Municipal Finance in India: Emerging Trends and Strategies for Resource Mobilization

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Abstract

Urban local governments are entrusted with a set of responsibilities of providing basic urban amenities and services to the people. They are dependent on states and centre for grant in aid and loans as the own resources of ULBs are grossly inadequate. There is mismatch between functions and municipal resources. The efforts for additional resource mobilization to fulfill the commitments by the ULBs are not adequate due to various factors. The ULBs are becoming dependent on transfers and fiscal devolution from central and state governments to meet out their financial requirements. Central Government has launched JNNURM and its subsidiary schemes for infrastructure development in selected cities and towns with massive financial investment. These schemes envisage strengthening of urban local bodies through introducing reforms and stepping up concrete efforts for additional resource mobilization. Thus, it is necessary to reduce dependence of local bodies on government support. They should effectively exploit the revenue potential through rationalization of assessment norms, simplification of procedures; rebate on timely payment, revision of old levies and taxes etc. Municipal governments may be allowed to enjoy fiscal autonomy with freedom of choice in regard to imposing new taxes and revising tax rates. It is argued that municipal bodies are not financially strong enough to tap capital market for undertaking infrastructure works which involve huge capital investment, long gestation period. But the provision of marketing borrowing will certainly motivate the municipal bodies to revamp their financial strength to mobilize resources from market. There is also need to encourage private sector involvement in the development, strengthening and creator of urban infrastructure. Against this backdrop , the paper purports to highlight the emerging trends in municipal finance and suggesting the measures for resource mobilization.

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Introduction

India is one of the least urbanized countries in the world because between 1951 and 2001, the level of urbanization increased by 13 percentage points only. However, it has the second largest urban population in the world and more than two third of it, lives in 393 cities that have population of over one lakh. The four mega cities viz., Mumbai, Kolkata, Delhi and Chennai with a population of more than 6 million each in 2001 accounted for almost one fourth of population living in cities. As per 2001 census, 285 million population i.e. 27.8 percent of 1027 million total population of India is residing in 4368 cities and towns in the country, where as in 1991, 25.7 percent population lived in urban areas. The decadal growth in urban population during 1991-2001 has been 31.2 percent whereas at the beginning of the 20th century, only 10.8 percent of total 218 million population of the country resided in cities and towns. The number of million plus cities has increased to 35 in 2001 from 12 in 1981 and 23 in 1991. These 35 million plus cities account for 107.9 million urban population of the country. As per 2011 census, urban population was reported to be 377.1 million constituting 31.6 percent population of the country. There were 7935 towns and cities in India as per the census, 2011 (Table 1).

Table 1: Urbanization in India

[redacted]

Urbanization is critical to the development of country. About 30 percent of India's population resides in urban centers which account for about 340 million persons in absolute term. The urban population of India is likely to increase by 590 million, constituting about 40 percent of total population by the year 2030. India will have the largest growing work force for the next 20 years, as 270 million Indians will join the working age population by the year 2030. Job growth in cities will be more robust, growing at around 3.6 percent annually increasing from around 100 million today to 220 million in 2030. Cities will account for 70 percent of all new jobs created in India during 2010 to 2030. (McKinsey, 2010) The startling fact is that the proportion of population living in smaller towns has shown declining trend over the period while there is massive growth in population of larger towns. Importantly, growth of population in smaller towns has been reported negative while the growth of population in large cities and towns has been found massive. During 2001, the high proportion of urban population has been reported to be in Delhi, Pondicherry, Goa, Chandigarh, Maharashtra, Mizoram, Lakshadweep, Tamil Nadu, Karnataka, Gujarat etc. The high rate of growth of urban population during 1991-2001 has been reported high in Dadra & Nagar Haveli (14.59 percent) followed by Arunachal Pradesh (7.0 percent), Andaman and Nicobar Islands (4.14 percent), Sikkim (4.83 percent), and Delhi (4.14 percent).Cities provide benefits beyond their own boundaries. McKinsey (2010) in its report has pointed out that 180 million people who live close to cities were benefited with the economic opportunities, markets and the connecting infrastructure in the urban centers. These people were assumed to live in rural areas next to the about 70 largest urban centers in India. India will have 68 cities by 2030 with population of more than one million, compared with the figure of 35 in 2001. Similarly, the number of urban centers is likely to increase by 6000 in 2030. However the concentration of urban population is still in larger cities. About 57 percent of urban population of the country resides in the urban centers, comprising of less than one million populations (Table 2).

Table 2: Size-wise Urban Population of India

Classification of Urban Centers	2008	2030
Tier-I (More than 4 Million)	93 (27.0)	155 (26.0)
Tier-I (1 Million to 4 Million)	52 (15.0)	104 (18.0)
Tier-I (Less than 1 Million)	195 (57.0)	331 (56.0)
Total	340 (100.00)	590 (100.00)

Source: *McKinsey, 2010,*

Note: *The figures in the parentheses indicate the percentage to the total.*

As per 2011 census, there were 468 Class-I cities with more than 1 lakh population while 7935 cities and towns were reported. Out of 468 Class-I cities, there were 3 metropolitan cities viz., Mumbai, Delhi and Kolkata having the population of more than 10 million while 5 cities viz., Chennai, Bangalore, Hyderabad, Ahmadabad and Pune were having the population of 5-10 million. 34 cities were reported having the population in between 1-2 million while 372 cities and towns had population of 1 lakh to 5 lakh . As per information available, 3700 ULBs were reported in India and most of them were Nagar Panchayat (52.35 percent) and Municipalities (44.73 percent). Only 108 Municipal Corporations were reported during 2001. The numbers of ULBs were reported high in Madhya Pradesh followed by West Bengal and Bihar. There were only 44 ULBs in Jharkhand. In Madhya Pradesh, about 70 percent ULBs were reported in the category of Nagar Panchayats (Table 3).

Table 3: Number of Urban Local Bodies by Civic Status

Economic Growth

India is one of the fastest growing economies in the world today. After recording a growth rate of 5.5 percent per annum during 1981-2001, there has been further acceleration in GDP growth to 7.7 percent per annum during 2001-11. The economy has weathered the impact of the global slowdown of 2008 much better than most and is well on its way to resuming its journey to 8-9 percent per annum GDP growth. The transformed growth scenario in the economy in the 2000s and the expected acceleration in the growth of GDP, increasingly moving towards labour-intensive manufacturing, construction, and services, should augur well for migration in the years ahead. As more states join the fray of improving their investment environment through economic reforms, this should increase opportunities for non-agricultural employment. As the faster growth is expected to occur in the context of a more open economy, employment elasticity of the growth should increase. This should lead to greater employment opportunities in the industry and services sectors, and larger migration from rural to urban areas. Other forces contributing to urban growth would be expansion of city boundaries, large villages growing into towns in situ, and emergence of new towns either planned or the result of market forces possibly along the transport and growth corridors.

Unlike what would be predicted by the standard theories on rural-urban migration like Lewis (1954) and Harris-Todaro (1970), the evidence in India suggests that the rural-urban differentials in productivity have widened since 1993-94, indicating that there is considerable scope for migrants to take advantage of the higher productivity non-agricultural sectors if they can be equipped with the skills and education relevant for employment in urban areas. The economy seems to be far from reaching saturation point in migration and it is reasonable to expect a hastening in the pace of urbanization. The McKinsey Report (2010) on India's urbanization prospects estimates that over the period 2010-2030, urban India will create 70 percent of all new jobs in India and these urban jobs will be twice as productive as equivalent jobs in the rural sector.

Trends in urbanization in India have necessarily to be seen in the context of overall trends in population growth. India is experiencing a significant slowing down of population growth in the period 2001-11, reflecting a decline in fertility rates. The data shows growth of population after slowing down marginally from 2.1 percent per annum in the 1980s to 2 percent per annum in the 1990s is estimated to decelerate significantly in the decade 2001-11, increasing by only 1.5 percent per annum. The deceleration in rural population growth is from 1.7 percent per annum to 1.2 percent per annum and that in urban population from 2.8 percent per annum to 2.4 percent per annum. Within the context of a slower growth of urban population in 2001-11 compared with the earlier decade, a differentiated urban spatial structure is emerging as India advances on the path of urbanization and economic growth. The cities of India have been growing in population size. In 1951, there were only five metropolitan cities (with population of over 1 million), i.e., Kolkata, Mumbai, Chennai, Hyderabad, and Delhi. Their number increased to 12 in 1981 and 35 in 2001. Their share in urban population increased from 18.9 percent in 1951 to 27.7 percent in 1981 and 37.8 percent in 2001. By 2001, all the original five metropolitan cities had grown to population of over 5 million, and Bangalore had joined their ranks. The 29 cities which had population between 1 million and 5 million in 2001 included four state capitals, i.e. Jaipur, Lucknow, Bhopal, and Patna, and other cities such as Meerut, Faridabad, Pune, Surat, Nagpur, Kanpur, and Ludhiana**.** As the projections for 2011 show, the number of such cities increases to 50 and their population accounts for 42.3 percent of the total urban population, and Ahmadabad and Pune join the rank of cities with population over 5 million. By year 2006, 27 percent of urban population lived in tier-I cities (with population of more than 4 million), 14 percent in tier-II cities (1 million to 4 million) and 59 percent in tier-III & IV cities (population of less than one million). The contribution of urban centers in India's GDP is estimated to be 58 percent in 2008. The contribution of tier-III & IV cities is estimated to be about half of the total GDP coming from urban India (Table 4).

Table 4: India's Urban GDP

[redacted]

There has been increasing trend of contribution of cities in India's GDP. The share of cities in GDP was reported 46 percent in 1990 which increased to 54 percent in 2001 and 58 percent in 2008. It's share is likely to increase by 70 percent by the year 2030(Table 5).

Table 5: Contribution of Cities in GDP

[redacted]

Structure and Composition of Municipalities

The 74th Constitution Amendment Act, 1992 envisages the following types of municipalities:

- **Municipal Corporation**

  The Act made a provision for the constitution of Municipal Corporation in the metropolitan cities which have population of one million and above. The Governor generally takes the following points into the account while notifying municipal corporation: (i) the population of the area; (ii) the density of population; (iii) the percentage of employment in non-agricultural activities; (iv) the economic importance of the area; (v) such other factors as the Governor may deem fit.

- **Municipal Council**

  A smaller urban area is notified by the Governor taking into account the above factors as municipal council. In most of the states, population ranges in between 15,000 to 5 lakh. Andhra Pradesh, Gujarat, Karnataka and West Bengal have provision of population density while only Andhra Pradesh and Karnataka have made criteria of revenue generation.

- **Nagar Panchayats**

  Transitional area is to be known as the Nagar Panchayat. This has also been left to the Governor's notification taking into account the same considerations as in case of larger area in transition from a rural to urban. Population, population density, percentage of population engaged in non-farm activities and economic importance are important criterion for its formation. The population of Nagar Panchayat varies from state to state. It ranges in between 5,000 to 5 lakh. Andhra Pradesh, Gujarat, Karnataka and Maharashtra have made provision for formation of Nagar Panchayat in a city or town if 50 to 75 percent population is engaged in non-agricultural activities.

- **Functions and Finances**

The Constitutional Amendment Act, 1992 assigned a critical role in urban development and governance. The Act inserted the Twelfth Schedule (Article 243W) to the Constitution of India providing for an illustrative list of legitimate municipal functions

Panel 1: Twelfth Schedule of the Constitution

Sl. No	Functions
1.	Urban Planning, including town planning
2.	Regulation of land use and constitution of buildings
3.	Planning for economic and social development
4.	Roads and bridges
5.	Water supply for domestic, industrial and commercial purposes
6.	Public health, sanitation conservancy and solid waste management
7.	Fire services
8.	Urban forestry, protection of environment and promotion of ecological aspects
9.	Safeguarding the interests of wealth sections of society, including the disabled and mentally retarded
10.	Slum improvement and upgrading
11.	Urban poverty alleviation
12.	Provision of urban amenities and facilities such as parks, gardens, play grounds
13.	Promotion of Cultural, educational and aesthetic aspects
14.	Burials and burial grounds, cremation, cremation grounds and elctric cremations
15.	Cattle pounds, prevention of cruelty to animals
16.	Vital statistics including registration of births and deaths
17.	Public amenities including street lighting, parking lots, bus stops and public conveniences
18.	Regulation of slaughter houses and tanneries

Source: *74th Constitutional Amendment Act*

The state list in the Constitution empowers the state governments to lay down the functions, powers and responsibilities of municipal governments. Accordingly out of powers and responsibilities enumerated in the state list, the state governments have assigned certain functions and duties to municipalities. Typically, these have consisted of public health and sanitation, burials and cremations and cremation grounds, libraries, museums and other similar institutions controlled and funded by the state; communications, i.e. roads and bridges, water supplies, drainage, and embankments subject to the provision of list, and markets and fairs. The main functions which the municipalities are associated and which are generally, though not uniformly, performed by them include services that have the characteristics of private goods, for example, water supply, sewerage and drainage, and conservancy and sanitation and others that are in the nature of public goods, for example, street lighting and municipal roads. In addition, the municipalities are vested with a number of regulatory duties such as development of markets, commercial complexes, and the like. Several municipal corporations have a larger functional domain, which consists of running hospitals and dispensaries, electricity generation, and distribution and bus transport services. The functional domain of municipalities has witnessed periodic shifts and changes, on account of the withdrawal of certain functions and creation of development authorities such as PHE, Land Development Authorities, State Road Transport Corporation, etc. There is mismatch between the functions and finances.

The incorporation of schedule 12 into the Constitution has been understood that the municipal functional domain has acquired some sort of a discrete character, apart from an expansion of its portfolio. However, the functions and duties enumerated in schedule 12 are not in addition to what the municipalities were responsible for in the pre-1992 period. There is substantial overlap between the functions of municipalities in pre-1992 period and those that are listed in Schedule 12. Of the 18 functions enumerated in Schedule 12, 11 formed part of the municipal domain even in pre-1992 period. These are regulation of land use and construction of buildings, roads and bridges; water supply for domestic, industrial and commercial purposes; public health, sanitation, conservancy, and solid waste management; fire services; provision of urban amenities and facilities such as parks, gardens and play grounds; burials and burial grounds; and cremation grounds and electric cremations; cattle ponds, prevention of cruelty to animals; vital statistics including registration of births and deaths; public amenities including street lighting, bus stop and public conveniences, and regulation of slaughter houses and tanneries. The remaining functions incorporated in the Schedule 12 are part of the state list and concurrent list.

In order to strengthen the fiscal base of the urban local bodies, the 74th Amendment empowers the state legislature to enact law in order to:

1. authorize an urban local body to levy, collect and appropriate taxes, duties, tolls, and fees;
2. assign to an urban local body taxes, duties, tolls and fees levied and collected by the state government; and
3. Provide for making grant in aid to the urban local bodies from the Consolidated Fund of the state.

The principles which shall govern the above fiscal resources have been left to be recommended by the State Finance Commission. The commission shall lay down principles which should govern:

1. the distribution between the state and the urban local bodies of the net proceeds of the taxes, duties and fees leviable by the state, which may be divided between them and the allocation between the urban local bodies at all levels of their respective shares of such proceeds;
2. the determination of the taxes, duties, tolls and fees which may be assigned to or appropriated by the urban local bodies; and
3. the grants in aid to the urban local bodies from the Consolidated Fund of the state.

Urban local bodies derive finances from tax and non tax sources. They also receive funds from the state governments in the form of grants in aid as also a share in taxes collected by the state government. There is some variation among the states in the matter of taxation powers entrusted to the ULB's. However, significant variations exist across states in the application of taxation powers and the rate structure of taxes. Octroi is levied only in a few states while professions tax is limited to few others.

The Constitution of India does not lay down the revenue base for municipalities. The powers to determine their revenue base are

Income Tax authority, tax base, tax rate setting, local tax autonomy, or even the grants in aid and other forms of transfers rests with the state governments. Within this framework, the state governments have specified the taxes that the municipalities can levy and collect, which historically have comprised of taxes on land and buildings; taxes on entry of goods into a local area for consumption, use or sale therein; taxes on advertisements other than advertisements published in newspapers; taxes on professions, trades, callings and employment, and taxes on entertainment. In addition, there are charges, fees and fines forming the non-tax base of municipalities. Taxes on property and taxes on the entry of goods into a local area for consumption, use or sale therein (octroi) firm the backbone of municipal tax base in India. The revenue base of municipalities in Indian states has shown little change. Octroi, a major source of revenue for municipalities has been abolished without being substituted by any other local source and has substantially shrunk the revenue base of municipalities in such states as Haryana, Orissa, and Rajasthan. However, many states have changed the system of property taxation and are in process of shifting from a single entry, cash based system to an accrual based accounting system. Some corporations have raised funds in the capital markets for financing city based infrastructure activities by using credit enhancement instruments.

Revenue Assignment of ULBs

Most common revenue sources available to the municipalities to discharge various local government functions in India can be divided into the following broad categories: (i) Taxes; (ii) Non-Taxes; (iii) User Charges, fees and sale % hire purchase; (iv) assigned revenues; (v) grants and contribution; (vi) debt and (vii) other revenues (Panel 2)

Panel 2 : Revenue Assignment of Urban Local Bodies

Category	Particulars
Taxes	Property Tax, Advertisement Tax, Tax on Animals, Vacant Land Tax, Taxes or Carriages and Carts, Octroi
Non Taxes, User charges & Fees Charges	Water Charges, Water Supply Donations, Trade Licensing Fee, Building Permit Fees, Development Charges/Betterment Charges, Mutation Fee, Magisterial Fines, Market Fee, Slaughter House Fee, Encroachment Fee, Parking Fee etc.
Sales & Hire Charges	Sale of Rubbish, Certificate Fees, Sale of Forms, Staff Raters Rents, Shop Room Rents
Assigned Revenues	Entertainment Tax, Surcharge on Stamp Duty, Profession Tax, Motor Vehicles Tax, Entry Tax

Grants & Contributions	
(a) Non Plan Grants	Animal and Vehicle Tax Compensation, Toll Compensation (Octroi Compensation), Property Tax Compensation, Per Capita Grant.
(b) Plan Grants	Road Grants, School Building Grants, Master Plan Grants Integrated Development of Small and Medium Towns (UIDSSMT), SJSRY, NSDP, ILCS, EIVS, UBSP, JNNURM, IHSDP etc.
Debt	Water Supply Schemes, Sewerage Schemes, Roads, ILCs, UIDSSMT, IHSDP, JNNURM, other civic Infrastructure Projects and Capital Works.

Source: *P.K. Mohanty, 2005*

Property tax is the most important source of taxation in majority of the urban local bodies in the country. A few states like Maharashtra and Gujarat do still have octroi, considered to be an obnoxious tax and needed to be phased out. The major sources of municipal user charges and fees levied by selected municipal corporations in the country are shown in Panel 3).

Panel 3: Major Sources of User Charges and Fees of Municipal Corporation in India

State	Municipal Corporation	User Charges and Cess
Maharashtra	Greater Mumbai	Water charges, sewerage charges, Building License Fees
West Bengal	Kolkata	Planning Fees, Car Parking Fees, Mutation Fees
Karnataka	Bangalore	Betterment Charges, Building License Fees, Penalty for late Tax Payment
Orissa	Bhubaneswar	Building License Fees, Market Fees, Water Charges, Building related Fees
Gujarat	Surat	Water Charges, Building related Fees, Betterment Charges
Tamil Nadu	Chennai	Building License Fees, Market Fees, Other License Fees, Parking Fees
Andhra Pradesh	Hyderabad	Dangerous and Offensive Trade License Fees, Market Fees, Slaughter House Fees
Uttar Pradesh	Kanpur	Building License Fees, Market Fees

Panel 4 presented below shows the major sources of assigned or shared revenues in selected municipal corporations in the country.

Panel 4: Panel showing the Shared Municipal Revenue in India

State	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
Tamil Nadu	Chennai	Surcharge on Sales Tax, Duty on Transfer of Property, Entertainment Tax
Gujarat	Surat	Transfer of Immovable Property Tax, Professional Tax, Entertainment Tax

The major sources of grants in aid provided to municipalities are octroi compensation, development grants and urban infrastructure projects based grants (Panel 5).

Panel 5: Major Sources of Grants in Aid to Municipal Corporations in India

State	Municipal Corporation	Grants in Aid to Municipal Corporation
Maharashtra	Greater Mumbai	Primary Education Grant, Secondary Education Grant
West Bengal	Kolkata	Dearness Allowance Grant, Great to Implement Recommendations of Pay Commission, Water Supply, Sewerage and Drainage Grants
Karnataka	Bangalore	Octroi Compensation, Motor Vehicle Tax Compensation, Family Planning Schemes Grants
Orissa	Bhubaneswar	Salary and 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	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, Education Grant (Primary & Secondary)
Uttar Pradesh	Kanpur	Octroi Compensation, Salary Grant, Education Grant (Primary & Secondary), Medical Grant, Road Grant

In view of the growing physical mismatch between the functional responsibilities and existing resources of ULBs, Government of India under JNNURM Mission has extended financial support to the selected cities; however, the financial assistance has been mainly of capital expenditure for development of infrastructure and improving the delivery of public services. The reforms agenda under JNNURM Mission for strengthening of ULBs is still unfinished and it requires political and administrative will power besides concrete efforts for resource mobilization and imposing user chargers for the services being provided by ULBs.

Trends in Municipal Finances

The revenue structure of the municipalities shows that the relative share of own sources of revenue to transfers have declined. Although the share of tax income to total revenues declined substantially between 1974-75 and 1979-80, it went up from 15.39 percent in 1979-80 to 48 percent in 1997-98. The share of non tax revenue, however, has been declining over the years; it has declined from 22 percent in 1979-80 to 17 percent in 1997-98. Municipal bodies raised approximately Rs. 3900 crore on their own during the year 1991-92 which constituted a mere 4.7 percent of revenues by the Central Government and 8 percent of the revenues raised by State Governments. There has been growth of 119.69 percent in total receipts of ULBs in India during 1997-98 to 2004-05. However, the growth in total receipts of ULBs in India 2004-05 to 2007-08 was reported only 66.05 percent. During 2007-08, tax revenue constituted about 34 percent in total receipts while non-tax revenue constituted only 19 percent. Thus, transfers from Central and State Governments accounted for 44 percent. There has been fluctuation in the composition of revenue structure of ULBs in India during 1974-75 to 2007-08. The share of tax revenue in total receipts has shown a declining trend while the share of government transfers is showing increasing trend except the year 1979-80 (Table 6).

Table 6: Trends of Revenue Structure of ULBs in India

[redacted]

Sources of municipal finance during the recent period are shown in Table 7 . There has been growth of 112.37 percent in total revenue of the local governments during 2002-03 to 2007-08. During 2002-03, own revenue constituted 63.48 percent in total revenue of the local bodies while during 2007-08, own revenue constituted only 52.94 percent. Thus, there has been drastic decline in the share of own revenue in total revenue of the local governments. Non-tax revenue constituted 21.23 percent in 2002-03 while it was reported only 18.56 percent in 2007-08. There has been manifold increase in the transfers from Government of India during 2002-03 to 2007-08. Even there has been phenomenon growth in the devolution of funds to the ULBs during the period. Total revenue comprised of only 0.85 percent of GDP in 2002-03 while its slightly increased to 0.94 per cent during 2007-08. Own revenue accounted for 0.54 percent of GDP in 2002-03 while it slightly decline to 0.50 percent in 2007-08. Total expenditure of ULBs constituted only 1 percent of GDP in 2007-08. Out of total expenditure, revenue expenditure accounted for 60.46 percent in 2007-08 while revenue expenditure constituted 72.54 percent during

2002-03. Thus, there has been increasing trend in capital expenditure as centrally sponsored schemes made provision of capital expenditure for infrastructure development and improving the system for the delivery of public services.

Table 7: Sources of Municipal Finance

(Rs. in crore)

[redacted]

Total revenue of ULBs as proportion of GSDP is shown in Table 8. During 2002-03, total revenue of ULBs against the GSDP was reported significantly high in the state of Chhattisgarh followed by Madhya Pradesh and West Bengal while it was found low in Assam and Bihar. Similarly, 2007-08, total revenue of ULBs comprised of GSDP in the tune of 1.73 percent of GSDP in Chhattisgarh, 1.5 percent in Madhya Pradesh and 0.71 percent in West Bengal.

Table 8: Total Revenue of Urban Local Bodies in Selected States

(Percent of GSDP)

[redacted]

Own revenue of ULBs as proportion of GSDP in selected states, is shown in Table 9 During 2002-03, own revenue constituted 0.34 percent in West Bengal, 0.31 percent in Chhattisgarh and only 0.08 percent in Jharkhand while during 2007-08, own revenue of GSDP was found significant in the state of West Bengal, Chhattisgarh and Madhya Pradesh.

Table 9: Own Revenue of Urban Local Bodies

(Percent of GSDP)

[redacted]

A study conducted by O.P. Mathur (2009) in selected cities in different states of India demonstrates that the share of property tax in total municipal revenue is about one fourth only. During 2004-05, property tax as percentage of total municipal revenue was reported 26 percent while its slightly decline to 23 percent during 2006-07. Property tax demand was estimated to be Rs. 11213.70 crore during 2004-05 which slightly increased in 2006-07. However, property tax revenue against the property tax demand was reported quite low (only 34.64 percent). Property tax revenue against the property tax demand was reported only 39.56 percent during 2006-07. The efficiency of property tax collection was reported low, less than 40 percent. Per capita tax revenue was reported Rs. 442.10 in 2004-05 which slightly increased to Rs. 486.10 in 2006-07. Property tax as percentage of municipal expenditure was reported only 27 percent in 2006-07 (Table 10).

Table 10: Revenue Status of Property Tax

[redacted]

Municipal expenditure grew by 117.41 percent during 2002-03 to 2007-08 while the growth of revenue expenditure was reported 81.19 percent during the corresponding period. The growth of capital expenditure grew by 213.14 percent during the period which shows an increasing trend due to launch of centrally sponsored schemes for the infrastructure development. Total expenditure comprises only 0.88 percent of GDP during 2002-03 which slightly increased to 1 per cent during 2007-08 (Table 11).

Table 11: Municipal Expenditure in India

(Rs.in Crore)

[redacted]

Property tax composition in municipal expenditure has been insignificant in most of the urban local bodies of India. Even in Patna, where property tax reforms were introduced and Patna Model of Property Tax is treated as the best practice, property tax constituted only 9 percent of the total municipal expenditure. However, it was found somewhat satisfactory in Meerut (23.5 percent) followed by Varanasi (17 percent), Delhi (16.3 percent) and Allahabad (13 percent). The dependence of Municipal Corporation on central and state transfers was found significantly high in Meerut followed by Agra, Allahabad, Patna and Jaipur. Even per capita property tax was reported very low in most of the cities and particularly in the city of Patna it is Rs. 25.5 (Table 12).

Table 12: Composition of Property Tax in Municipal Expenditure

[redacted]

A study conducted by O.P. Mathur (2009) shows that there has been increasing trend of revenue expenditure on municipal services. Average cost recovery constitutes only 18.2 percent in Lucknow while it was reported high i.e. 55.2 percent in Palakkad in Kerala. Thus, the ULBs are spending more on municipal services as against their revenue income (Table 13).

Table 13 : Average Cost Recovery of Selected ULBs: 2007-08

[redacted]

It is clear from the above analysis that the present institutional arrangements for the provision of urban services is unlikely to sustain in the face of mounting fiscal pressures on municipal bodies and the rapid demand for urban services. The new economic policies, oriented towards market based economy led growth objectives, would also entail a significant contribution of the urban sector and efforts would be needed to reduce infrastructure bottlenecks and increase urban productivity and employment. The growing fiscal stress on municipal bodies will require fiscal corrections, effective fiscal management, and resources mobilization through initiating financing reforms. Moreover, legislative exercises to precisely define the functions and finances of municipal bodies especially after functional devolution as per 74th Amendment Act are needed. Again, there should be re-assessments of finances of municipal bodies after complete functional devolution. Introduction of administrative reforms to develop an accountable municipal bureaucracy with suitably design policies regarding staff recruitment, incentives and penalties to ensure results, results, performance contracting etc. is also called for. Training of newly elected municipal representatives and municipal officials regarding the Constitutional mandates and especially effective fiscal management/ administration is also needed. As per fiscal needs of municipal bodies, State Governments should make serious efforts for resource mobilization through enlarging fiscal domain of local bodies and its resource base.

Trends Analysis of Municipal Finance

A study of selected JNNURM cities in pre and post-JNNURM period by the author during 2011-2012 reveals interesting trends and patterns. There has been significant increase in the per capita municipal revenue in the post-JNNURM period (2010-11) as compared to the per capita municipal revenue in the pre-JNNURM period (2000-01). However, contrast variations emerge from the per capita municipal revenue across the urban local bodies (Table 14). Per capita own resources in pre-JNNURM period were reported significantly high in Bhopal (Rs. 378) followed Guwahati (Rs. 236) and Raipur (Rs. 202) and lowest in Bodh Gaya (Rs. 37). During the post-JNNURM period, per capita own resources were reported significantly high in Bodh Gaya (Rs. 1562) followed by Bhopal (Rs. 1065), Asansol (Rs. 1056) and low in Ranchi (Rs. 161). Per capita municipal revenue during the pre-JNNURM period were reported significantly high in Raipur followed by Bhopal, Guwahati, Puri and low in Bodh Gaya while during the post-JNNURM period, per capita municipal revenue were recorded significantly high in Puri (Rs. 6064) followed by Guwahati (Rs. 3117), Ranchi (Rs. 2825) and Asansol (Rs. 2340). It was recorded low in Raipur (Rs. 905).

Table14 : Per Capita Income of Municipal Revenue

(In Rs.)

[redacted]

Per capita municipal expenditure was reported significantly high during post-JNNURM period (2009-10) as compared to pre-JNNURM (2000-01). However, contrast variations emerge across the urban local bodies (Table 15). During pre-JNNURM period, per capita municipal expenditure was recorded significantly high in Raipur (Rs. 689) followed by Bhopal (Rs. 422), Puri (Rs. 325), Guwahati (Rs. 307) and low in Ranchi (Rs. 78). During the post-JNNURM period, per capita municipal expenditure was recorded high in Puri (Rs. 6046), Guwahati (Rs. 3117), Ranchi (Rs. 2804), Raipur (Rs. 2110), Bhopal (Rs. 1700). It was found low in Bodh Gaya (Rs. 162).

Table 15: Per Capita Municipal Revenue Expenditure

(Rs.in Crores)

[redacted]

The growth of municipal revenue during the pre (2001-02 to 2003-04) and post-JNNURM period (2004-05 to 2010-11) in the selected local bodies demonstrates that there has been higher growth in municipal revenue in post-JNNURM period as compared to the growth of municipal revenue in pre-JNNURM period (Table 16). During pre-JNNURM period, the highest growth in own revenue sources of ULBs was recorded in Ranchi (104.42 percent) followed by Asansol (62.89 percent), while it was found negative growth rate in Guwahati. During post-JNNURM period, the highest growth of municipal revenue was recorded in Guwahati (1081.26 percent) followed by Puri (362.77) while it was found negative growth in Bodh Gaya. The growth in tax revenue was recorded high in Ranchi, Bhopal and Puri during pre-JNNURM period while during post-JNNURM period, tax revenue grew at the faster pace in Puri, Bodh Gaya, Ranchi and Bhopal. The growth in non-tax revenue was recorded significantly in Ranchi (197.52 percent) followed by Bodh Gaya (53.98 per cent) during the pre-JNNURM period while growth of non-tax revenue was recorded significantly high in Puri (351.26 percent).

Table 16: Growth of Municipal Revenue

(In Percentage)

[redacted]

Growth of municipal expenditure during the pre and post-JNNURM period demonstrates that there has been higher growth in total municipal expenditure in post-JNNURM period as compared to the growth of municipal expenditure during pre-JNNURM period (Table 17). During pre-JNNURM period, the significant growth of municipal expenditure was recorded in Ranchi (235.42 percent) followed by Bodh Gaya (74.02 percent) and negative growth in Puri. The growth of municipal expenditure during the post-JNNURM period was recorded significantly high in Puri (3462.80 percent) followed by Ranchi (1280.50 percent) while it was recorded low in Bodh Gaya (63.7 percent). The growth in establishment expenses in post-JNNURM period was recorded high, as compared to the growth in municipal expenditure in pre-JNNURM period, in Puri, Ranchi and Bhopal. Due to availability of capital revenue from JNNURM and other centrally sponsored schemes as well as international funding agencies, there has been higher growth in revenue income and revenue expenditure during the post-JNNURM period.

Table 17: Growth of Municipal Revenue Expenditure

(In percentage)

[redacted]

Composition of municipal revenue during pre-JNNURM and post-JNNRUM period reveals interesting facts (Table 18). The share of own revenues during pre-JNNURM period (2003-04) was recorded high in Bhopal (67.95 percent) followed by Asansol (48.84 percent), Ranchi (46.92 percent) and Bodh Gaya (43.42 percent). Own resources during post-JNNURM period (2009-10) constituted highest in Bhopal (79.03 percent), followed by Raipur (62.18 percent), Bodh Gaya (62.12 percent) and Asansol (57.53 percent). Thus, there has been structural change in the composition of municipal revenue over the period. During pre-JNNURM period, grants and transfers accounted significantly high in Guwahati (81.88 percent) followed by Puri (71.57 percent), Raipur (65.54 percent) and Bodh Gaya (56.58 percent). During the post-JNNURM period, grants and transfers constituted highest share in Puri (95.16 percent) followed by Ranchi (82.46 percent), Guwahati (81.08 percent) and Bodh Gaya (37.88 percent). Thus, it is indicative that ULBs are becoming dependent on grants and transfers from central and state governments for meeting out their municipal expenditure as their own sources are grossly inadequate.

Table18: Composition of Municipal Revenue

(In Percentage)

[redacted]

Establishment is the major head of expenditure in urban local governments (Table 19). The expenditure for administrative and establishment head is gradually increasing. During pre-JNNURM period (2004-05), the share of establishment cost was recorded high in Guwahati (97.56 percent) followed by Bhopal (36.09 percent), Ranchi (30.29 percent). During post-JNNURM period (2009-10), witnessed the highest share of establishment expenses in Asansol (46.84 percent) followed by Guwahati (39.36 percent), Raipur (38.9 percent) and Bhopal (33.10 percent). It was found as low as 1.88 percent in Puri but it does not mean that establishment expenses are low in proportion and absolute term as some of the local bodies have shown administrative and establishment cost under the heads of different civic services being delivered by them.

Table 19: Composition of Municipal Expenditure

(In Percentage)

[redacted]

It appears from the analysis of municipal finances in selected states and ULBs that there has been positive and significant impact of JNNURM on the municipal finances. The income of the ULBs has increased besides increasing the tax and non tax net for resource mobilization .The per capita availability of municipal income and expenditure also shows positive impact of Mission while the higher growth in municipal income and expenditure during post JNNURM period has shown positive trends.

Strategies for Resource Mobilization

- It is necessary to reduce dependence of local bodies on government budgetary support. They should effectively exploit the revenue potential through rationalization of assessment norms, simplification of procedures; rebate on timely payment, revision of old levies and taxes.
- Municipal governments may be allowed to enjoy fiscal autonomy with freedom of choice in regard to imposing new taxes and revising tax rates. It is argued that municipal bodies are not financially strong enough to tap capital market for undertaking infrastructure works which involve huge capital investment, long gestation period. But the provision of marketing borrowing will certainly motivate the municipal bodies to revamp their financial strength to mobilize resources from market.

- Urban local bodies need to be strengthened as local self-government with clear functions, independent financial resources, and autonomy to take decisions on investment and service delivery. They must also be made accountable to citizens.
- There is also need to encourage private sector involvement in the development, strengthening and creator of urban infrastructure. The conducive investment climate has to be created for encouraging the greater participation of private sector through introduction of suitable package of incentives. The concept of commercialization of urban infrastructure is very successful in developed countries. It can be also adopted in India with judicious mix.
- Contracting out of urban services has been quite common in the western countries. In this system, local authority contracts with private firm or public agency to take responsibility for operation and maintenance of a service or specific tasks. These arrangements can be based on profit sharing arrangement.
- It is also suggested that in effective public-private partnership should be developed in respect of each major urban services as well as at all the stages of activities from planning to resource mobilization, construction, management and maintenance.
- Urban local governments in India are among the weakest in the world both in terms of capacity to raise resources and financial autonomy. While transfers from state governments and the Government of India have increased in recent years, the tax bases of ULBs are narrow and inflexible and lack buoyancy, and they have also not been able to levy rational user charges for the services they deliver. Thus, it is imperative to broaden the tax net and effective implementation of user charges by the ULBs through administrative and political will.
- Local government severely lack the capacity for planning for local economic development and capital investments, preparation and management of projects, financial management and maintaining appropriate accounting and information systems which are crucial to efficient provision of urban infrastructure. Strengthening of local governments in these areas is imperative.
- In view of the importance of urban infrastructure for economic growth, the Government should take step by providing substantial funds and facilitating the use of additional mechanisms for

funding of ULBs. The unfinished agenda of municipal reforms need to be completed.

- User charges need to be structured to meet operation and maintenance cost, debt servicing, and depreciation towards the cost of the project. In addition, they must also generate some surplus to enable building the equity base of ULBs, supported. Moreover, levying of water and sewerage charges, parking, etc. is imperative to increase the net of user charges and non-tax revenue of the ULBs. The user charges are also required to be assessed on regular basis for rationale increase depending on the cost of operation and maintenance and other necessary financial requirements.
- The ULBs must be made an integral part of revenue mobilization. The combination of benefit taxes, user fees, development charges and borrowings for long gestation capital works are appropriate for meeting out growing municipal expenditure. User charges should be based on the marginal cost of additional units of services from the infrastructure and development charges on the marginal cost of extending infrastructure.
- There is imperative need to evolve a national consensus on the municipal finance schedule for assignment of the ULBs to match the list of functions included in the 12^{th} schedule. The state governments need to provide freedom to ULBs in matters relating to tax base, tax rate and exemptions. The new taxes such as vacant land tax, taxation on central and state governments properties, profession tax, entertainment tax, advertisement tax, business licensing fee or tax, motor vehicle tax, development impact fee, planning permission fee, betterment levy, surcharge on stamp duty on registration deeds and a share in value-added tax, etc. may be included in the scheme of revenue assignment to ULBs.
- Property tax is collected under various municipal Acts with components such as water tax, drainage tax, lighting tax, conservancy tax and general tax. It is desirable that services like water supply, sewerage, solid waste management, drainage may be financed or maintained through user charges as the property tax denotes creation of infrastructure not for delivering of services and therefore delivery of basic services to the citizens may be operated and maintained through rationale user charges.
- The system of inter-governmental fiscal transfers should be made

effective to resolve the problems of vertical imbalance in the assignment of responsibilities and fiscal powers between the centre, state and local bodies. These transfers may be an effective tool to correct the growing vertical imbalance and reduce the inequalities amongst ULBs.

- There is imperative need to review the expenditure norms and rationalizing them to realistic levels. Effective expenditure management and reducing the administrative and establishment expenditure by the ULBs is imperative in the present context. The accounting reforms such as accrual based accounting, and adoption of national municipal accounting manual, etc. is likely to enable the ULBs to improving financial health.
- There is imperative need to create municipal finance data base at the ULB level, state level and national level. In order to prepare a municipal finance data base and its MIS, it is imperative to evolve a standard format of preparing data base by the ULBs and state level. It is also suggested that Government of India should evolve a standard format of budgeting of the urban local governments so that uniform data may be compiled from the ULBs for assessment and analysis.

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