



# **DAILY EDITORIAL ANALYSIS**

**TOPIC**

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**STRENGTHENING LOCAL BODIES:  
16TH FC'S PUSH FOR FISCAL  
DEVOLUTION**

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## STRENGTHENING LOCAL BODIES: 16TH FC'S PUSH FOR FISCAL DEVOLUTION

### Context

- The **16th Finance Commission (FC)** marks a significant shift in India's fiscal architecture by substantially increasing financial devolution to **Urban Local Governments (ULGs)**.

### About Urban Local Governance in India

- Urban Local Governance refers to the system through which cities and towns are administered by elected local bodies.
- It is the **third tier of government**, below the Union and State governments, and is responsible for delivering essential public services at the city level.

### Why Urban Local Governance Matters?

- Cities contribute **over 60% of India's GDP** and are expected to drive future economic growth. Effective urban governance ensures better service delivery, sustainable development, improved quality of life, and economic competitiveness.
- Poor governance, on the other hand, leads to infrastructure deficits and social inequality.
  - ♦ Municipal revenues in India are about **0.6% of GDP**, which is very low compared to many developing countries.

### Constitutional Basis of Urban Local Governance

- Urban governance in India gained constitutional status through the **74th Constitutional Amendment Act, 1992**.
- It recognised municipalities as institutions of self-government;
  - ♦ Added the **12th Schedule to the Constitution (listing 18 functions of municipalities)**.
  - ♦ Made provisions for **regular elections every five years**.
  - ♦ Mandated the creation of **State Finance Commissions (SFCs)** to review **municipal finances**.
  - ♦ Introduced **reservations for women and marginalized groups** in municipal bodies.
- The objective was to promote **democratic decentralisation**, meaning decision-making power should move closer to citizens.

### Types of Urban Local Bodies (ULBs)

- **Municipal Corporation:** Established in large cities (e.g., Mumbai, Delhi, Bengaluru).
  - ♦ **Functions:** Urban planning, Water supply, Sanitation and waste management, Roads and street lighting, and Public health.
- **Municipal Council:** For smaller cities and towns.
- **Nagar Panchayat:** For transitional areas moving from rural to urban. These bodies are composed of **elected representatives (Councillors)**, a **Mayor or Chairperson**, an administrative head (often a Municipal Commissioner, usually appointed by the state government).

### Key Functions of Urban Local Governments

- According to the **12th Schedule**, major responsibilities include urban planning and regulation of land use, roads and bridges, water supply, public health and sanitation, solid waste management, fire services, urban poverty alleviation, and slum improvement.

### Financial Structure of Urban Local Governance

- **Own-Source Revenue:** Property tax; User charges (water, parking, etc.); Advertisement tax; and Fees and licenses.
  - ♦ It is often weak in India due to poor tax collection systems, political resistance to raising taxes, and inadequate valuation systems.

- **State Government Transfers:** ULBs depend heavily on state grants.
- **Finance Commission Grants:** The **Finance Commission (FC)** recommends grants to local bodies **every five years**.

### Historic Increase in Urban Grants

- The 16th FC has raised overall grants to ULGs by **230%**, from approximately ₹1.55 trillion under the 15th FC to **₹3.56 trillion for the 2026–31 period**.
- **Key Highlights:**
  - ♦ **ULG share in local-body grants increased to 45%**, up from 36%. It is the **highest urban share in Finance Commission history**.
  - ♦ It reflects recognition of rapid urbanisation, cities' growing contribution to GDP, and expanding infrastructure and service delivery needs.
- It signals a policy acknowledgement that cities are not merely administrative units but economic growth engines.

### Differentiated and Strategic Grant Structure

- The 16th FC has introduced a more structured and diversified urban grant framework, consisting of:
  - ♦ **Basic Grants:** ₹2.32 trillion
  - ♦ **Performance Grants:** ₹54,032 crore
  - ♦ **Special Infrastructure Grants:** ₹56,100 crore
  - ♦ **Urbanisation Premium:** ₹10,000 crore
- It balances unconditional support with performance-linked incentives and infrastructure-specific assistance.

#### Do You Know?

- **Basic Grants:** Provide foundational support for routine municipal functions.
- **Performance Grants:** Reward good governance practices and administrative efficiency.
- **Special Infrastructure Grants:** Address city-specific infrastructure gaps.
- **Urbanisation Premium:** Recognises pressures from rapid urban growth.

### Greater Flexibility Through Untied Funds

- **Untied funds** allow ULGs to allocate resources according to **local priorities** rather than being confined to centrally prescribed schemes.
  - ♦ The remaining tied grants focus on essential urban services such as sanitation, solid-waste management, water supply, and wastewater management.
  - ♦ It enhances fiscal autonomy while ensuring continued attention to critical urban sectors.
- Approximately **52%** of the total urban grants are now untied, compared to just **21% under the 15th FC**.

### Complementarity with Union Budget Initiatives

- The Union Budget's allocation of **₹5,000 crore per City Economic Region over five years in Tier-II and Tier-III cities** could reinforce this fiscal shift. However, its effectiveness depends on:
  - ♦ Routing funds through **empowered municipal institutions**;
  - ♦ Avoiding the creation of new centralised, scheme-driven mechanisms;
- Additional funding risks diluting local autonomy rather than strengthening it, without institutional empowerment.

### Key Concerns & Issues

- **Urban Investment Gap:** According to a World Bank estimate, **1.18% of GDP annually** required urban capital investment (2021–36); **but** current municipal revenues are barely about **0.6% of GDP**.
  - ♦ In comparison, South Africa's ULGs mobilise about **6% of GDP**; and Brazil's ULGs mobilise about **7.4% of GDP**;
  - ♦ It highlights India's weak municipal revenue base and limited fiscal capacity.

- **Governance Deficits:**

- ♦ **Delayed Municipal Elections:** The Brihanmumbai Municipal Corporation polls were delayed by nearly four years. Bengaluru has not held civic elections since 2015.
  - Comptroller and Auditor General reports show an average **22-month delay** in municipal polling.
  - Delayed elections undermine accountability, legitimacy, and citizen responsiveness.
- ♦ **Weak Financial Autonomy:** Limited own-source revenues; Heavy dependence on state transfers; Political and administrative control by state governments.
- ♦ **Limited Administrative Capacity:** Even larger grants may fail to translate into improved infrastructure or service delivery without institutional strengthening.

### Way Forward: Strengthening Institutional Foundations

- The 16th FC retains reform-linked eligibility conditions, including timely ULG elections, publication of audited accounts, constitution of State Finance Commissions (SFCs), and tabling of 'action taken reports'.
  - ♦ Democratic decentralisation remains incomplete while these are meaningful safeguards.
- **To maximise the 16th FC's impact, India needs to** ensure timely and regular municipal elections, strengthen municipal revenue mobilisation, enhance administrative and technical capacity, and deepen fiscal autonomy at the city level.

### Conclusion

- The 16th Finance Commission represents a historic fiscal correction in favour of urban India. The increased allocation, higher urban share, and expanded untied funds mark a decisive move toward empowering cities.
- However, financial devolution without governance reform risks underperformance. Strengthening institutional foundations ie democratic accountability, fiscal autonomy, and administrative capacity is essential to ensure that enhanced grants translate into better infrastructure, improved services, and sustainable urban growth.

Source: BS

### Daily Mains Practice Question

**[Q]** Financial transfers alone cannot ensure effective urban governance. Discuss in the context of democratic decentralisation, fiscal autonomy, and institutional capacity.

