

Local Government Finance: A Review of Fiscal Decentralisation in India

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Abstract- Local governments in India are an integral part of the governance structure. The provision of public goods and services is entrusted with the local bodies due to their superior knowledge of specific public needs and regional requirements. Various functions and responsibilities have been devolved to local governments through 73rd and 74th Constitutional Amendment Acts of 1992 to catalyse the development process. This paper aims to analyse and review the process of fiscal decentralisation. Various researches and empirical studies have been reviewed to develop insight into the effectiveness of fiscal decentralisation in augmenting local governments' finance and ensuring efficient service delivery. The major themes that emerge from extant literature suggest that for vast countries like India, fiscal decentralisation does not significantly contribute to economic growth. The decentralisation policies have both positive and negative implications, on the positive side, decentralisation improves performance and service delivery, while on the negative side, it increases fiscal imbalance. To utilise fiscal decentralisation as a catalyst of development, there is a strong need to enhance the resources base of local self-governing institutions along with ensuring accountability and adequate observations by higher tiers of government. Local governments need to adopt innovative financing mechanism to fill the resource gap and reduce their reliance on fiscal transfers.

Keywords: fiscal empowerment, local bodies, public service delivery, fiscal discipline.

1. INTRODUCTION

In past several decades, economies both developed and developing have gone through significant structural changes in governance to improve their functioning and promote efficient public service delivery for development purposes. Dissatisfaction from previous centralized structure of service delivery, promotion from state controlled to market economy, realization of the need for economic, social and political diversification have been prominent causes for the phenomena (M. Govinda Rao, 2011). Such restructuring is expected to achieve various goals like efficiency in resource allocation, improved governance and administration, economic growth stimulation, poverty reduction, gender balance, and empowerment of weaker sections (M. Govinda Rao, 2000). One of the main components of restructuring have been the devolution of decision-making powers from central to sub-national governments which may include both fiscal and political decision-making powers (Vazquez, 2011). The process of devolution of powers from centre to sub-national and from sub-national to local bodies is given many names in economics like 'decentralization' and 'de-concentration'. De-concentration refers to when central government only decentralizes its operations to sub-national governments and does not provide decision making power, on the other hand, decentralization encompasses political, administrative, and fiscal dimensions (Vazquez, 2016).

Fiscal decentralization means the transfer of revenue and expenditure authority from national to sub-national governments. This transfer is concerned with four main interactions of fiscal nature that take place among government hierarchy, namely (i) decisions of expenditure; (ii) tax and revenue-generation powers; (iii) sub-national borrowings and (iv) intergovernmental fiscal transfers (Duc Hong Vo, 2010). The fiscal decentralization theory makes its base from the works of Tiebout (1956), Musgrave (1959), Oates (1972), Olson (1969) and others. In the extant literature on fiscal decentralization, it has been defined as democratization among the levels of government where local governments are established through democratic process and are granted powers of generating their own revenues and incur expenditures accordingly.

Various studies have shown both positive and negative aspects of fiscal decentralization in developing nations, extant literature on fiscal decentralization provides several noteworthy features, most significant of them is the lack of data essential to perform an evaluation of effectiveness of fiscal decentralization policy (Singh, 2020), the concern of availability and quality of data has constrained academicians and researchers from deriving accurate measures and definitions of fiscal decentralization (Bahl and Vazquez, 2022). Besides data, another issue is the lack of micro level studies that are citizen centric and portray accurately the situation of end consumer. The empowerment of local bodies

must be done with the intent to empower local population (Bahl and Bird, 2018), and for that matter rigorous research is required that focuses on finding ways to develop local populations and improve situations from below. This paper attempts to study the decentralization of fiscal as well as administrative responsibilities and functions in India in order to draw conclusions on effectiveness and issues of fiscal decentralization in the country.

2. REVIEW OF LITERATURE

2.1. THEORETICAL FRAMEWORK

The early theories of public finance mention the roles of national and sub-national governments in public expenditure and revenue activities. Local governments have been given attention in early public finance theories, though main emphasis was on central government's role. Wagner (1880) gave the law of increasing state activity where he mentions three points, (i) continuous increase in central and local government activities, (ii) both levels of government perform new functions and old functions more efficiently, (iii) expansion in government functions increases public expenditure. Musgrave (1959) introduced the 'Three function framework' suggesting three main functions or branches of state activity, (i) stabilization, (ii) redistribution, and (iii) resource allocation. Peacock and Wiseman (1961) mentioned three effects in their theory, (i) displacement effect, (ii) inspection effect, and (iii) concentration effect, where concentration effect separates the functions of central and local government by suggesting that central government's activities grow faster than that of state and local government's activities.

However, the fiscal decentralization theory became the centre of academic attention after the emergence of "Decentralization Theorem" by Oates (1972). In relation to the Musgrave's allocation function, Oates (1972) argued that sub-national or local governments are best suited for the provision of public goods and services given their proximity to the public and better information of specific needs. Fiscal decentralization theory has been rectified, improved and broadened through numerous studies attempting to find out positive as well as negative implications of decentralization for economic growth. Those who found support for fiscal decentralization suggest, it results in increased efficiency, better resource allocation and accountability (Bahl, 1999), fiscal decentralization prevents central government from becoming profit maximiser because of the competition among levels of government (Brennan and Buchanan, 1980). Studies finding negative aspects about fiscal decentralization assert that the stabilization function is best performed by the central government because if there is high disparity in capacities of sub-national governments, stability is compromised (Paul Smoke, 2001). Another popular view on negative impact of fiscal decentralization is that main revenue sources for local government are income inelastic and they cannot increase their revenues with the rise in income levels (Richard M. Bird, 2006). Though, as divided the fiscal decentralization literature may be, it has some serious insights on the working of governmental hierarchy and suggests efficient ways to improve service delivery in economies.

2.2 RECENT DEVELOPMENTS IN THE LITERATURE

Sankalpa Bhattacharjee et al. (2024) studied the impact of fiscal decentralisation policies on health and educational service delivery components among 18 non-special category states in India, they conclude that the policy of decentralisation as an instrument to augment public service delivery is effective.

Sovik Mukherjee (2023) in his India-China comparative study, analysed the data for the period 2006-2019 to find out whether fiscal decentralization policies reduce poverty and inequality and found out that decentralization of fiscal functions and powers helped reduce poverty but there was an increase in income inequality.

Rahul Pathak (2023) studied the impact of subnational fiscal rules (local governments are not allowed to have fiscal deficits) on public investment and asserted that reduced expenditure on development and capital projects to meet fiscal targets can be counterproductive because such expenditure has positive externalities.

Ahmad Fadhil Imran, et. al. (2023) in their study on potential moral hazards in fiscal decentralization found that apart from the moral hazard problem that can occur any time, fiscal decentralization has the potential to be a solution for economic inequality.

Teboho Mosikari and Sanele Stungwa (2023) used panel data for the period of 2010-2019 in their study to find out a relationship between fiscal decentralization and economic growth in South Africa, their findings imply that for efficient provision of public goods and services, the government needs to fully adopt fiscal decentralization policy.

Nupur Nirola et. al. (2022) studied fiscal decentralization and regional disparity issues in India, their findings suggest that in order to harness the potential benefits of decentralization to reduce regional income disparities, governments should focus on improving the quality of institutions through control on corruption at the sub-national level.

Shyam Nath and Yeti Nisha Madhu (2022) used the data from Municipal corporations of Delhi and Mumbai to study what happens to fiscal efforts of local bodies when they get regular grants and state expenditure rises more than their own expenditure. Their study revealed that increasing expenditure from the states dampens the local expenditure and service provision at the local level is adversely affected.

Gajjela Pradeep Shravan (2022) studied the functions, responsibilities and resources of rural local bodies and found that along with income reforms, expenditure reforms and vitalised service delivery are also equally significant. Transfers from commissions and fiscal decentralization is also significant.

Archana Jain and Archana Singh (2022) studied municipal finances of Meerut Municipal Corporation and concluded that under fiscal decentralization, local bodies must generate additional sources of income like municipal bonds and market securities rather than relying mainly on state fiscal transfers.

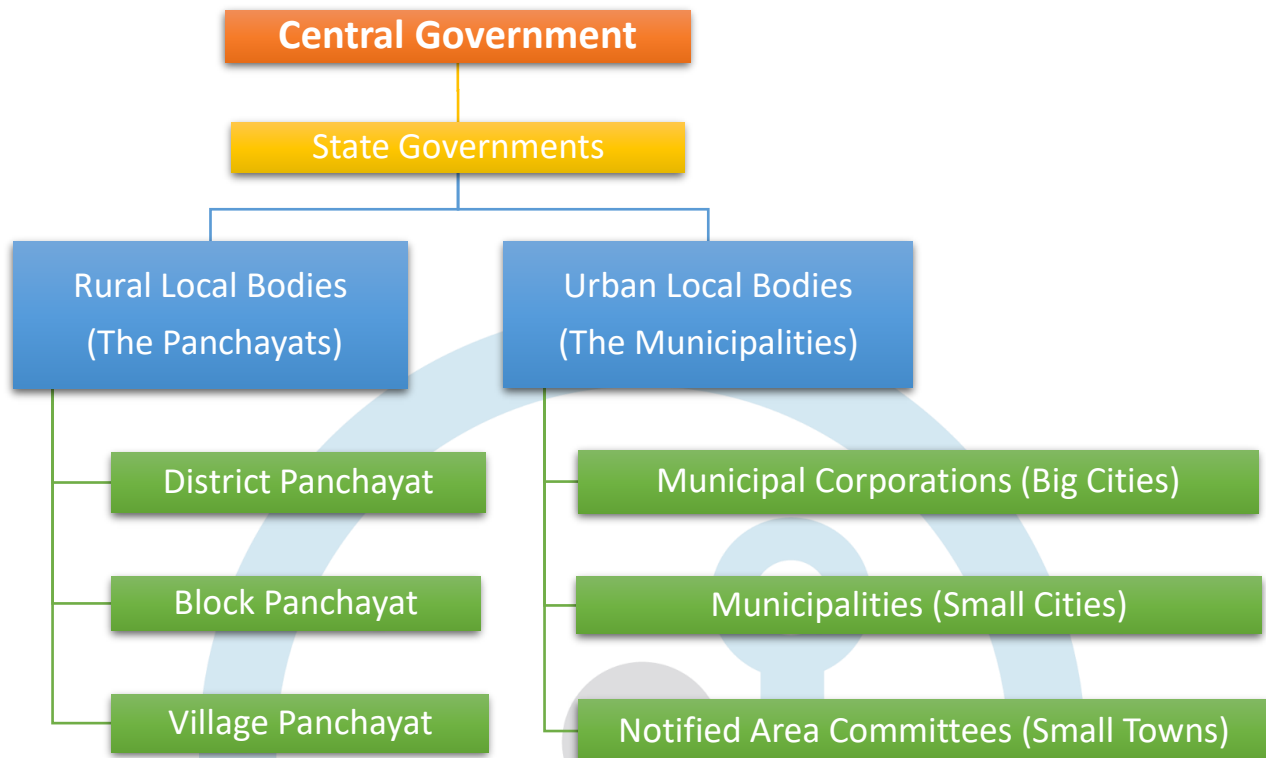
U B Singh (2020) performed a comprehensive analysis on mobilisation of financial resources in **Lucknow Municipal Corporation** and concluded that the corporation has enough funds and sources of funds, better financial management is needed to maintain fiscal discipline and it is possible through decentralization which provides responsibility and transparency.

OBJECTIVES AND METHODOLOGY

The purpose of this paper is to develop insights on how fiscal decentralization has contributed to the structural transformation of country's governance and what is the current scenario of local government revenue sources along with their responsibilities and functions. The paper also aims to find out positive as well as negative implications of fiscal decentralisation for contemporary India. Methodology in research refers to the system of models, techniques and procedures followed to find solution to the research problem (Panneerselvam, 2014), and research design is the orchestration of conditions under which data is collected and analysed in order to maintain relevance to the purpose of research (Kothari, 2004). In this paper, we make use of secondary data from various sources like Reserve Bank of India database, reports of Comptroller and Auditor General of India, Indian public finance statistics, Ministry of Panchayati Raj – Local Government Directory and other relevant researches, reports, journals and studies. The paper adopts exploratory research methods to increase our understanding of the fiscal decentralisation theory and its implications for the holistic growth of the nation.

FISCAL DECENTRALIZATION IN INDIA

Fiscal decentralization in India dates back to the pre-independence era, when Lord Mayo who served as the 4th viceroy of India from 1869 to 1872, introduced a resolution in 1870 providing the local governments with the power to balance their budget through taxation, it was a legislative devolution inaugurated by the Indian Councils Act 1861. Lord Mayo also ordered first census in India in the year 1871. However, a major step towards fiscal decentralization was taken post-independence in the year 1992 with 73rd and 74th Constitutional Amendment Acts, which envisaged the devolution of functions, fiscal responsibilities and powers to local self-governments, where state governments were made compulsory to form local self-governments at both rural and urban levels, thereby granting them constitutional status. Before 1992, India was a traditional two-tier federal structure with central government at the top and state governments as sub-national governments sharing functions and powers (M. Govinda Rao, 2001). The 73rd Constitutional Amendment deals with rural self-governments by providing a three-tier structure titled “The Panchayats” which are – District Panchayat, Block Panchayat and Village Panchayat, while the 74th Constitutional Amendment deals with urban self-governments titled “The Municipalities” which are – Municipal Corporations, Municipalities and Notified Area Councils or Town Councils. The decentralised structure of governance in India after the Constitutional Amendments of 1992 is shown in **Figure 1**. The constitutional amendments provided local governments a place in Indian Constitution, and made them 3rd tier of government in India. However, the states were endowed with the authority to allocate functions and powers to local governments. It was made mandatory for the states to empower both rural and urban local governments with fiscal responsibilities and authorities (Meenakshi, 2022). These local governments have the authority to raise finance from various sources in order to provide civic amenities to the population living within their respective jurisdictions, however, in India, local governments are almost entirely dependent on higher tiers of government to meet their expenditure requirements.

Figure 1. Structure of Governance in India

Source: Author's representation

Appropriate powers and responsibilities have been provided to local governments by their respective states through legislation. Such devolution has been brought in India by taking lessons from other developing and developed countries. Decentralization is thought to improve economic conditions by bringing efficiency in provision of public goods and better administration at all levels. Fiscal decentralization is though vulnerable to economic inequalities due to varying fiscal capacities of local governments and specific needs in different areas of a country, therefore, in decentralized fiscal system, provisions are made so that higher levels of government such as central and/or state may provide grants and aids to these local governments (Jha, 2013). Numerous attempts have been made to assess the role of fiscal decentralization in developing countries such as India, studies like Bird and Vaillancourt (1997), Meenakshi (2022), Bhattacharjee et al. (2024), Rao et. al. (2011), Yinghua Jin and Mark Rider (2020) have provided significant insights on the importance of fiscal decentralization and issues to be addressed for countries like India. Fiscal decentralization has played a pivotal role in economic growth of countries due to its merits of providing fiscal autonomy to local governments, maintain efficient provision of local public goods and services to best suit the needs of society (Oates, 2006). However, good governance is required to unleash the potential of fiscal decentralization in large countries like India, because the effects of fiscal decentralization can be positive if there exists an efficient governance at all levels (Ryota Nakatani, et. Al., 2022). Several state specific studies have shown mixed results regarding the impacts of fiscal decentralization on economic development in developing countries, especially in India where a considerably large number of local governments operate.

Table – 1. Number of Sub-National and Local

Name	Total
1. No. of States/Union Territories (UTs)	36
2. No. of Districts	785
3. No. of Sub-Districts	7129
4. No. of Development Blocks	7256
5. No. of Villages	664494
a) No. of Inhabited Village	648509
b) No. of Un-inhabited Villages	15216

c)	No. of Forest Villages	769
d)	No. of Villages (Rural)	640742
e)	No. of Villages (Urban)	13703
6.	No. of Rural Local Bodies	262595
a)	No. of District Panchayats	665
b)	No. of Block Panchayats	6706
c)	No. of Gram Panchayats	255224
7.	No. of Traditional Local Bodies	16151
a)	No. of District Level Councils	14
b)	No. of Intermediate Level Councils	2288
c)	No. of Village Level Councils	13849
8.	No. of Urban Local Bodies	4867
a)	No. of Municipal Corporations	254
b)	No. of Municipalities	1877
c)	No. of Town Panchayats	2405
9.	No. of Cantonment Boards	59
10.	No. of Parliament Constituencies	543
11.	No. of Assembly Constituencies	4120

Source – Ministry of Panchayati Raj, Local Government Directory (2023).

There are a total of 262595 Rural Local Bodies, 16151 Traditional Local Bodies and 4867 Urban Local Bodies in India as shown in **Table 1**. Decentralization of financial responsibilities and authorities to lower tiers of government is a significant challenge in countries like India due to a vast population and large number of local governments. Such reluctance in devolution of authorities can also be political because state governments feel the need to exert control on their lower government levels in order to maintain balance, also local governments in India are susceptible to the influence of local elite class (Bardhan, 2006; Asha, 2023). A large disparity is seen in terms of decentralisation among states in India (Kalirajan & Otsuka, 2012) which is a major reason of the lack in uniform development of local bodies in different states.

Table 2. State wise number of Local Bodies

S.No.	State/UT Name	Districts	Sub-districts	Villages	Village Panchayat	Urban Bodies
1	Andaman and Nicobar Islands	3	9	560	70	1
2	Andhra Pradesh	26	679	17950	13325	123
3	Arunachal Pradesh	25	209	5485	2108	35
4	Assam	35	157	27959	2197	114
5	Bihar	38	534	45410	8054	270
6	Chandigarh	1	1	0	N.A	1
7	Chhattisgarh	33	249	20374	11654	170
8	Delhi	11	33	222	N.A	4
9	Goa	2	12	429	191	14

10	Gujarat	33	270	19039	14621	166
11	Haryana	22	143	7596	6225	88
12	Himachal Pradesh	12	190	21253	3615	61
13	Jammu and Kashmir	20	208	6857	4291	78
14	Jharkhand	24	264	32737	4345	55
15	Karnataka	31	236	30715	5953	316
16	Kerala	14	78	1666	941	93
17	Ladakh	2	15	248	193	2
18	Lakshadweep	1	10	27	10	N.A
19	Madhya Pradesh	55	424	55882	23011	413
20	Maharashtra	36	358	44620	27906	410
21	Manipur	16	65	3856	161	27
22	Meghalaya	12	54	7098	N.A	11
23	Mizoram	11	28	875	N.A	23
24	Nagaland	16	120	1644	N.A	39
25	Odisha	30	476	52245	6794	115
26	Puducherry	4	8	127	108	5
27	Punjab	23	96	12784	13241	166
28	Rajasthan	50	426	46958	11254	240
29	Sikkim	6	18	483	199	7
30	Tamil Nadu	38	313	18696	12525	647
31	Telangana	33	594	11226	12769	142
32	Dadra and Nagar Haveli and Daman & Diu	3	3	101	38	3
33	Tripura	8	23	898	589	27
34	Uttar Pradesh	75	351	110143	57702	770
35	Uttarakhand	13	129	17325	7795	103
36	West Bengal	23	346	41006	3339	128
	Total	785	7129	664494	255224	4867

Source – Ministry of Panchayati Raj, Local Government Directory (2023).

Functions and Responsibilities of Local Bodies

As discuss in earlier section of the paper, the 73rd and 74th Constitutional Amendment Acts paved the way for strengthening local governance in India by providing illustrative lists of functions and responsibilities that state

governments need to devolve partially or fully to local bodies through appropriate legislature. The Amendments also entrusted the Finance Commission to review local bodies' finances and recommend principles for devolution of funds. These local government institutions also have their own sources of funds to meet their expenditure requirements. Rural Local Bodies in India rely mainly on devolution from higher levels of government to meet their expenditures of service delivery and functioning, the own sources of revenue of Panchayati Raj Institutions (RLBs) form almost no part of their funds

Sources of Revenue for Rural Local Bodies–

i) Revenue from the Central Government: The Central Finance Commission recommends the central government to provide grants and other aids to local bodies.

ii) Revenue from the State Government: Rural Local Bodies also get a share of revenue from respective state governments, such revenues are of two types:

a) Revenue allocations that are recommended by the State Finance Commission;

b) Scheme specific grants.

iii) Internal resources of Revenue: Rural Local Bodies in different states use various mechanisms for revenue generation. Two important sources are

a) Income from taxes.

b) Non-tax income, etc.

Expenditure Responsibilities and Functions of Rural Local Bodies–

Functional devolution to Rural Local Bodies (3 tier Panchayati Raj institutions) has been categorised on the basis of “Compulsory and Discretionary functions” as follows:

i) Compulsory functions:

- To provide health facilities by establishing health centres and dispensaries.
- Ensure the welfare of weaker sections.
- Construction and maintenance of roads, wells, ponds etc.
- Supply clean drinking water.
- Cleanliness and sanitation.
- Provision of primary education.

ii) Discretionary functions:

- Organisation of village markets and fairs.
- Construct playgrounds and rest houses (Baraat Ghar).
- Organise awareness programmes.

Sources of Revenue for Urban Local Bodies–

74th Amendment Act specifies following sources of revenue for Urban Local Bodies or Municipalities-

i) Own Source Revenue:

a) Tax revenue: Taxes are a major source of revenue for ULBs, they levy taxes such as – sewage management tax, water tax, etc. Municipal taxes are of two types-

Compulsory taxes such as tax on house, tax on water etc.

Discretionary taxes such as tax on businesses, growth etc.

b) Non-tax revenue: Besides the revenue generated from taxable sources, the municipalities in India also generate income from other sources like Water charges, duty on slaughterhouse, licensing fee, punishment, municipal properties, additional stamp duties, towers on houses, etc.

ii) External revenue sources:

a) Grants-in-Aid: ULBs in the country get grants from their respective state governments, these grants differ from state to state according to the State finance commissions. Central Finance Commission also recommends the central government to provide grants to ULBs.

b) Loans/Bonds: ULBs are also entitled to borrow from state governments depending on the respective Municipal Acts of different states. Larger ULBs such as Municipal Corporations have also started the initiative to issue municipal bonds in order to strengthen their revenue base.

Expenditure Responsibilities and Functions of Urban Local Bodies in Uttar Pradesh –

The 74th Amendment Act has laid down a list of 18 broad functions to be devolved to Urban Local Bodies in order to decentralize powers and functions, however, state governments have the authority to devolve all or some of these functions either fully or partially, majority of the states have not devolved all 18 functions, there are still functions that are shared between ULBs and various government agencies. The functions mentioned in the 12th Schedule of 74th CAA are-

1. Town and urban planning are included.
2. Control over building construction and land use.
3. Making plans for social and economic advancement.

4. Roads and bridges.
5. Water supply for commercial, industrial, and domestic use.
6. Solid waste management, sanitation conservation, and public health.
7. Fire services.
8. Urban forestry, environmental preservation, and ecological elements promotion.
9. Protecting the interests of the weaker sections of society, such as the mentally ill and disabled.
10. Slum modernization and enhancement.
11. Reducing urban poverty.
12. Providing urban services and amenities including playgrounds, gardens, and parks.
13. The advancement of artistic, educational, and cultural facets.
14. Burials; cemeteries; cremations; electric crematoriums.
15. Cattle pounds; preventing cruelty to animals.
16. Vital statistics, such as birth and death registration.
17. Public facilities such as parking lots, bus stations, street lighting, and restrooms.
18. Control over tanneries and slaughterhouses.

Positive Implications of Fiscal Decentralisation for India-

As challenging as it may be to implement decentralised policies in complex structure of Indian federation, it can yield fruitful results for a holistic development of the country. The influence of fiscal decentralisation on governance, resource allocation, and development outcomes in India has been thoroughly examined, as evidenced by empirical studies. Research, like that done by Aadil Ahmad et al. (2018), highlights the favourable relationship between enhanced economic growth and fiscal decentralisation, especially when it comes to sub-national governments' revenue decentralization. This is consistent with other similar studies and empirical evidences that suggest devolution of financial powers such as revenue and expenditure authorities to levels of government can increase the efficiency of service delivery and promote economic development in India (A. Asfaw et al., 2007; Agarwal, 2019; de Xavier, 2021; Mishra, 2023), which emphasises the ability of fiscal decentralisation to address local needs and imbalances in different regions of the country. Additionally, the work of Jin & Rider (2022) emphasises the importance of a fiscal devolution for countries like China and India. Through an extensive analysis of the available literature and reviewing the major impacts fiscal decentralisation had on the Indian economy after the reforms of 1990s, we can broadly summarise its positive implications.

(i) Public Service Delivery and Accountability

Delivering basic amenities such as infrastructure, roads, housing, health, education, sanitation etc. can be more effective if it is performed by local governments that are closer to the public and have superior knowledge of the needs in their locality (Oates, 1972; Rao, 2000). The argument is further reinforced by the fact that public goods have distinct characteristics in different geographical locations and the local governments have better knowledge in this regard. Oates (1999) also argues that delivering public goods according to local preferences can attain higher degree of social welfare because preferences for public goods vary among regions and this way, individuals can move to the regions that best fits their needs. Fiscal decentralisation has also shown evidences of increased accountability among local governments, it is because local bodies are subject to closer scrutiny within their constituencies. Provisions have been made under the FD policy to mandate local governments to prepare budgets, accounts, balance sheets, etc. and such accounts are also audited. Another reason for increased accountability is that individuals are closer to the officials and can ask direct questions.

(ii) Productivity and Competition

Under decentralised governance structure, the local governments are responsible for the welfare of the population under their jurisdictions, every local level government constantly tries to outperform other governments which creates a healthy competitive environment and enhances productivity. The government units under decentralised structure function within a country-wide unified market system, which provides the uninterrupted flow of factors and products among the localities which ensures suitable environment for market economy (Kalirajan and Otsuka, 2012). Fiscal decentralisation also encourages competition among local governments to attract investment, business, skilled labour, which leads to improvement in economic performance and growth. Under decentralisation policies, the local governments are also allocated funds based on performance and other aspects, this encourages the authorities to compete among themselves in terms of performance to attract more grants and fiscal transfers from the higher levels of government.

Fiscal Decentralisation in India: major challenges-

Fiscal decentralisation can be successful if there is adequate devolution of financial authorities and responsibilities along with adequate devolution of funds to the local governments because majority of the local authorities in India lack the

resources to generate funds on their own (Rao, 2011). Various empirical researches have shown that revenue decentralisation is negatively associated with economic growth while expenditure decentralisation has a strong positive association (Ganaie et al, 2018; Pasichnyi et al, 2019; Faridi et al, 2019) which poses numerous challenges to decentralisation in India. The major challenges of fiscal decentralisation are summarised below-

(i) Assignment of Functions and Responsibilities

It is often unclear how the central government, state governments, and local governments are supposed to distribute duties and obligations. Overlapping responsibilities, inefficiencies, and subpar service delivery result from this lack of clarity. Furthermore, capacity and resource restrictions frequently make it difficult for local governments to carry out their allocated responsibilities in an efficient manner (Rao, 2000).

(ii) Intergovernmental Transfers and Equity

One of the most important aspects of fiscal decentralisation is the system of intergovernmental transfers, which includes grants and allocations (Rao, 2000). These transfers, meanwhile, may not fully address the disparate requirements of various regions and may even be unfair. It is still difficult to guarantee an equitable allocation of resources while encouraging fiscal discipline (Rao, 2001).

(iii) Local Revenue Mobilisation

Local governments' financial independence is restricted by their heavy reliance on transfers from higher levels of government. Effective decentralisation requires the ability to generate income locally through taxes, fees, and other means. Local income mobilisation is hampered by outdated revenue-generating methods, inadequate administrative capabilities, and small local tax bases (Mukhopadhyay, 2023).

(iv) Accountability and Governance

The goal of fiscal decentralisation is to enhance local government and service delivery. However, ensuring transparency and accountability in local financial management remains challenging for the higher governments (Bhadra and Banerjee, 2020). To solve this dilemma, it is imperative to strengthen local institutions, augment citizen engagement, and foster efficient oversight systems.

(v) Political Will and Administrative Capacity

Strong political will and administrative ability are necessary for the implementation of fiscal decentralisation (Rao, 2001). Although local bodies are acknowledged as the third tier of government by constitutional provisions, their real empowerment and resource distribution frequently fall short. Ongoing challenges include strengthening administrative capacities, encouraging budgetary restraint, and cultivating collaboration among all levels of government.

Conclusion

Fiscal Decentralisation is considered the fiscal empowerment of the lower tiers of government, it is one of the most significant elements of decentralisation policies. The 73rd and 74th Constitutional Amendment Acts of 1992 have been major steps towards decentralising financial as well as service delivery functions to the lower tiers of government in India. The proximity of local governments to the population proves to be an advantage in providing services that are best suited for various regions. A comprehensive review of the extant literature on fiscal decentralisation and local government finances performed in the paper reveals that there are mixed results of fiscal decentralisation policy in India, on one hand, it improves service delivery, performance of local governments and economic growth of the regions, but on the other hand, there are numerous challenges like inadequate own resources, lack of accountability, fiscal imbalance etc. In a vast country like India, complete decentralisation is subject to various issues and challenges. Therefore, the need to decentralise expenditure responsibilities more than revenue authorities arises, the higher levels of governments must ensure the adequate transfer of resources to the local bodies in order to meet the expenditure requirements while maintaining careful observation. The resource bases of the local governments also need to be augmented to support a larger proportion of the expenditure through their own sources. Innovative financing vehicles such as municipal bonds, market borrowings, investments etc must be adopted to increase own sourced revenue. It is also evident that an overall impact of fiscal decentralisation including both revenue and expenditure decentralisation is positive on economic growth, therefore, it is essential to address the challenges associated with fiscal decentralisation policy to draw maximum benefits.

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Conflict of Interest

The authors declare no conflict of interest.

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