

The many faces of Indian Federalism

during a Pandemic

NCAER 18th India Policy Forum Lecture

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15th July, 2021

Let me, at the outset, express my gratitude to the NCAER for inviting me to give this 18th India Policy Forum Lecture on “Federalism during the Pandemic”. I would like to thank Poonam Gupta, who, shortly after taking this responsibility as the new Director-General of the NCAER, has arranged this exceedingly cohesive event for which I am privileged to give this speech. I am also grateful to my friend, scholar and policy shaper Dr. Arvind Panagariya for kindly chairing the session.

Constitutions are written with predictability and certainty. They are not designed for Black Swan events like this pandemic. To quote James Madison, “In framing a system which we wish to

last for ages, we should not lose sight of the changes which ages will produce. This is equally applicable to rules, regulations, conventions and laws.

Introduction

The term Federalism was introduced by the German born American economist Richard Musgrave in 1959. According to Wallace E. Oakes writing in 1999 much later on Fiscal Federalism said that “it is concerned with understanding of which functions and instruments are best centralised and which are best placed in the sphere of decentralised levelsof government. This concept applies to all forms of government: unitary, federaland confederal”.

The evolution of fiscal federalism in India thus has a long genesis. It primarily dates back to the government of India Act of 1919 and 1935. While the Act of 1919 provided for a separation of revenue heads between the Centre and the

provinces, the 1935 Act allowed for the sharing of Centre's revenues and for the provision of grants-in-aid to provinces. The Government of India Act, 1935 established the basic structure of fiscal federalism in India, one that survives even today.

Article 1 of our Constitution describes India, that is, "Bharat as a 'Union of States' rather than a 'Federation of States'". The country is described as 'Union' although its Constitution is federal in structure. On November 4, 1948, while moving the Draft Constitution in the Constituent Assembly, B.R. Ambedkar responded to the question as to why India is a "Union" and not a "Federation of States":

"The Drafting Committee wanted to make it clear that though India was to be a federation, the federation was not the result of an agreement by the States to join in a federation and that the federation not being the result of an agreement no State has the right to secede from it. The Federation is a Union because it is indestructible."

Political scientist Alfred Stepan classified India as a “holding together” as opposed to a “coming together” federation. Unlike the federal form of government in the United States, which is described as an indestructible Union composed of indestructible States, India is an indestructible Union of destructible States.

Institutional Mechanism Envisaged at the time of Independence

Broadly speaking, in the evolution of Fiscal Federalism there has been a marked stability in the process and procedures. The annual budgetary processes of both the Central and the Federal Governments are independent exercises and have to go through the Parliament or State Legislature. The Finance Commission which was first constituted in 1951 under Article 280 of the Constitution has had an unbroken legacy. It performs the functions broadly enshrined in the

Article 280 of the Constitution.

Basically, the President is expected every five years to constitute a Finance Commission with the purpose of advising on the distribution of the net proceeds of all taxes between the Union and States, and thereafter, its distribution among the States as well as the grants in aids.¹

For most of the post-independence era, the existence of the Planning Commission injected centralising dependence in more ways than one. The Planning Commission became an unconstitutional parallel institution for the transfer of resources from the Union of States. While focus of the Finance Commission remained on the revenue account, the Planning Commission was concerned predominantly with the

¹ Article 280 reads as:

(1) The President shall, within two years from the commencement of this Constitution and thereafter at the expiration of every fifth year or at such earlier time as the President considers necessary, by order constitute a Finance Commission which shall consist of a Chairman and four other members to be appointed by the President.

(2) It shall be the duty of the Commission to make recommendations to the President as to the distribution between the Union and the States of the net proceeds of taxes which are to be, or may be, divided between them under this Chapter and the allocation between the States of the respective shares of such proceeds; the principles which should govern the grants in aid of the revenues of the States out of the Consolidated Fund of India; any other matter referred to the Commission by the President in the interests of sound finance.

(3) The Commission shall determine their procedure and shall have such powers in the performance of their functions as Parliament may by law confer on them.

capital account. Successive Finance Commissions commented on this as being inconsistent with the spirit of the constitution in the devolution of resources. There were other developments like the 73rd and 74th amendments of the Constitution in 1992 giving status to Panchayat Raj institutions and Urban local bodies with specific functions assigned to them under the eleventh and twelfth schedules.

As a coordinating entity between the Centre and the States the two key institutions have remained, the National Development Council constituted in 1952 to oversee the work of the Planning Commission to approve their five year plans and their midterm appraisal and the formation of the Inter State Council by a Constitutional Amendment in 1990 based on the recommendations of the Sarkaria Commission Report.

Pre-Pandemic

So, what are the challenges to the Indian Federalism? These are pre-pandemic and have in an opaque way existed for long.

FIRST, the future of the VIIth Schedule. I need to dwell on this a bit. The VIIth Schedule of the Constitution broadly demarcates the functions of the governance into three entities. This schedule distributes the legislative and financial powers between the Union and the States. List I pertains to subjects of the Union, while List II pertains to subjects which belong to the States and List III in a category called the Concurrent List belongs to both the Union and the States and in the event of conflicting legislation, the law passed by the Union shall prevail.

Over a period of time the Concurrent List has sought to occupy increasing space. This is not only by the 42nd Amendment of the Constitution (1975), which shifted the subjects of forest and education from the State List to the Concurrent List. Furthermore in 1976, family planning was added to the

Concurrent List. This is the bedrock of the subsequent National Population Policy, which anecdotally is currently being debated in multiple forums. This transfer to the Concurrent subjects means the principal obligation in relation to issues of family planning are in the domain of both the Centre and the States except, as said earlier, any central legislation would override any laws made by the States.

While this was a formal act entirely through constitutional amendment there are other ways in which the original demarcation was sought to be whittled down and often metamorphasized. Take for instance the issue of Entitlement driven legislations. Some time ago we entered an era of Entitlement based Standalone Legislation. The classic examples are the Mahatma Gandhi National Rural Employment Guarantee Act of 2005, the Right of Children to Free and Compulsory Education Act 2009 and the National Food Security Act 2013. How do these stand-alone entitlement legislations mesh with the VIIth Schedule of the Constitution?

Do they transgress the earmarked borders? And how is it that none of the States, at any stage opposed the transgression of these limits. This was the area where the fiscal romantics should have really intervened as employment, education and food were entirely intended to be in the domain of the States. The issue of the States autonomy, I scarcely remember ever came up for serious analytical critiques. Political expediency pervaded Constitutional misgivings.

SECOND, the issue of incongruence of Article 282 of the Constitution with the letter and spirit of the VIIth Schedule. Article 282 of the Constitution which says, “The Union or a State may make any grants for any public purpose, notwithstanding that the purpose is not one with respect to which Parliament or the Legislature of the State, as the case may be, may make laws.”

Originally in the Constitution, it was not expected to be an overarching provision but an extra-ordinary one to be used

very sparingly and If I quote Shri K Santhanam, Chairman of the 2nd Finance Commission on Article 282, he said - *“This was not intended to be one of the major provisions for making readjustments between the Union and the States, if that was the idea, then there was no purpose in evolving such a complicated set of relations of shares, assignments and grants. There is no purpose in having two Articles enabling the Centre to assist the States - one through the Finance Commission and the other by more executive discretion. In the latter case, even parliamentary legislation is not needed. Of course, it will have to be included in the Budget. But, beyond being an item in the Budget, no further sanction needs to be taken. Therefore, in my view, this Article was a residuary, a reserve Article, to enable the Union to deal with unforeseen contingencies. That was how this Article was used both by the British Government and, after transfer of power, before the first year of the First Five Year Plan. Under this Article, only some grow-more-food grants and some rehabilitation grants were given.”*

N.A. Palkhivala, Constitutional expert, in his opinion given to 9th Finance Commission, opined - *“Art. 282 is not intended to enable the Union to make such grants as fall properly under Art. 275. Art. 282 embodies merely a residuary power which enables the Union or a State to make any grant for any purpose, irrespective of the question whether the purpose is one over which the grantor has legislative power.”*

THIRD, view this along with the changes in Part XII of the constitution which resulted in the adoption of GST designed to make India into one common market and entity. The GST Council which is also a constitutional body takes decisions through its fitment committee on the rates of the GST tax as both the Parliament and State legislatures have assigned their financial powers to this Empowered Committee. In the States that we have visited being part of Finance Commission, the States have often complained that their fiscal autonomy has been circumscribed by the GST and the room for manoeuvre on revenues had been greatly circumscribed. It is a case of pooled

sovereignty for the Betterment of Common Good. Nonetheless, GST Council is still in its nascent phase and needs to revisit its design and decision making process in a more fundamental way. The entire area of GST Reforms is an ongoing dynamic. In the Report of the 15th Finance Commission which was submitted, these reforms have been exclusively analyzed and are also necessary to enable it to fulfil its original purpose.

New challenges

I now come to the new challenges posed due to the pandemic.

It was inevitable that a global pandemic which emerged for the first time after independence, the constitution and the constitutional division of powers; this is an uncharted territory. The most fundamental lesson from India's experience with the second wave of the COVID-19 pandemic, is that managing a grave national crisis requires Federalism by way of Fiscal Fraternity of Centre and States.

The federal government must inevitably take the anchor's role.

Constitutional Play of Events

From a federal perspective, the Seventh Schedule of the Constitution which distributes the powers between different constituent units (Union and the States) gives states precedence over the Centre on health. Entry 81 of the Union List grants the legislative power for “inter-state migration; inter-state quarantine” to the Centre; meanwhile, Entries 1, 2 and 6 of the State List give the legislative field of “public order,” “police” and importantly “public health and sanitation; hospitals and dispensaries” to the states; but Entries 23 and 29 of the Concurrent List allocate the areas of “social security and social insurance; employment and unemployment” and “prevention of the extension from one state to another of infectious or contagious diseases or pests affecting men, animals or plants” to both the Centre and

States. There is a significant overlap and opacity in the demarcation of roles, functions and responsibilities.

The Constitution further states under Article 73 and 162 that the executive power of the Union and states is “coextensive with the legislative power”. Thus, from the constitutional scheme, the state governments are expected to play the primary role in the management of healthcare, as well as law and order, while the Centre is expected to provide the overarching national leadership, facilitate coordination among key federating units, monitor the overall pandemic situation, and provide financial and other critical assistance to the states.

As the crisis loomed large in India in early March 2020, the Centre and the States invoked two available legal instruments to deal with the crisis. The Centre declared the pandemic as a “notified disaster”, and cited the Disaster Management (DM) Act, 2005, in particular, to impose the nationwide

lockdown on 24 March 2020. *As the word “disaster” is not present in the Seventh Schedule, the Centre used its residuary powers to invoke the law and to issue various directives to the states as the pandemic situation aggravated.*

The states, for their part, turned to the Epidemic Diseases Act, 1897, which empowers the states to deal with an epidemic-like situation. Many state governments used this law to issue State Epidemic Diseases COVID-19, 2020 regulations for their jurisdictions, including restrictions on movement and closure of commercial establishments, offices, and other public places. Various sections of the Indian Penal Code, 1860 were used by the states as a guide for laying down punishments for violators, much before the Centre started to issue its own guidelines.

Key Dynamics of India’s Federal Response

The federal response to the pandemic has evolved in a number of ways. The following comments summarise the key responses, and the dynamics they involved.

First Wave is a play Between Central Unilateralism and State Autonomy

Constitutional provisions and existing legislations confer the primary responsibility for handling a situation like the COVID-19 pandemic, to the state government. Nonetheless, the Centre assumed the role of anchor and led from the front in managing the pandemic, particularly during the periods involving national lockdowns (24 March – 31 May 2020). As the pandemic threatened human lives and livelihoods, demanding swift action on a national scale, the Centre took over the many responsibilities which otherwise fall within the domain of the state. Among many comprehensive measures, the Centre took a series of decisions to scale up vaccine procurement, knowledge production for setting standards and guidelines for the state and local governments, and mitigation

of inter-state externalities.

Therefore, the pandemic invoked the wider powers of the Centre in full display, especially during the early phase: it was the Centre that imposed the lockdown, and it was also the Centre that monitored state responses including physical- distancing norms, regulation of economic activities, and provision of financial packages.

Second wave: Confederation

The first wave of the pandemic was about ‘unitary’ and understandably a centralised response by the Union. The opposite has been the case during the second wave. *Louise Tillin, a known scholar on federalism captures this trend succinctly when she says: “India has moved from unilateral centralized decision-making in the first wave to something that approximates unilateral decentralized decision-making—by default—in the second wave”.* For

one, the Centre during the first wave acted swiftly and decisively as federal governments ought to do during national emergencies.

The decentralisation logic became more visible in the case of the vaccination policy. As the country faced acute vaccine shortages many state governments called for autonomy to procure vaccines from international markets. The Centre acceded, as analysts found it impractical given the demand-supply mismatch and the competition for vaccines. Several states which went ahead with tenders for procuring vaccines found no prospective bidders. This, along with differential pricing of vaccines created an untenable situation. It soon became a contentious aspect of India's federal structure as the Centre and the states blamed each other for the confusion. It even required the intervention of the Supreme Court to end the Centre-state deadlock.

Clash between States

Apart from issues of Centre-State coordination, various State Governments ran into conflicts with other State Governments on the availability of oxygen, essential medicines and seeking to garner access and supply chains. The intervention of the Supreme Court in seeking to resolve this deadlock between the States was resorted to by several State Governments. In the end, order prevailed and the issue of vaccine procurement and supplies at the most optimum prices is in the domain of the Central Government as it should be. Equally, the interplay between international diplomacy, foreign policy, encouraging new vaccine supplies in orderly way is now the new approach which is being adopted for the ongoing pandemic. This would be equally applicable in case the pandemic lingers on or there is an emergence of another variant or what is loosely being called the third wave.

Launching the nationwide federal response, the Prime Minister on April 20 addressed the nation and appealed for Covid-appropriate behaviour; he also asked authorities to quickly ramp up responses.

The Way Forward

Ongoing Changes required- Even Pre-Pandemic

Firstly, The substantive point is re-look of the VIIth Schedule in a contemporary context. Unless we re-draw the contours of the schedule, some of the incongruities between the contours of the VIIth Schedule and Article 282 of the Constitution and the standalone legislation of the subjects primarily will remain cluttered and opaque.

Both in theory and practice, many beliefs and principles which prompted our forefathers to give the Constitution its present shape may need some basic reconsideration. Long before I said this in a report submitted in 1971 by a Committee called Rajamannar Committee formally known as the Centre–State relations Inquiry Committee, said “that it is desirable to constitute a High Powered Commission consisting of eminent

lawyers and jurists and elderly statesmen with administrative experience to examine the entries of List I and List III in the VIIth Schedule of the Constitution and suggest redistribution of entries”.

Second, the symmetry in the working of the GST Council and the Finance Commission deserves serious considerations. The Finance commissions recommend distribution of revenues between Union and the States and thereafter, among the States further to the third tier. They look at projections of the expenditure and revenue, but issue of GST rates exemptions, changes, and implementation of the indirect taxes are entirely within the domain of the GST Council. This leads to unsettled questions on the ways to monitor, scrutinise and optimise revenue outcomes. Since both the Finance Commission and the GST Council are constitutional bodies, the coordination mechanism between the two is now an inescapable necessity. For the first five years of the GST, a 14 per cent guaranteed compensation by the Goods and Services Tax (Compensation

to states act) 2017 is provided to the States. The fact that the GST Council is a permanent body while the Finance Ministry is not and makes awards for a five year or six year span further complicates the dynamics. The commonalities of issues and the absence of any recourse mechanism as a course correction is an aspect that many states highlighted to us.

Thirdly, with the abolition of the Planning Commission, many economists and policy makers have argued about an institutional vacuum. While the NDC is performing an important function, the States have pleaded for a credible institution acting as a link for a policy dialogue with the Centre. In many countries of the world like Australia, States came together in 2005 to set up the council for the Australian federation to jointly represent their interests in Canberra. We have an institutional entity and how to rejuvenate and rekindle Inter-State Council deserves serious consideration. In this institutional vacuum created, there needs to serious consideration on building entities by way of a permanent consultative mechanism.

Fourthly, reforms in Public Finance Management Systems are a continuous process. Previous Finance Commissions recommended on various aspects of PFM systems of both Union and States with focus on budgetary, accounting processes, and financial reporting.

Fifth, the Post Pandemic Changes Required

Reprioritisation of Expenditure to Critical Care and Needs.

In the light of the pandemic, the endemic neglect of the health infrastructure and the health sector as a whole needs redressal. This must be a high priority because we have become painfully aware that given the multiplicity of factors, this may not be the last pandemic. At a national level, the strengthening of the healthcare infrastructure based on the recommendations of the National Health Mission 2005 and the National Health Mission 2017, public outlays need to be substantially augmented. We cannot get away from strengthening district hospitals and

multispecialty care as also the availability of increased manpower, which should be available even in the normal course of our health programs. Apart from strengthening district hospitals, primary health centers at the block level also need substantial strengthening.

Many of these regulatory and other changes have been outlined in the Report of the 15th Finance Commission, which has devoted a special chapter on health. Among other things, these include a permanent national health service based on best international practices, other innovative changes like the DND courses or training of paramedics can have immediate multiplier effects. The National Rural Health Mission's recommendations and some notable examples of well-functioning decentralized health systems in some states would be worthy of replication. In this regard **Rs. 70,051 crore for urban HWCs, building-less sub centres, PHCs, CHCs, block level public health units, support for diagnostic**

infrastructure for the primary healthcare activities were recommended by 15th FC. These have been fully accepted and their implementation has commenced.

Sixth, Comprehensive National Legislation

In many ways, the pandemic has also exposed the inadequacies of the existing constitutional and legal provisions in dealing with a pandemic or a health emergency of pan-India dimensions. There are concerns about the vagueness of both the Disaster Management Act, 2005 and the Epidemic Diseases Act, 1897 in the context of a pandemic. While both these laws do not have provisions related to health emergencies, both Centre and States resorted to either expansive interpretation or ad-hoc measures such as issuing ordinances for instance to protect the frontline workers or ensure implementation of physical-distancing norms. This makes it imperative for the Federal government to initiate the drafting of a Comprehensive National Legislation that can effectively

deal with pandemics like the COVID-19, and other national emergencies that India could face in the future.

Seventh, More Democratic Decentralisation to the Third Tier

There are extraordinary stories of success by many states strengthening the role of their third tier during the pandemic. Illustratively, the Odisha government in delegating powers to the Sarpanch, in the protocols followed by the Mumbai Municipal Corporation in coordination with the Mumbai Police, and the role of local bodies in Kerala and indeed in other states as well.²

Eighth, FRBM Rules

² For instance, the Odisha government delegated the *sarpanch* with the powers of a magistrate to control the movement of migrants and oversee physical-distancing norms. Similarly, the Kerala government allowed local bodies to do contact-tracing, conduct health camps and sanitation drives, and sensitise people on health protocols. The local governments at the village level also helped “in sustaining agricultural activities by ensuring the labour supply and availability of critical food supply chains in villages.”

During the first wave, district-level interventions in Agra (Uttar Pradesh), Bhilwara (Rajasthan), and Pathanamthitta (Kerala) were exemplary in containing the spread of infections. Similarly, municipalities in states like Maharashtra where the COVID-19 cases have been steep, also made innovations in crisis management at different phases of the pandemic. Worth mentioning is the collaboration between the Brihan Mumbai Municipal Corporation (BMC) and the Mumbai Police to supervise quarantine procedures and create public awareness in the Dharavi slums; they succeeded in controlling the Covid situation in the area. The BMC repeated the feat during the second wave by quickly innovating in contact-tracing, testing, and expanding medical support by creating ‘ward-level war rooms’. In other words, decentralised responses bore fruits at the local level, wherever governments have delegated powers and trusted these self-governing institutions.

Aligning the Fiscal and Debt path of both the Centre and the States is an arduous but inescapable task. A differentiated Debt path of States which recognises the present constraints and issues of legacy debt must be handled with sagacity and sensitivity. This issue has been greatly aggravated during the Pandemic.

Many countries have amended their fiscal rules to provide for additional public spending to revive their economies that have been adversely affected by the Covid-19 pandemic. Fiscal rules provide a credible commitment to fiscal prudence. They set numerical limits on fiscal aggregates such as the level of fiscal deficit, public debt, or growth of public expenditure. A key feature of robust fiscal legislation is the 'escape clause'. Such a clause allows for temporary deviation from fiscal targets in the event of unforeseen circumstances. This is in accordance with a limited number of well-defined exceptional circumstances, time limits on how long fiscal policy can deviate from the targets specified in the rule, and a requirement for fiscal policy

to return to the specified targets after the escape clause is terminated.

Among the Asian, middle-income emerging peers of India, Indonesia's fiscal rule provides for limiting the fiscal deficit to 3% of GDP in any given year. Indonesia has since decided to suspend its fiscal deficit cap of 3% of GDP during 2020-2022.

In 2018, comprehensive amendments were introduced to the FRBM Act, 2003 to incorporate some of the recommendations of the FRBM Review Committee report chaired by me. Among other changes, the fiscal deficit target of 3% was proposed to be achieved by 31 March 2021. Another key feature of the amendment was to prescribe a relatively more nuanced escape clause. The statutory escape clause, as per the recommendations, allows the central government to deviate from the annual fiscal deficit target on grounds of national security, act of war, national calamity, collapse of agriculture severely affecting farm output and incomes,

structural reforms in the economy with unanticipated fiscal implications, or decline in real output growth of a quarter by at least 3 percentage points below its average of the previous four quarters. However, any deviation from the fiscal deficit target could not exceed 0.5% of the GDP in a year. The escape clause also mandates that a statement explaining the reasons for deviation and the path of return to fiscal deficit targets should be laid before both houses of parliament.

Even before the pandemic, the escape clause was invoked to informally deviate from the fiscal deficit targets. While presenting the budget for 2020-21, the finance minister used the escape clause to deviate from the fiscal deficit target of 3.3% for 2019-20. The escape clause was also used to deviate from the target for the next financial year, that is, 2020-21. Using the escape clause, the fiscal deficit was relaxed by 0.5% to 3.8% for the financial year ending 31 March 2020, and to 3.5% for the financial year ending 31 March 2021. The achievement of 3% of fiscal deficit target was shifted to 31 March 2023.

The Finance Minister while presenting the Budget Speech mentioned about the need to draw a fresh fiscal roadmap. This has become an inescapable necessity. Indeed, the FC has made a pointed suggestion for the constitution of an intergovernmental group—intergovernmental because it must have the Centre and States to evolve a more realistic fiscal roadmap given the ongoing pandemic and the uncertainties it entails. In the long run, no doubt, fiscal institutions like the Fiscal Council will be of enormous value.

Federalism to Unitary to Confederation

The first wave of the pandemic was about unilateralism and overtly centralised response by the Union. The opposite has been the case during the second wave which has been more of the form of **confederation**. A **confederation** (also known as a confederacy or league) is a union of sovereign groups or

states united for purposes of common action. Likewise, the relationship between the member states and the general government and the distribution of powers among them varies.

In the past few months, the country has witnessed an interesting and remarkably coordinated effort by the Centre and states in addressing a collective challenge. This exigency response will help us a great deal in understanding Centre-state relations as well as in improving mechanisms of federal governance.

The experience offers an opportunity to revisit the recent debate around the federal organisation of powers under the Constitution's Seventh Schedule. It has been argued that such organisation of powers is not cast in stone and the arrangement requires a review. Such an exercise is indeed necessary, but what should be its broad contours? The review should allow the carving out of the roles of the Centre and states to address hitherto disregarded and emerging concerns — a viral

pandemic or climate change, for instance.

Conclusion

Even prior to the pandemic, federalism in India had multiple challenges. Its fragility has been greatly compounded by the underfunded and neglected health system and weak state capacity. The spirit of cooperative federalism in a broader sense of the term has been an abiding theme of our federal polity. The most important lesson is one of flexibility—flexibility between unitary, federal and confederal. The evolving role of the central government as a principal anchor in extraordinary times like these is an inescapable national priority. The engagement of State government in not only implementation but in amelioration, containment, roll out and engagement with all stakeholders is a synergy without which our responses would not be optimum. Furthermore, going beyond centralization or decentralization, the engagement of the third tier of government to the initiatives to both the

Central and the State governments would enhance its reach, coverage and awareness, an important bulwark in times like these.

“Unity is vision; it must have been part of the process of learning to see.” – Henry Adams

“The significance which is in unity is an eternal wonder.” –
Rabindranath Tagore