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**NITI Aayog: Reimagining  
Fiscal Federalism**

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## NITI AAYOG: REIMAGINING FISCAL FEDERALISM

### Context

- Recent Governing Council meeting of the NITI Aayog that was skipped by the representatives of several States and Union Territories highlighted both structural and functional issues.

### About

- India's Constitution-makers envisioned the country as a union of States, emphasising unity and integrity. However, over the years, India has transformed significantly—economically, politically, demographically, and socially.
- As the new aspirational India accelerates along its growth trajectory, it's essential to revisit the concept of fiscal federalism.

### National Institution for Transforming India (NITI) Aayog

- National Institution for Transforming India (NITI) Aayog was established by the government **to replace the Planning Commission** in 2015 with the aim **to move away from the top-down approach of the Planning Commission** and focus on **'Co-operative Federalism'**.
- Advisory Role:** The NITI Aayog's primary function is advisory, lacking the authority to distribute resources or allocate funds to states.
  - Unlike the Planning Commission, which allowed consultations with states, the NITI Aayog's focus shifted toward creating indices to evaluate states.
- Conditional Transfers:** In the past, the Planning Commission provided grants to States using the **Gadgil-Mukherjee formula**. With the Planning Commission disbanded, NITI Aayog could step in to facilitate 'transformational' interventions. However, it currently lacks the financial resources for this purpose.
- Resource Allocation:** NITI Aayog 2.0 should receive significant resources (perhaps 1% to 2% of GDP) to promote accelerated growth in lagging States. By strategically allocating funds, it can address both **Type I and Type II imbalances**.
- Competitive Federalism:** The unintended consequence of this advisory approach has been 'Competitive Federalism'.
  - Meanwhile, the Finance Ministry retains the power to decide on grants to states. This situation has led to discontent among states, especially those ruled by opposition parties.
- Present Government's 'Double Engine' Approach:** It has campaigned in state elections based on providing **'double engine' governments (both at the state and central levels)**. This has raised concerns that **investment projects may favour** similar party-ruled states.
- Dependence on Regional Parties:** Present government now relies on support from parties governing states like Bihar and Andhra Pradesh, which face varying developmental deficits. The Finance Minister's intention to address their demands in the budget has not gone unnoticed.
- However, over time, the NITI Aayog has faced criticism due to its limited role as an advisory body without direct powers of resource allocation to states.

### Concerns and Issues Ahead of NITI Aayog

- Vertical Imbalance:** This arises because tax systems often yield more revenue to the Union government than to State or Provincial Governments. Yet, the Constitution assigns relatively greater responsibilities to the States.
  - For instance, post the introduction of the Goods and Services Tax (GST), States shoulder 60% of public expenditure, while the Centre handles 40% to fulfill their constitutionally mandated duties.
- Horizontal Imbalance:** This stems from differing levels of development among States due to varying growth rates and disparities in social and infrastructure capital.
  - Traditionally, Finance Commissions have addressed these imbalances effectively, making them the first pillar of India's fiscal federal structure.
  - However, India's horizontal imbalance requires a more nuanced approach. It involves two types:

- ◆ **Type I Imbalance:** This pertains to the provision of basic public goods and services.
- ◆ **Type II Imbalance:** This results from infrastructure deficits that hinder growth. These deficits are often historically conditioned or path-dependent.

### Structural Issues of NITI Aayog

- **Replacement of the Planning Commission:** Unlike the centralised planning approach of the Planning Commission, NITI Aayog was envisioned as a more flexible and dynamic institution.
  - ◆ However, the transition from a centralised planning model to a think tank with a focus on cooperative federalism posed initial challenges. Some critics argue that NITI Aayog lacks the same level of authority and financial resources as its predecessor.
- **Composition and Representation:** The composition of NITI Aayog's Governing Council includes all State Chief Ministers, Lieutenant Governors of Union Territories, and several Union Ministers.
  - ◆ While this ensures representation, it can also lead to divergent interests and varying priorities.
  - ◆ Critics point out that the presence of Union Ministers in the council might dilute the States' voice, as the Centre's interests could overshadow those of the States.
- **Resource Constraints:** Unlike the Planning Commission, which had a dedicated allocation for grants to States, NITI Aayog lacks direct financial resources. It relies on the central budget for its functioning.
  - ◆ This resource constraint affects NITI Aayog's ability to drive transformative interventions at the State level effectively.

### Functional Issues of NITI Aayog

- **Policy Implementation and Execution:** While NITI Aayog formulates policies and provides recommendations, its impact on policy execution remains limited. Implementation lies primarily with individual States and ministries.
  - ◆ Critics argue that NITI Aayog should play a more active role in monitoring and evaluating policy outcomes.
- **Lack of Statutory Powers:** Unlike the Planning Commission, NITI Aayog doesn't have statutory powers. It operates as an advisory body, which limits its ability to enforce policy decisions.
  - ◆ Some experts advocate for granting NITI Aayog more legal authority to ensure effective coordination between the Centre and States.
- **Cooperative Federalism vs. Competitive Federalism:** NITI Aayog promotes cooperative federalism, emphasising collaboration and dialogue between the Centre and States. However, there's a fine balance between cooperation and healthy competition.
  - ◆ Critics argue that NITI Aayog should also encourage competitive federalism, where States compete to improve governance, attract investments, and enhance development outcomes.

### Recent Recommendations and Best Practices

- **Common Vision:** Prime Minister stressed the need for a common vision between the Centre and states to achieve a developed India by 2047.
  - ◆ He urged states to take financially prudent decisions and use platforms like the Gati Shakti Portal for infrastructure and logistics.
- **State-Level Best Practices:** States highlighted various best practices, including green strategies, zone-wise planning, tourism, urban planning, and quality workmanship
- **Easing MSME Exports:** NITI Aayog recommends simplifying e-commerce routes for Micro, Small, and Medium Enterprises (MSMEs) to boost exports, including creating a single national trade portal for approvals and compliances.
- **Integration into Global Value Chains:** NITI Aayog emphasises integrating India into global value chains and adapting to emerging trading systems.

### Conclusion and Way Forward

- As India celebrates its 75th year, reimagining fiscal federalism becomes critical. NITI Aayog, with adequate resources and a clear mandate, can be the catalyst for a more balanced and competitive federal structure—one that aligns with the evolving needs of our diverse nation.

- NITI Aayog has made significant contributions, addressing these issues will be crucial for its continued effectiveness in shaping India's development path, and it needs to evolve to strike a better balance between advisory functions and active engagement with states, fostering genuine cooperative federalism.
- NITI Aayog needs **to regain some of the responsibilities that the Planning Commission** had for states, including meaningful consultations on grants and projects to promote true cooperative federalism.

Source: TH



### Mains Practice Question

[Q] Compare and contrast the principles followed by the NITI Aayog with the erstwhile Planning Commission in India. Highlights the structural and functional challenges ahead of NITI Aayog.

