telephone	3	-	9
<i>Social Services</i>			
Primary education	10	2	-
Health	5	7	-
Social Welfare	2	8	2
Housing	3	9	-
<i>Transportation</i>			
Highways and roads	12	-	-
Street lighting	9	-	3
Mass transportation	4	2	6
<i>General urban services</i>			
Refuse collection	12	-	-
Parks and recreation	11	1	-
Markets and abattoirs	9	-	3
Cemeteries	9	-	3
Fire protection	10	-	2
Law enforcement	-	2	10

* Include Francistown (Botswana), Bogota and Cali (Colombia), Ahmedabad, Mumbai, Kolkata and Delhi (India), Jakarta (Indonesia), Nairobi (Kenya), Seoul, Daegu, and Gwangju (Republic of Korea)

Source: Bahl & Linn (1992)

Table 2: Local Public Responsibility for Services in Selected Cities with Moderate Responsibility (No. of Sample Towns* = 8)

	Primary Responsibility	No of Cities with Secondary Responsibility	No Responsibility
<i>Public Utilities</i>			
Water Supply	8	-	-
Sewerage & Drainage	8	-	-
Electricity	-	-	8
Telephone	1	-	7
<i>Social Services</i>			
Primary education	2	3	3
Health	2	5	1
Social Welfare	-	6	2
Housing	2	2	4
<i>Transportation</i>			
Highways and roads	5	2	1
Street lighting	6	1	1
Mass transportation	1	1	6
<i>General urban services</i>			
Refuse collection	8	-	-
Parks and recreation	7	1	-
Markets and abattoirs	8	-	-
Cemeteries	8	-	-
Fire protection	7	1	-
Law enforcement	-	1	7

* Include Cartagena (Colombia), Chennai (India), Casablanca (Morocco), Karachi (Pakistan), Manila (Philippines), Bangkok (Thailand), Lusaka and Kitwe (Zambia)

Source: Bahl & Linn (1992)

Table 3: Local Public Responsibility for Services in Selected Cities with Little Responsibility (No. of Sample Towns* = 10)

	Primary Responsibility	No of Cities with Secondary Responsibility	No Responsibility
<i>Public Utilities</i>			
Water Supply	1	4	5
Sewerage & Drainage	3	3	4
Electricity	-	-	10
Telephone	-	-	10
<i>Social Services</i>			
Primary education	2	3	5
Health	-	9	1
Social Welfare	-	5	5

Housing	-	2	8
<i>Transportation</i>			
Highways and roads	6	4	-
Street lighting	8	-	2
Mass transportation	-	3	7
<i>General urban services</i>			
Refuse collection	10	-	-
Parks and recreation	10	-	-
Markets and abattoirs	10	-	-
Cemeteries	10	-	-
Fire protection	9	n.a.	n.a
Law enforcement	-	3	7

* Include Teheran (Iran), Kingston (Jamaica), Lagos (Nigeria), Gujranwala (Pakistan), Lima (Peru), Davao (Philippines), Tunis (Tunisia), Valenica (Venezuela), Kinshasa and Bukuru (Zaire)

Source: Bahl & Linn (1992)

The international patterns regarding the assignment of functions to urban local bodies point to some broad regularities which can be explained in terms of the theory of fiscal federalism, which is concerned with inter-governmental relationships including political economy of the same (Mundle 2000). It is obvious that functions such as street cleaning are universally municipal, just as defence is universally considered as belonging to the domain of national governments. Logically speaking, the various functions exercised by governments at different levels in a federation can be portrayed on a scale with street cleaning at bottom and defence at top. On the similar lines, but to the inverse, the refuse collection may remain at top and law enforcement may remain at bottom in the case of local government.

Services like refuse collection, markets, abattoirs, cemeteries, parks and recreation as well as basic services like water supply, sewerage and roads are within the domain of urban local governments. Social services like health, education and welfare as well as infrastructure services like electricity and telecom are not relegated much importance and are considered to be outside the purview of urban local governments. Transportation and housing keep emerging as key areas determining urban growth and several local governments started deploying resources towards providing support infrastructure for the same.

3. Patterns of Local Government Finances in Select Countries

Although it is easier to find the similarities of devolution of essential functions across the cities in the cross-sectional study of Bahl and Linn (1992), the finances have not been studied empirically in that fashion i.e, cross-sectional studies of the city finances across the world. This is because of the fact that the local government finances are more complex than local government functions. The municipal government finances are largely determined by the existing legal and institutional framework within which revenues are raised and transferred, and expenditures are made and devolved across the governments. In this

framework, inter-government transfers assume significance because of their presence, at least to some extent, in a majority of the countries.

However, it is well acknowledged that when finances follow functions, the financial systems are simpler and easier to comprehend and work towards better. Bahl and Linn (1992), therefore, suggest the following simple framework for the identification of revenue sources that are appropriate to finance particular types of municipal expenditures:

- (1) Where the benefits of local public services are measurable and accrue to readily identified individuals within a jurisdiction, user charges are the appropriate financing instruments.
- (2) Local public services such as administration, traffic control, street lighting and security which are services to the general public in the sense that identification of beneficiaries and measurement of benefits and costs to individuals are difficult, are most appropriately financed by taxes on local residents.
- (3) The cost of services for which significant spillovers to neighbouring jurisdictions occur e.g., health, education and welfare, should be borne by substantial state or national intergovernmental transfers.
- (4) Borrowing is an appropriate source to finance capital outlays on infrastructure services, particularly, public utilities and roads.

In spite of the uniformity in principles applicable to municipal functions laid down by Bahl and Linn (1992), one can find that the functional base of local bodies vary from one to another and one state to another and one nation to another. These are, to some extent, laid down in the political economic structure of governments. However, apart from functional base, another important component determining urban local government finances is the transfers or grants from upper tiers of governments and autonomy of decision making with respect to taxes and charges levy, which also play an important role. In the following sections, the functional base and finances (revenue and expenditure structure) of urban local bodies in select countries are examined and presented for providing an overview. A snapshot view of the same in the Organisation of Economic Co-operation and Development (OECD) countries is provided in Box 1.

Box 1: Municipal Finances in OECD Countries

Table 4 provides a picture of local government finances in OECD countries. Property tax is the dominant local tax in Australia, Canada, Ireland, New Zealand, United Kingdom and the United States. These countries have either less important local governments (e.g., Ireland, Australia) or local governments that are more dependent on inter-governmental transfers (e.g., Canada, U.K.).

Income tax is the most important local tax in Austria, Belgium, Luxembourg, Switzerland, Norway, Sweden, Denmark, Finland and Japan. A small number of countries have a balanced local tax structure. These include France, Spain, Portugal,

Italy and Turkey. Countries influenced by the Anglo-Saxon tradition appear to depend heavily on property taxes and inter-governmental transfers.

Table 4 The Pattern of Local Taxation in OECD Countries 1988

Local Tax as per cent of					
Country	Total tax	Local Revenue	Income Tax	Sales Tax	Property Tax
Australia	3.3	43.2	0.0	0.0	99.6
Austria	10.8	52.7	50.6	33.2	9.2
Belgium	5.0	37.4	76.8	0.0	0.0
Canada	9.1	39.1	0.0	0.3	84.5
Denmark	30.0	49.6	92.1	0.1	7.8
Finland	25.6	45.0	99.1	0.1	0.9
France	8.9	44.3	14.7	4.9	34.2
Germany	8.7	36.7	81.9	0.3	17.1
Greece	9.9	n.a.	0.0	33.2	0.0
Ireland	2.2	6.2	0.0	0.0	100.0
Italy	1.8	3.6	41.7	22.3	0.0
Japan	25.9	n.a.	61.0	11.5	22.4
Luxembourg	11.9	55.4	80.5	15.1	3.7
Netherlands	2.2	5.9	0.0	1.3	73.5
New Zealand	5.5	n.a.	0.0	1.4	92.4
Norway	20.9	n.a.	88.9	0.0	7.6
Portugal	5.4	n.a.	43.6	29.4	23.7
Spain	11.3	57.3	31.7	29.6	27.1
Sweden	27.6	61.1	99.6	0.4	0.0
Switzerland	15.8	n.a.	86.3	0.4	13.3
Turkey	10.1	n.a.	41.0	37.4	3.4
U.K.	10.5	32.6	0.0	0.0	100.0
U.S.A.	12.2	40.0	6.0	15.3	74.2

Source : OECD (1990, 1991)

3.1 Patterns of Local Government Revenues

It is well laid in public finances theory that the expenses matching with functions should also match with revenues. The matching of revenues with expenses is an essential indicator of state of financial health of local governments and a necessary requirement in some of the countries. However, conceptually there exist potential mis-matches due to the design of the system such that there is devolution of responsibility but not equivalent revenue (which is known as vertical imbalance) and that there is variation in the revenue generation capacity of respective local government (which is known as horizontal imbalance).

The theory on the nature and causes of vertical and horizontal imbalances is well laid and quite extensive due to the widely varying financial and legal institutions. The imbalance of local government finances is normally plugged-in through the design of a system of inter-governmental fiscal transfers. Inter-government fiscal transfers assume greater importance in

local government finances, as they sometimes assume a significant proportion of the expenditures and are essential for meeting with the development goals of local governments.

It is a standard practice that most of the local governments in several countries rely upon tax revenues as a major source of income, within which they depend upon the reliable and stable taxes like the property tax universally, and, to some extent, on income tax, where it is levied and collected. Buoyant taxes like those on flow of goods and services does not provide a major income, whereas this tax together with income tax holds a major proportion of tax revenue of central/federal governments.

Table 5 gives a comparative picture of local government expenses in the select countries. In all these countries, tax revenue is the major source although it varied between 30 percent in Germany and 45 per cent in Canada. However, among the taxes, property tax, which is considered as a stable income source, is an important source in Australia, Canada and the US. Denmark and Germany are characteristically dependent upon income and profit taxes. Interestingly, tax revenue on goods and services, which is a buoyant tax, is almost zero in all the countries excepting the US, where it is sizable (8 per cent).

Non-tax income also contributes to a good amount of revenue in Australia, Germany and the US, whereas it contributes modest in Canada (17 per cent) and low in Denmark (8 per cent). Almost a similar pattern of revenue contribution can be found in the case of municipal fees, charges and sales. Interestingly, capital revenue is not a revenue source in Canada, Denmark and the US and only marginal revenue source in Australia and Germany.

Grants, as claimed earlier, show their relatively greater importance in the total local government revenues of all the countries. Their importance is much stronger in Canada, the US, Denmark and Germany, wherein their share is between 32 and 39 per cent of total revenues but it is relatively modest in Australia (17 per cent). This underscores the existence of devolution principles.

An interesting feature of the local government revenues is their share in the total government revenue and the GDP, both of which reflect the strength and presence of local government system. In a relatively weak local government system like that in Australia it contributes to only 6 per cent of total government revenue (and concomitantly low contribution of only 2 per cent to GDP), but in Denmark, it contributes to more than half of the total government expenditure (and an almost one-third of the GDP); elsewhere, it contributes in the order of about 20 per cent of total government expenditure and about 8 per cent of the GDP.

Table 5: Local Government Revenues in Select Countries, 1998

	<i>(per cent distribution)</i>				
	Australia	Canada	Denmark	Germany	USA
<i>Total Tax</i>	44.8	43.2	50.9	30.6	38.9
-Income and profit	-	-	47.7	23.9	2.4
-property	44.8	40.3	3.2	6.4	28.4
-goods and services	-	0	0	0.3	8.1
-other taxes	-	2.8	-	0.1	-
<i>Non Tax Income</i>	32.6	17.5	8.1	32.8	23.9
-enterprise & property	3.0	2.9	1.2	3.4	10.8
-fees, sales & fines	24.3	13.9	5.8	24.7	11.7
-other non-tax	5.3	0.7	1.1	4.7	1.4
<i>Capital Revenue</i>	6.2	-	0.7	4.2	0.1
<i>Grants</i>	16.4	39.3	40.3	32.5	37.0
<i>Total Revenue</i>	100	100	100	100	100
<i>Total Revenue in consolidated government revenue (%)</i>	5.9	17.9	54.3	18.8	25.0
<i>Total Revenue as % of GDP</i>	2.1	8.0	31.1	8.9	9.0

Source: McLean (2002), Boadway and Watts (2004)

3.2 Patterns of Local Government Expenditures

Unlike the revenue sources, which present a good structure/arrangement and sources, expenditure is not well structured and varies over countries and time with the assignment of functions, which itself undergoes change. In fact, expenditure is an area, where the local governments have little control and lesser discipline. Federal/central governments of several countries tend to devolve the functions to lower tiers of governments but do little when it comes to finances. Fiscal imbalances that arise in several systems is on account of such one-sided devolution – devolution on expenditure side but non-devolution on income side.

The table 6 indicates the expenditure structures of local governments of five select countries that have strong local government financial systems, albeit with varying degrees of service provision and varying extent of inter-government transfers. Almost all of them have some basic level of local government expenditure on the provision of general public services (in a range of 4 to 14 per cent) and on recreation, culture and religious (3 to 18 per cent), but the expenditure on other items are markedly different among these countries.

Whereas public safety and order has been assigned 11 per cent expenditure in the US, it amounted to less than 1 per cent in Denmark; likewise, spending on education is largest in the US (43 per cent) as compared to a very modest spending in Australia (0.4 per cent). Spending on fuel and energy (0-3.4 per cent) and on agriculture, forestry and fishing (0-1.3 per cent) is expectedly low in all these countries. Transportation may not be regarded as an essential

function, yet the spending on it is sizable and varies between 2.7 and 27.5 per cent respectively. Likewise, spending on economic affairs and services is also modest (0.7 to 10.9 per cent) but relatively sizeable. Expenses on these two non-essential services are high because all of the sample countries are economically well-developed and require these services for their growth.

The share of local government expenditure in the consolidated government expenditure is also widely varying. In Australia, where the local government system is relatively small in size and functions, it is only of the order of 6 per cent, whereas in Denmark, where the local governments are provided with numerous responsibilities, the local government expenditure is very large at about 60 per cent of the consolidated government expenditure. The US and Canada have somewhat similar systems and structures of local governments and therefore they also share similar levels of local government expenditure (18 and 26 per cent of consolidated government expenditure), which is also matched by that of Germany (18.1 per cent). However, Germany has a large amount of spending on welfare items as compared to the heavy spending on education by the US and Canada.

The share of local government expenses in the country's GDP gives more or less same picture i.e., Denmark has a large proportion due to larger size of municipal government and their function (32 per cent), and the US and Canada have modest proportion of expenses in the GDP (8 per cent) which is almost matched by that of Germany (9 per cent), and, lastly, Australia has the least proportion (2 per cent) due to relatively smaller role played by the local government system there in service delivery.

Table 6: Local Government Expenditures in Select Countries, 1998
(per cent distribution)

	Australia	Canada	Denmark	Germany	USA
<i>General Public Services</i>	13.7	5.5	3.9	7.4	5.7
<i>Public Order & Safety</i>	2.4	9.1	0.3	3.4	10.9
<i>Education</i>	0.4	42.0	12.4	13.0	43.3
<i>Health</i>	2.1	1.4	16.2	14.5	8.9
<i>Social security & welfare</i>	6.3	7.0	57.5	24.6	7.8
<i>Housing & community amenities</i>	18.7	5.5	1.0	15.3	2.0
<i>Recreation, culture & religious</i>	17.7	6.4	2.9	5.7	3.4
<i>Fuel & Energy</i>	0.2	3.4	0.0	0.1	0.0
<i>Agriculture, forestry & fishing</i>	1.3	0.3	0.0	0.6	0.6
<i>Transportation & communication</i>	27.5	11.3	2.7	6.0	6.0
<i>Other Economic Affairs & Services</i>	3.9	3.1	2.2	4.1	0.5
<i>Other</i>	5.8	5.1	0.7	5.3	10.9
<i>Total</i>	100.0	100.0	100.0	100.0	100.0
<i>Total as % consolidated government expenditure</i>	6.1	18.1	59.2	18	26.2
<i>Total as % of GDP</i>	2.2	8.1	32.6	9.2	8.8

Source: McLean (2002), Boadway and Watts (2004)

4. Patterns of Urban Public Finances in India

Indian Constitution made India as a union of States and the Municipalities are constituted under State legislation. Owing to the elaborate Constitutional provisions, the Parliament and the State Legislatures flourished as democratic institutions over the years. However, this has not been the case with the urban local bodies, in spite of the fact that some of the urban local government institutions came into existence long before the formation of States. In fact, in the process of centralisation, these cities lost their independence and autonomy in functioning.

After independence, over the years, there was a steady encroachment on the traditional functions of the municipal authorities by the para-statal and specialised agencies of the State and Central Governments, which has weakened the base and capacity of the ULBs and hampered decentralisation (Mohanty 1995). Thus, the Municipalities or Municipal governments became weak and are unable to meet the needs and aspirations of the people. In this background, the enactment of the Constitution (74th Amendment) Act, 1992 signifies a landmark initiative of the Government of India, which is aimed at re-establishing and strengthening the local self-government.

4.1 Municipal Functions in India

Regarding the functional domain of the urban local bodies, the 74th Amendment Act envisages that the State Governments may, by law, endow them with such powers and authority as may be necessary to enable them to function as institutions of self-government with respect to (i) preparation of plans for economic development and social justice; (ii) performance of functions and implementation of schemes as may be entrusted to them. Thus the role envisaged of the urban local bodies is much broader than that as providers of public services. However, the Constitution does not distinguish between the functional domain of the three categories of municipal bodies: Municipal Corporations, Municipal Councils and Nagar Panchayats. Table 7 shows the municipal functions of select states.

Table 7: Local Government Functions in Select States in India

<i>Function</i>	Goa	Haryana	Karnataka	Kerala	Madhya Pradesh	Uttar Pradesh	West Bengal
<i>Civic Amenities</i>	Water supply, Sewerage, Drainage, and Street lights	Water supply, Sewerage, Street sweeping and Street lights	Water supply, Sewerage, Drainage, Street sweeping and Street lights	Water supply, Sewerage, Drainage, Street sweeping and Street lights	Water supply, Sewerage, Drainage, Street sweeping and Street lights	Water supply, Sewerage, Drainage, Street sweeping and Street lights	Water supply, Sewerage, Drainage, Street sweeping and Street lights
<i>Social Welfare</i>	Provision for lunatics, leprosy patients	Creches for children of weaker section women	Shelter for destitute women, orphans	Organizing civil society against social evils	Provision for lunatics, destitutes, blind, disabled & old	Removing social disabilities of weaker sections	Old age homes, shelter for deprived classes or sections
<i>Slum improvement and Sanitation</i>	Sanitary dwellings for poor		Sanitary dwellings for poor		Sanitary dwellings for poor		Sanitary dwelling improvements for poor
<i>Education</i>	Schools, libraries and museums		Schools, libraries, art galleries, public places and museums	Schools, libraries and museums	Schools, libraries and museums	Schools, libraries, culture institutions and museums	Schools, libraries, physical education, sports and museums
<i>Urban Planning</i>				Yes		Yes	Yes
<i>Economic and social development planning</i>			Yes	Yes		Yes	
<i>Urban environment – amenities</i>		Yes	Yes	Yes	Yes	Yes	Yes

Source: Based on Mathur and Thakur (2004)

The Twelfth Schedule to Part IX of the Constitution of India (Article 243W) added through 74th Amendment Act provides an illustrative list of municipal functions which includes:

- ⇒ Urban planning including town planning;
- ⇒ Regulation of land use and construction of buildings;
- ⇒ Planning for economic and social development;
- ⇒ Roads and bridges;
- ⇒ Water supply for domestic, industrial and commercial purposes;
- ⇒ Public health, sanitation, conservancy and solid waste management;
- ⇒ Fire services;
- ⇒ -Urban forestry, protection of environment and promotion of ecological aspects;
- ⇒ Safeguarding the interests of weaker sections of society, including the handicapped and the mentally retarded;
- ⇒ Slum improvement and upgradation;
- ⇒ Urban poverty alleviation;
- ⇒ Provision of urban amenities and facilities e.g. parks, gardens, and playgrounds;
- ⇒ Promotion of cultural, educational and aesthetic aspects;
- ⇒ Burials and burial grounds, cremation ghats/grounds, and electric crematoria;
- ⇒ Cattle pounds, prevention of cruelty to animals;
- ⇒ Vital statistics including registration of births and deaths;
- ⇒ Public amenities including street lighting, parking lots, bus stops and public conveniences;
- ⇒ Regulation of slaughter houses and tanneries.

4.2 Municipal Finances in India

The size of the municipal public sector in India is quite small compared to many countries. This is partly due to the low level of India's urbanisation and partly due to the neglect of municipal finances. NIPFP (1995) estimates the total revenues raised by the Municipalities in the country in 1993-94 at Rs.3,900 crore, i.e. 4.6% of the revenues raised by the Central Government and 8.5% of those by the State Governments taken together. This amount is as low as 0.6% of the country's GDP at factor cost. The NIPFP study concludes: "Considering the fact that the Municipalities produced over 50% of the country's GDP, it is obvious that the Municipalities have not benefitted from the multitude of activities that take place within their jurisdictions, and are thus peripheral to the Indian economy."

4.2.1 Municipal Revenues

Municipal revenues include taxes, shared revenues, charges and fees, loans and grants from government and non-government sources. Table 8 shows the relative importance of each in select Indian states.

Table 8
Share of Municipal Revenue Sources: 1991-92

State	"Own" Revenues % in Total Revenues	Shared Revenues % in Total Revenues	Grants-in-Aid % in Total Revenues	Property Tax as % of Own Revenues	Non-Tax as % of Own Revenues
Andhra Pradesh	55.10	30.2	11.2	69.7	21.3
Assam	70.92	6.9	7.8	37.8	42.2
Gujarat	88.96	--	11.0	15.6	18.9
Kerala	76.79	11.1	3.4	41.6	26.3
Maharashtra	90.81	0.5	4.9	15.9	29.5
Punjab	87.85	--	10.2	9.9	14.1
West Bengal	27.89	27.3	30.8	66.5	30.7

Source: NIPFP (1995)

It is evident that the existing base of municipal taxes in India is narrow and limited to 'property tax' in the non-Octroi States and 'Octroi' in Octroi-levying States. Vacant land tax, a variant of the property tax, is levied by some States and the potential of it is not exploited. Octroi is regarded by many as an obnoxious tax, yet it is the most important source of municipal revenues in Maharashtra, Gujarat, Punjab, Rajasthan and Orissa. Other important municipal taxes comprise Profession tax, Entertainment tax, Advertisement tax, Surcharge on Stamp Duty and Motor Vehicles tax. These taxes too are not properly exploited. Table 9 shows major sources of 'own' taxes levied by select Municipal Corporations in the country.

Table 9
Major Sources of 'Own' Municipal Taxes in India

Name of State	Name of Municipal Corporation	Own Municipal Taxes
Maharashtra	Greater Mumbai	Octroi, Property Tax, Wheel Tax
West Bengal	Kolkata	Property Tax, Profession Tax, Advertisement Tax
Karnataka	Bangalore	Property Tax, Advertisement Tax
Orissa	Bhubaneswar	Octroi, Property Tax
Gujarat	Surat	Octroi, Property Tax, Vehicle Tax, Theatre Tax
Tamil Nadu	Chennai	Property Tax, Profession Tax, Advertisement Tax

Andhra Pradesh	Hyderabad	Property Tax
Uttar Pradesh	Kanpur	Property Tax, Advertisement Tax, Terminal Tax

Source: Municipal Budgets

Some Indian States share Motor Vehicles tax, Profession tax, Entertainment tax and Stamp duty/Registration Charges with Municipalities. Table 10 shows the major sources of shared revenues in select Municipal Corporations in the country.

Table 10
Major Sources of 'Shared' Municipal Taxes in India

Name of State	Name of Municipal Corporation	Shared Municipal Taxes
Maharashtra	Greater Mumbai	Non-agricultural Assessment Tax, Entertainment Tax
West Bengal	Kolkata	Motor Vehicles Tax, Entertainment Tax
Karnataka	Bangalore	Entertainment Tax, Surcharge on Stamp Duty
Orissa	Bhubaneswar	-
Gujarat	Surat	Entertainment Tax
Tamil Nadu	Chennai	Surcharge on Sales Tax, Duty on Transfer of Property, Entertainment Tax
Andhra Pradesh	Hyderabad	Transfer of Immovable Property Tax, Profession Tax, Entertainment Tax
Uttar Pradesh	Kanpur	-

Source: Municipal Budgets

User charges are grossly under-utilised source of municipal revenues in India in spite of their inherent attractiveness as instruments of charging for the public services. Major sources of user charges and fees levied by select Municipal Corporations in the country are shown in Table 11.

Table 11
Major Sources of User Charges and Fees in India

Name of State	Name of Municipal Corporation	User Charges and Fees
Maharashtra	Greater Mumbai	Water Charges, Sewerage Charges, Building Licence Fees

West Bengal	Kolkata	Planning Fees, Car Parking Fees, Mutation Fees
Karnataka	Bangalore	Betterment Charges, Building Licence Fees, Penalty for Late Tax payment
Orissa	Bhubaneswar	Building Licence Fees, Market Fees,
Gujarat	Surat	Water Charges, Building-related Fees, Betterment Charges
Tamil Nadu	Chennai	Building Licence Fees, Market Fees, other Licence Fees, Parking Fees
Andhra Pradesh	Hyderabad	Dangerous and Offensive Trade Licence Fees, Market Fees, Slaughter House Fees
Uttar Pradesh	Kanpur	Building Licence Fees, Market Fees

Source: Municipal Budgets

State Governments provide grants and loans to the authorities where services have benefit spillovers and distributional consequences. Central and State Governments in many countries place primary education, preventive health care, social assistance and environmental protection under the 'agency' functions for which grants are provided. State Governments mostly provide grants to their local bodies for specific functions. They also provide equalising grants to tackle the problems of fiscal imbalances between rich and poor Municipalities. In general, the transfer/grant-in-aid systems operating in various States in India are not based on the principles of public finance. Often these are negotiated, distorting the local priorities and constraining the local incentives to raise resources. Table 11 shows the major categories of transfers to selected Municipal Corporations in India by the concerned State Governments.

Table 11
Major Sources of Grants-in-aid to Municipal Corporations in India

Name of State	Name of Municipal Corporation	Grants-in-aid provided to Municipal Corporations
Maharashtra	Greater Mumbai	Primary Education Grant, Secondary Education Grant
West Bengal	Kolkata	Dearness Allowance Grant, Grant to implement Recommendations of Pay Commission, Water Supply, Sewerage & Drainage Grants
Karnataka	Bangalore	Octroi Compensation, Motor-Vehicle Tax Compensation, Family Planning Schemes Grants
Orissa	Bhubaneswar	Salary & Dearness Allowance Grants, Road Development Grant, Primary Education Grant, Secondary Education

		Grant
Gujarat	Surat	Education Grant, Family Planning Grant, Small Savings Grant
Tamil Nadu	Chennai	Revenue Grant, Contributions, Compensation for Toll
Andhra Pradesh	Hyderabad	Dearness Allowance Grant, Property Tax Compensation, Octroi Compensation, Per Capita Grant, Motor Vehicle Tax Compensation, Road Grant
Uttar Pradesh	Kanpur	Octroi Compensation, Salary Grant, Education Grant (Primary & Secondary Education), Medical Grant, Road Grant

Source: Municipal Budgets

5. Summary

In spite of the heterogeneity of the local government finance systems in countries across the world, few lessons can be learnt in the context of evolving local government finances in developing countries like India. Most of the countries have stable levels of spending on public services, amenities and recreation & culture and spending on energy and agriculture had been almost negligent. It is the areas like housing, transport and education where they show an array of deviations as a result of the system priorities. Municipal revenue and expenditures are very small in India (about 0.5%) when compared to that of Western countries.

Tax revenue has been the stable income base of the systems and so do the well designed systems of transfers, both which contribute to almost 80% of the local government revenues. Property and income taxes are the stable tax sources. Property taxes seldom accounted for more than 20% of local current revenues in developed countries. However, in many developing countries including India, the dependence of municipal authorities on property taxes is inordinately heavy, reflecting their narrow revenue base. Interestingly, without buoyant taxes like Octroi, the resources available to some of the ULBs are smaller in amount.

Non-tax revenue income is also important to economically robust countries like the US, Germany and Australia. There is a visible trend in the OECD countries towards more effective utilisation of user charges and benefit taxes by local governments. This is attributed partly to citizens' preference for user charges over general taxes. In contrast, user charges in India remain a grossly under-exploited source till today, which would require reforming the local governments in making them realise the need for reforms. Reforms aiming at better recovery of costs of services provided are still looming around the municipal governments.

Inter-government transfers are yet to become reliable and regular revenue sources for municipal governments. This also underlines the need for designing and implementing fiscal devolution in effective manner. Further, the transfer system needs to be streamlined and rationalised, particularly at the level of transfer between State and local governments. Inter-governmental transfers may also be pegged to a better fiscal performance of urban local governments, such as making them recover the costs of services (commercially oriented) to the extent possible, so they will find an incentive in reforming their systems.

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