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Devolution of Central Taxes to the States: Contribution by different states to Tax Kitty

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THE devolution of Central Taxes to the States has always been a hotly debated topic. However, in the last few years, this debate has been raised to a different level by the Southern States; Karnataka, Tamil Nadu, Kerala and Andhra. In a conclave organized in Bangalore, sometime back, Southern States claimed that they are not getting their fair share of Central taxes. They also contend that the terms of reference (TOR) of 15th Finance Commission were adverse to their interest and that consideration of 2011 Census data for devolution of central taxes as against 1971 data earlier, will reduce their share of central taxes further and in turn will reward poorly managed Northern States which have much higher population. Their claim is based on the fact that they have done a good job in controlling their population and fertility rates (at about 1.5%), while the fertility rate of the Northern States remains too high at about 2.5% because of bad governance, and therefore population-based criteria, more so the latest census data will affect their share adversely.

It is pertinent to mention that the scheme of devolution of central taxes to states is provided under **article 280 of the constitution** as per which a '**Finance Commission**' is constituted every five years by the President of India, to decide the devolution of share of central taxes to the states. 15th Finance Commission was constituted under the chairmanship of N K Singh, which recommended that 41% of Central taxes be shared with the states. Earlier, the 14th Finance commission had submitted its report in 2014 and increased the State's share from 32% to a whopping 42%. Still, some States are not happy because of huge requirement of social spending for which they need more and more resources.

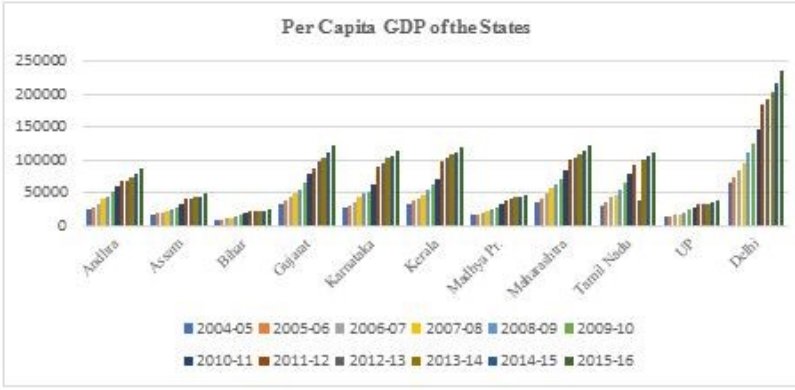
As per the latest data, five southern states; Tamil Nadu, Karnataka, Kerala, Andhra Pradesh & Telangana contribute about one third of national GDP and 30% of Central Taxes, while they receive only about 18% share of Central Taxes from the Centre and therefore on face of it, their contention appears to be justified. It is also relevant to mention, that per capita GDP of the southern states at about Rs.1,20,000/-, is much higher, as compared to the northern states or more specifically the BIMARU states of Bihar, UP, Rajasthan and MP where it is below Rs.50,000/- (2015-16 figures) showing much lesser economic activity happening there, as is clear from the Table-1 below:-

Table 1.: Per capita GDP of States

Per Capita Income at Constant (2011-12) Prices													
	State	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16
1	Andhra	25959	28223	32961	39780	44376	50515	58733	69000	68865	72254	78039	86118
2	Assam	16782	18396	19737	21290	24099	28383	33087	41142	41609	43002	44809	48465
3	Bihar	7914	8223	9967	11051	13728	15457	19111	21750	22201	22776	23223	24572
4	Gujarat	32021	37780	43395	50016	55068	64097	77485	87481	96683	102589	111370	122148
5	Karnataka	26882	31239	35981	42419	48084	51364	62251	90263	94417	101918	106245	113303
6	Kerala	32351	36958	41318	46865	54560	62114	69943	97912	103551	107846	112444	119777
7	Madhya Pr.	15442	16631	19028	20935	25278	28651	32453	38551	41287	42778	44357	46324
8	Maharashtra	36077	41965	49831	57760	62234	69765	84858	99173	103426	109364	113629	121514
9	Tamil Nadu	30062	35243	42288	47606	54137	64338	78473	92984	36937	101591	106186	111454
10	UP	12950	14221	16013	17785	20422	23671	26698	32002	32908	34044	34583	36850
11	Delhi	63877	72208	83275	95241	111756	125936	145129	185361	193175	202216	216029	234328

Source : Public Finance Statistics 2017

Figure 1.: Per Capita GDP of states in India



Source :constructed by author from Table 3.12

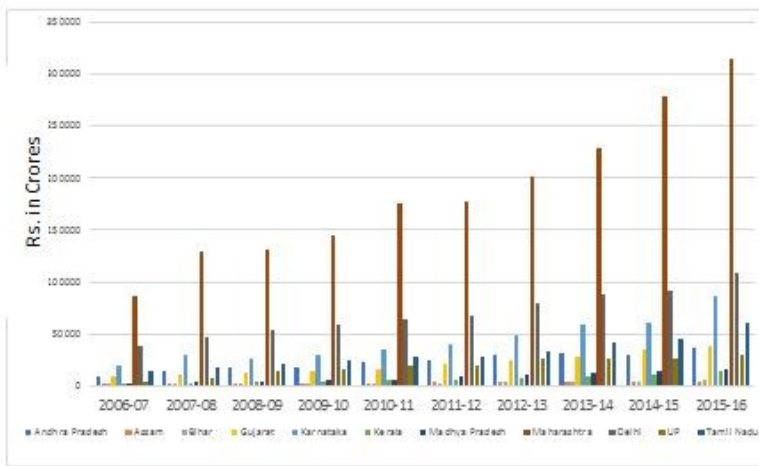
It has also been noticed that fertility rates of southern states is about 1.5, while that of northern states is over 2.5 and thus much more population is being added in the northern states as compared to the southern states. Therefore, if the Census data of 2011 is taken as a basis for division of central taxes, then share of Southern States in the Central Tax kitty is going to go down further. It can be stated that four southern states combined contribute about 1/3rd of National GDP, while their population is only about 20%. Further, they have done much more work on Human Development Index (HDI) and had done much higher spending on education and health in the past, which resulted into tremendous increase in human development index as also the per capita GDP. It can also be seen that southern states are much more industrialized and their literacy rate is much higher at about 85-95% as compared to about 75% in the northern states, a stark gap of over 10%. These factors make a huge difference in the economic activity happening there. In this context, it is necessary to examine as to how much taxes are contributed by each State to the Central Tax kitty and how much is the growth, year on year basis, which are shown in Table 2. From the analysis of these details, it may be concluded that Maharashtra contributes maximum amount to the national tax kitty which is to the tune of 37% of revenue collection of the Centre. Delhi comes next and contributes about 12% while Karnataka contributes about 9% and Tamil Nadu about 7%. It can also be noted that among Northern states, UP contributes significantly towards Central Taxes at about 4%. Of course Bihar and Madhya Pradesh contribute much lesser and Assam is even smaller.

TABLE 2.: STATE AND U.T. WISE BREAK-UP OF TAX COLLECTION (Rs.in crore)

States	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16
Andhra Pradesh	7843	8936	10173	13835	17494	18716	23133	2518	29947.7	32296.1	29769.01	36241.34
Bihar	346	421	553.87	791.42	1719.32	1997.82	2581.09	3058.4	3806.7	4491.6	4425.75	6519.42
Karnataka	11862	14527	19014.83	30806.94	27311.15	29220.86	35824.8	40956	49047.8	59769.8	60595.22	85920.98
Maharashtra	58946	71425	86709.33	129353.9	131168.5	145507.62	174968.59	177363.3	202128.9	229494.9	277720.11	314056.27
Tamil Nadu	11321	12924	14747.54	18010.29	20651.09	24265.07	28409.46	28327.5	33051.3	42681.3	44732.62	60077.95
UP	3239	3624	4262.2	7044.62	14453	15905	19850.5	20130.3	25745.6	25886.5	24981.22	27159.83
Delhi	25847	32426	38399.62	46961.39	54705.03	59621.71	64208.09	68410.5	79137.1	88140.4	91247.9	108882.5

Source : Director Budget (CBDT),2016

Figure 2: State-wise Income-tax Collections



Source: constructed from Table 3.14

The Table 3 reflects the devolution of Central Taxes to the States in the three financial years .

Table 3: Devolution of Central Taxes to States:

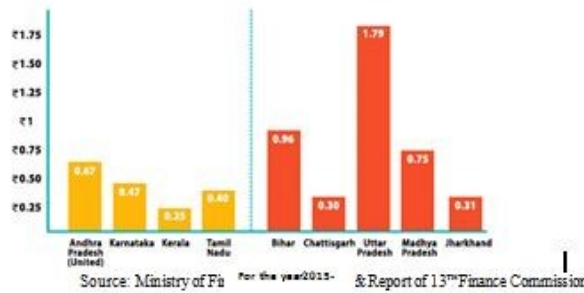
State-wise distribution of net proceeds of Union taxes and duties (Rs. In Crores)

State	2013-14 (Actuals)	2014-15 (RE)	2015-16 (BE)
Andhra Pradesh	21,842.95	13,692.42	22,637.97
Assam	11,423.45	12,283.71	17,400.88
Bihar	34,374.49	36,963.07	50,747.58
Jharkhand	8,822.63	9,487.01	16,498.80
Karnataka	13,628.02	14,654.25	24,789.78
Kerala	7,371.20	7,926.29	13,121.77
Madhya Pradesh	22,418.73	24,106.99	39,705.39
Maharashtra	16,370.20	17,602.97	29,061.94
Tamil Nadu	15,645.81	16,824.03	21,149.89
Telangana	-*	9,795.40	12,823.25
Uttar Pradesh	61,957.20	66,622.91	94,313.46
Total	3,14,112.66	3,37,808.45	5,23,958.24

* The State of Telangana was not created at that time; BE stands for Budget estimate, RE for Revised estimate, Source: Ministry of Finance data

From the Table 2 and Table-3, it can be concluded that Tamil Nadu gets just 40 paise for each rupee contributed by it as tax to Central kitty (FY 2015-16), while Karnataka gets 47 paise and Kerala only 25 paise. On the other hand, UP gets Rs. 1.80, for each rupee contributed by it towards central taxes, Bihar gets 96 paise, MP gets 75 paise and Jharkhand gets only 31 paise. Therefore, it is not correct to say that all northern states are getting more than what they are contributing to the national tax kitty.

Figure 3.: Ratio of Central Taxes received and Central Taxes Paid



Source: Ministry of Finance Statistics, 2015 & Report of 13th Finance Commission.

If we compare, growth in taxes year-on-year basis, we find that there is wide variation among different states in the same year, as also, in the same state over a period of time. Further there appears to be no definite trends in growth of taxes from year on year basis. The growth rate in respect of Tamil Nadu varies from 0 to 34.30%, for the period 2007-08 to 2015-16 while in respect of Karnataka it varies from -11% to 62%. In respect of Bihar it varies from -1.47% to 117.24% and in respect of Maharashtra the growth varies from 1.37% to 49.18%. If we examine the data further, we find that growth for the year 2007-08 is the highest in most of the states and is mostly over 20% and thereafter such growth has not been reported in any of the years. This is also the year in which buoyancy in tax collections was the highest and was of the order of 2%. The relevant data is available in the Finance Ministry and CBDT website and is tabulated as Table 5.

Table4: Growth in tax collection of States

States	05-06	06-07	07-08	08-09	09-10	10-11	11-12	12-13	13-14	14-15	15-16
1 Karnataka	22.47	30.89	62.02	-11.35	6.99	22.60	14.32	19.76	21.86	1.38	41.79
2 Maharashtra	21.17	21.40	49.18	1.40	10.93	20.25	1.37	13.96	13.54	21.01	13.08
3 Tamil Nadu	11.89	17.61	22.12	14.66	17.50	17.08	-0.29	16.68	29.14	4.81	34.30
4 UP	25.45	18	65.28	105.16	10.05	24.81	1.41	27.89	0.55	4.92	7.92

Source :13th Finance commission report, Public Finance Statistics 2016, CBDT Statistics 2018

It is generally believed that tax collection growth is directly co-relatable with the GDP growth, but to establish it empirically it is necessary to work out the GDP growth of different states and compare it with the growth of tax collections and to go for regression analysis to see the relationship between them. The details of GDP growth have been adopted from the statistics of Union Ministry of Finance and is tabulated as Table 5.

Table 5: GDP Growth of States

	05-06	06-07	07-08	08-09	09-10	10-11	11-12	12-13	2012-13	2013-14	2014-15	2015-16	2016-17
5 Karnataka	10.51	9.98	12.6	7.11	1.3	10.15	3.69	6.08	6.2	9.6	6.7	8.2	7.5
8 Maharashtra	13.35	13.53	11.26	2.58	9.3	11.26	4.52	7.78	6	7.3	5.4	8.5	9.4

9	Tamil Nadu	13.96	15.21	6.13	5.45	10.83	13.12	7.39	3.39	5.4	7.6	4.9	6.1	7.4
10	UP	6.51	8.07	7.32	6.99	6.58	7.86	5.58	5.78	4.7	5.8	4	8.1	7.2

Source :13th Finance commission report, Public Finance Statistics 2016, CBDT Statistics 2018

Figure 4 : State - wise GDP Growth



Source :constructed from Table 6

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From the above, it can be concluded that there is significant fluctuation in GDP growth of different states. While growth of Tamil Nadu is varying from 3.09 to 15.21, that of Karnataka is varying from 1.3 to 12.6 while that of Maharashtra is varying from 2.08 to 13.53. But in respect of state of Uttar Pradesh it is more steady and ranging from 4.0 to 8.1.

However, it is necessary to examine whether the southern states are justified in holding the view that they are not getting their fair share of central taxes. Constitutionally, the purpose of finance commission is to create some kind of 'equalization' among advantaged and disadvantaged states and therefore, division of the country on southern and northern lines is unfair and unjust. From the point of view of equalization, the adoption of population figures of 2011 Census as one of the criteria of devolution appears to be justified as adopting 1971 Census data was not only unrealistic, it also meant a case of a reverse discrimination for the heavily populated states. For example, no share of taxes contributed by the southern states is going to states like Maharashtra, Gujarat, Delhi, Punjab & Haryana which are located in north and west and are already developed states and their per capita income is even higher than that of southern states. Further, Maharashtra alone contributes about 37% of Central Taxes which is highest but it has never complained on this account. Most of the southern states had experienced massive social movement in the past, especially in the 20th century, resulting in demographic transition. For example, Kerala experienced a strong literacy movement, thanks to the efforts of the princely state of Travancore-Cochin, Jesuits and communists. Similarly, Tamil Nadu experienced the social (anti-Brahmin) movement, leading to social mobility and emancipation of women. Further, in the pre-Independence period, the expenditure on education and health was much higher in the Madras Presidency than in the Bengal Presidency. Thanks to these historical factors, the southern states experienced lower fertility rate than the northern ones, most of which are poor. Even after Independence, the expenditure on social sector had remained comparatively lower in northern states. The 'family planning' programmes were not implemented vigorously there. It should be remembered that no state would promote population growth deliberately, just to get more resources from the Finance Commission. The strategy for population planning not only warrants heightened governance, it also demands adequate resources that poor states obviously lack. Further there is a separate clause in the terms of 15th Finance Commission which rewards the states which reach fertility rates at replacement level and will certainly go to the benefit of southern states.

It may also be noted, that collection of taxes alone could not be a criteria for measuring of economic activity in a particular state. It is a well-known fact that taxes are normally paid by the Companies / Corporation at their head office or corporate office which are located in bigger towns like Mumbai, Delhi, Bangalore, Chennai, Kolkata, Hyderabad etc. For example, Tata Group is spread all over the country, with the predominant presence in West Bengal and Jharkhand. However, they pay most of taxes in Mumbai. Similarly Infosys & Wipro, well known I.T companies have their offices all over the country but they pay taxes at Bangalore. In the same way PSUs like HAL has their production facilities all over the country like in Kanpur, Koraput, Nasik etc. but it pays taxes in Bangalore. Likewise, most of the mineral rich states like Orissa, Jharkhand, West Bengal, and Chhattisgarh do not get income taxes from the mining companies which may be based in other cities / states.

Further, the very purpose of finance commission is to allocate higher resources to the States having higher population below the poverty line so that Human Development of such a state can take place. It is in this background that the states like UP get larger share from Central Taxes than they contribute. As per the latest statistics, UP gets about Rs.1.80 for every rupee contributed by it to the Central Kitty, while States like Karnataka and Tamil Nadu get only about only 47 paise & 40 paise respectively for each rupee contributed by them. But in the circumstances, we need to think in a holistic way as a country that all Indians get a decent life, education, healthcare, jobs and social dignity which includes women, dalits, Muslims, south, north, east, west. We must allocate resources equitably for the development and progress of one and all including and especially the weakest of us and not in terms of north and south division. The clamor of southern states may be justified in terms of the present parameters but in the process they should not ignore history. If we go back, in the pre-independence period, the deficit of Madras and Bombay presidencies used to be met from the surplus of Bengal Presidency. In fact, mineral rich northern states did not get a fair share of their due taxes / royalty and in a way subsidized the industrialization of the entire country.

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