Funding of Rural Local Bodies – polity

The Standing Committee on Rural Development and Panchayati Raj has flagged the "steady decline in the allocation of funds to Panchayati Raj Institutions" and urged the Centre to take "urgent steps" to ensure that adequate, untied, and performance-linked funds are allocated to rural local bodies.

Sources of Funds for Rural Local Bodies

1. Own Source Revenue (OSR)

Rural local bodies (RLBs) independently mobilize funds through tax revenues such as property tax, professional tax, vehicle tax, and advertisement tax. They also collect non-tax revenues, including user fees for water supply, sanitation, licensing, markets, and community assets. Additional receipts come from penalties, fines, and charges for use of panchayat facilities. OSR reflects the financial self-reliance of Panchayati Raj Institutions (PRIs), but currently forms only a very small fraction of their total funds.

2. Shared/Assigned Revenue

Higher-level governments (State or Central) collect certain taxes and assign a share to PRIs. Examples include cess and surcharges on land revenue, entertainment tax share, and royalties or lease proceeds from mining, quarrying, and social forestry activities. These revenues are typically fixed by state legislation or finance commission recommendations.

3. Central Finance Commission Grants

The Finance Commission of India recommends devolution of funds from the Union Government to local bodies. These include both *untied grants* (for general use) and *tied grants* (earmarked for specific purposes such as sanitation, drinking water, and infrastructure). Central grants form the majority share of Panchayat funding across India.

4. State Government Grants

State Finance Commissions (SFCs) recommend and state governments release grants-in-aid or devolved funds to PRIs. Allocation is usually based on parameters such as population, area, fiscal capacity, and development needs. These grants supplement central funds and are essential for bridging the gap between OSR and expenditure requirements.

Funds under Centrally Sponsored Schemes (CSS) and State Schemes

Panchayats act as implementing agencies for flagship rural development programs. Examples include MGNREGS, PMAY-G, Swachh Bharat Mission (Gramin), and National Rural Livelihood Mission (NRLM). These scheme funds are largely tied to specific projects and cannot be freely reallocated.

5. Special Grants

Special purpose grants under MP Local Area Development Scheme (MPLADS) and MLA/MLC Local Area Development Schemes. Backward Regions Grant Fund (BRGF) and other targeted programs for regional equity also channel funds through PRIs.

Issues Related to Funding of Rural Local Bodies

1. Decline in PRI Fund Allocation

The parliamentary committee has flagged a consistent reduction in overall allocation to PRIs, weakening fiscal decentralization. This hampers their constitutional responsibility to plan and implement local development programs effectively.

2. Governance & Transparency Concerns

The 2024 *Devolution to Panchayats in States Report* identifies poor conduct of social audits, low Gram Sabha participation, and inadequate financial disclosure as key barriers to transparency and citizen oversight.

3. Delay in State Finance Commission Constitution

Timely constitution of SFCs is critical for regular devolution of funds.
As of the latest report, only 25 states have set up SFCs, and just 9 have constituted the 6th SFC. States like Punjab and Tamil Nadu have strong compliance, while others (e.g., Arunachal Pradesh, Chhattisgarh, Gujarat, Jharkhand, Telangana) lag in submitting Action Taken Reports (ATRs), delaying fund flows.

4. Inability to Address Local Needs

Reduction in untied and flexible scheme transfers constrains PRIs' ability to address region-specific development priorities. Inconsistent transfer of the 29 subjects listed in the 11th Schedule—due to states' reluctance to cede control—further reduces Panchayats' functional autonomy.

5. Institutional Flaws

Frequent rotation of reserved seats for SCs, STs, and women disrupts leadership continuity, affecting long-term planning. District Planning Committees (DPCs) are often non-functional or weak, leading to poor integration of village, block, and district plans. Elected representatives often lack adequate training in financial management, governance, and participatory planning.

Status of PRI Funding (2024 Report)

1. Revenue Composition

PRIs raise only around 1% of their total revenue from taxes, showing extremely low self-reliance. Approximately 95% of revenues are sourced from central and state grants.

2. Revenue Per Panchayat

1. Average revenue from own taxes: ₹21,000 per Panchayat.
2. Non-tax receipts: ₹73,000 per Panchayat.
3. Central grants: ₹17 lakh per Panchayat (average).
4. State grants: ₹3.25 lakh per Panchayat (average).

3. Low Revenue Expenditure

Ratio of Panchayat revenue expenditure to nominal GSDP is below 0.6% for all states—ranging from just 0.001% in Bihar to 0.56% in Odisha.

4. Inter-State Disparities

High revenue states, Kerala (₹60 lakh+ per Panchayat) and West Bengal (₹57 lakh+). Low revenue states, Andhra Pradesh and Punjab (less than ₹6 lakh per Panchayat).

Steps Needed to Improve Funding of Rural Local Bodies

1. Performance-Linked Resources

Allocate sufficient untied funds linked to performance benchmarks, ensuring both flexibility and accountability. Strengthen Panchayats' OSR through effective tax base expansion, better collection mechanisms, and state support for enforcement.

2. Addressing Fund Allocation Decline

Ministry of Panchayati Raj, Ministry of Finance, and Finance Commission must coordinate to restore consistent and adequate allocations. Emphasis on predictable, formula-based transfers instead of ad-hoc grants.

3. Strengthening State Finance Commissions

All states must constitute SFCs regularly, adhere to report timelines, and fully implement recommendations. Regular ATR submission should be made a pre-condition for central grant release.

4. Ensuring Transparency

Prevent diversion of PRI funds by establishing statutory safeguards. Enhance fiscal transfer transparency via public disclosure portals, regular audits, and RTI compliance.

5. Improving Digital Infrastructure

Panchayats should be equipped as digital governance hubs to improve citizen access to schemes and service delivery. Use of e-Gram Swaraj and similar platforms should be expanded for budgeting, accounting, and real-time monitoring.

Conclusion

Strengthening the fiscal capacity of PRIs requires a multi-pronged approach—enhancing OSR, ensuring predictable and adequate intergovernmental transfers, improving SFC compliance, and promoting transparency and accountability through digital governance. This will enable PRIs to deliver on their constitutional mandate, address local priorities effectively, and contribute to sustainable rural development.

Source: https://indianexpress.com/article/india/parliamentary-panel-flags-decline-funding-rural-local-bodies-centre-act-10156854/