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ANALYSIS**

TOPIC

**MUNICIPAL FISCAL REFORMS
CRUCIAL FOR ADDRESSING URBAN
GOVERNANCE CHALLENGES**

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MUNICIPAL FISCAL REFORMS CRUCIAL FOR ADDRESSING URBAN GOVERNANCE CHALLENGES

Context

- Recently, the Reserve Bank of India (RBI) released a comprehensive report on municipal finances that emphasizes the growing demand for high-quality public services in urban areas, driven by rapid urbanization.
 - ♦ Despite this, municipal corporations (MCs) in India generate limited revenues and rely heavily on upper tiers of government for funding, limiting their operational flexibility.

Municipal Corporations (MCs) and Other Urban Local Bodies (ULBs)

- The **74th Constitution Amendment Act 1992** introduced **Part IX-A to the Constitution**, which provided a constitutional basis for the **establishment and functioning** of MCs and other ULBs.

Objectives

- Decentralize Powers;
- Enhance Financial Autonomy;
- Ensure Regular Elections;
- Promote Inclusive Governance;

Benefits of Robust Municipal Corporations (MCs) in India

- **Enhanced Public Services** such as clean drinking water, sanitation, waste management, and public health facilities.
 - ♦ It leads to improved living standards and better quality of life for urban residents.
- **Efficient Infrastructure Development** including roads, bridges, public transportation, and parks.
 - ♦ Efficient infrastructure development enhances connectivity, reduces traffic congestion, and promotes sustainable urban growth.
- **Economic Growth and Job Creation:** By creating a conducive environment for businesses and industries, robust MCs contribute to economic growth and job creation.
 - ♦ Well-maintained infrastructure and efficient public services attract investments and foster entrepreneurship, leading to increased employment opportunities.
- **Environmental Sustainability** through initiatives such as waste management, pollution control, and green spaces.
 - ♦ These efforts help in reducing the environmental impact of urbanization and improving the overall quality of the urban environment.
- **Democratic Governance** by providing a platform for citizen participation in decision-making processes.
 - ♦ Regular elections and transparent administrative practices empower residents to have a say in the development and management of their cities.
- **Social Equity** by ensuring that all sections of society have access to essential services and opportunities.
 - ♦ Programs aimed at improving education, healthcare, and housing for marginalized communities help in reducing social disparities and promoting inclusive growth.

Current Fiscal Challenges With Municipal Corporation

- **Inadequate Revenue Generation:** According to recent reports, municipal revenues constitute a **mere 0.6% of India's GDP in 2023-24**, despite urban areas contributing nearly 60% to the nation's economic output.
 - ♦ Poor property tax revenues, which account for **only 0.12% of GDP**, exacerbate this issue.
 - ♦ For instance, state transfers account for 30% of municipal revenues, while Union transfers contribute just 2.5%.
- **Dependence on Government Grants:** More than 50% of municipal corporations generate less than half their revenue independently, while government transfers rose by over 20% in 2022-23.
 - ♦ The concentration of revenue generation among a few large municipal corporations further exacerbates the issue, with the top ten MCs accounting for over 58% of total municipal revenues.

- **Inefficiency in Tax and Fee Collection:** The inefficiency in property tax systems and the inadequately adjusted user fees for essential services like water supply and sanitation affect cost recovery.
 - ♦ It leads to a lack of funds for maintaining and improving infrastructure and services.
- **Revenue Concentration:** Over 58% of municipal revenue is generated by the top 10 municipal corporations, leaving smaller and less affluent ULBs struggling to meet their financial obligations.
- **Fiscal Decentralization:** The devolution of financial powers to ULBs has been inadequate.
 - ♦ The quantum and predictability of funds transferred from state and central governments are often insufficient, leading to financial instability for ULBs.
- **Transparency and Accountability:** The absence of robust performance measurement and audit mechanisms makes it difficult to assess the financial health and service delivery of municipal corporations.

Strategic Recommendations for Financial Improvement

- **Own Sources of Revenue Generation: Property taxes** are the major constituent of tax revenues for MCs, but the collection efficiency is low.
 - ♦ The report suggests adopting technologies like **GIS-based property tax mapping and digital platforms** for tax collection to improve compliance and plug revenue leakages.
 - ♦ **Non-tax revenues** have also contributed to the recovery of municipal revenues, but there is still a need for better enforcement and augmentation of institutional capacity.
- **Borrowing and Municipal Bond Financing:** Municipal bond financing has seen some recovery, with MCs venturing into green municipal bonds to fund environmentally beneficial projects.
 - ♦ However, the reliance on transfers and grants from upper tiers of government continues, affecting the functional and financial autonomy of MCs.
- **Promoting Fiscal Decentralization:** Strengthening **State Finance Commissions (SFCs)** and establishing frameworks to estimate expenditure obligations and funding mix can enhance fiscal decentralization.
 - ♦ Clear rule-based frameworks for state and central transfers can ensure predictable compensation for ULBs.
- **Improving Transparency and Accountability:** Enforcing public disclosure laws and promoting citizen participation in budgeting and financial decision-making can enhance transparency and accountability.
 - ♦ Participatory budgeting and community involvement can help build trust and ensure that funds are used effectively.
- **Supporting Development Initiatives** such as the **Smart Cities Mission and the Atal Mission for Rejuvenation and Urban Transformation (AMRUT)** that aim to improve infrastructure, enhance service delivery, and promote sustainable urban development.
- **Reducing Dependence on Transfers:** Clearly defining rule-based frameworks for state and central transfers to ensure predictable compensation.

Conclusion and Way Forward

- Municipal fiscal reforms are essential for ensuring financial sustainability and accountability in urban governance.
- By addressing the challenges in revenue generation and enhancing participatory governance, India can build a more resilient and efficient municipal system.
- The success of these reforms will not only improve service delivery but also contribute to the overall development of urban areas.

Source: BS

Mains Practice Question

Discuss the significance of municipal fiscal reforms in addressing urban governance challenges. Analyze the key reforms required and their potential impact on urban development and citizen well-being.

