



Reviving the spirit of Centre-state alliance

For cooperative federalism to survive, empower the moribund Inter-State Council to fulfil its role of mediating Centre-state relations

The recent fracas between the Centre and states over fuel tax reduction is a stark reminder of just how “uncooperative” Centre-state relations have become in India. This lack of cooperation is a consequence of a failure to invest in institutional mechanisms to negotiate intergovernmental ties, particularly in the fiscal realm and a political culture that has little patience with the federal principle. As a result, today, India is entering an era of “uncooperative” federalism, which risks undermining our economic growth prospects and the foundations of our democratic consensus.

Beyond the specific economic context in which the dispute over rising prices and the urgent need to cut fuel taxes arose, the current episode reflects a more profound tension that lies at the heart of the federal bargain — of balancing the need for intergovernmental cooperation with the pres-

ures of maintaining autonomy and agency at the state government level.

In the fiscal realm, this tension is exacerbated by the fact that our constitutional design has several centralising features (the Centre controls the bulk of revenue-raising powers, even as states bear a larger share of expenditure responsibility) which, New Delhi has routinely, across political parties, misused to encroach on the powers of the states. States, on their part, have oscillated between resistance and strategic acquiescence (especially when there is political credit to be gained) to centralisation. It is in the interstices of the pulls of centralisation and pressures for autonomy, that the fiscal federal dynamic has been shaped.

The introduction of the Goods and Services Tax (GST) in 2017 changed the rules of the game. Lured by the promise of an excessively generous compensation (14% year-on-year tax growth for five years), states gave up a significant degree of tax autonomy to forge the so-called “grand bargain”. But they did so while seeking to preserve a degree of autonomy. Keeping critical revenue sources, particularly petrol and diesel, out of GST’s ambit was the compromise.

How these dynamics play out in realpolitik is best illustrated in Tamil Nadu finance minister P Thiagarajan’s response to the prime minister’s

call to states to reduce petrol taxes. The Centre’s ask, he argued, to synchronise goes against the spirit of fiscal federalism. States, he said, “are not extended arms of the central government without independent thinking”. Herein lies the crux of the challenge of cooperative federalism — that of ensuring that intergovernmental bargains like GST respect state autonomy.

Negotiating federal cooperation requires political maturity and a commitment to the federal principle. These conditions do not exist today, even though the need for cooperation evidenced in the fuel tax controversy is mounting. Consider the GST experience. Once GST was rolled out, and it became evident that the promise of revenue growth was overestimated, the Centre resorted to increasing revenue through cess and surcharge, which are not shareable with states. Since 2017, the Centre’s cess on petroleum products has increased at a far greater pace than the state Value Added Tax. Thus, states have rightly argued that the Centre’s call to cut taxes is in bad faith.

And it’s not just fuel tax. Despite popularising the rhetoric of cooperative federalism since 2014, the Centre has repeatedly undermined the terms of cooperation and squeezed states of resources. It has done so through cess and surcharge (now at



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nearly 20% of gross tax revenue), by increasing states’ share in central schemes, and amid the Covid-19 crisis, delaying GST payments and effectively altering the terms of its compensation commitment by resorting to a back-to-back loan mechanism.

This failure to uphold the fiscal bargain sits comfortably with the BJP’s broader political project. Ideologically, the BJP’s homogenising impulse sits in profound tension with the federal idea, which is principally about accommodation. This is, in turn, unleashing a renewed identity politics of sub-nationalism that leaves states with little incentive for effective federal cooperation. Centre-state battles in Opposition-ruled states are now an everyday occurrence. We are firmly in the era of “uncooperative federalism”.

But this era of “uncooperative federalism” coincides with an increased need for economic cooperation. From goods and services to capital, labour and natural resources, the national economy is increasingly inter-dependent and cooperation both across states and with the Centre is critical for growth. This makes

a case for deeper economic cooperation urgent, even as political imperatives are pulling in a different direction.

The path out of this quagmire is to invest in regular, sober Centre-state dialogue. This is where India’s federal compact has historically been at its weakest. The Planning Commission institutionalised itself as a centralising force. In its place, the Niti Aayog, despite deploying the rhetoric of cooperative federalism, plays the role of a technocratic body rather than a site for dialogue. Consequently, federal contestations are being negotiated in an institutional vacuum.

The answer could lie in empowering the moribund Inter-State Council (ISC) to fulfil its constitutionally mandated role of mediating Centre-state relations. By committing themselves to strengthening ISC, the Centre and states can rehabilitate cooperative federalism. The failure to do so will cost our economic and democratic future dearly.

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