



Report on Municipal Finances: RBI

For Prelims: Local governance, RBI, Municipal Corporations, GDP, GST.

For Mains: Report on Municipal Finances, RBI.

Why in News?

Recently, the [Reserve Bank of India \(RBI\)](#) has released the **Report on Municipal Finances**, compiling and analyzing budgetary data for 201 [Municipal Corporations \(MCs\)](#) across all States.

- The RBI Report explores '**Alternative Sources of Financing for Municipal Corporations**' as its theme.

What is a Municipal Corporation?

- **About:**
 - In India, the Municipal Corporation is the **urban local government** that is responsible for the development of any Metropolitan City having a **population of more than one million people**.
 - Mahanagar Palika, Nagar Palika, Nagar Nigam, City Corporation, and so on are some of the other names for it.
 - The Municipal Corporations are established in the states by the **acts of the state legislatures**, whereas in the Union Territories through the acts of the Parliament.
 - Municipal governments **rely heavily on property tax revenue** to fund their operations.
 - The first municipal corporation in India was created in **Madras in 1688, followed by municipal corporations in Bombay and Calcutta in 1726**.
- **Constitutional Provisions:**
 - In the Constitution of India, no provision was made for the establishment of local self-government, except the incorporation of **Article 40 in the [Directive Principles of State Policy](#)**.
 - The **74th Amendment Act, 1992** has inserted a new Part IX-A into the Constitution which deals with the administration of Municipalities and Nagar Palikas.
 - It consists of Article 243P to 243ZG. It also added a new **twelfth schedule** to the Constitution. The 12th schedule consists of 18 items.

What are the Findings?

- **Poor working of MCs:**
 - There have been several lacunae in the working of MCs and **no appreciable improvement in their functioning despite institutionalisation** of the structure of [local governance](#) in India.

- The availability and quality of essential services for **urban populations in India** has **consequently remained poor**.
- **Lack of Financial Autonomy:**
 - Most municipalities only prepare budgets and **review actuals against budget plans but do not use their audited financial statements** for balance sheet and cash flow management, resulting in **significant inefficiencies**.
 - While the size of the municipal budgets in India are much smaller than peers in other countries, **revenues are dominated by property tax collections and devolution of taxes and grants from upper tiers of government**, resulting in **lack of financial autonomy**.
- **Minimal Capital Expenditure:**
 - MCs' committed expenditure in the form of establishment expenses, administrative costs and interest and finance charges is rising, **but capital expenditure is minimal**.
 - MCs mostly rely on borrowings from banks and financial institutions and loans from centre/ state governments to finance their resource gaps in the absence of a **well-developed market for municipal bonds**.
- **Stagnant Revenues/Expenditure:**
 - Municipal revenues/expenditures in India have stagnated at around **1 % of GDP (Gross Domestic Product)** for over a decade.
 - In contrast, municipal revenues/ expenditures account for 7.4 % of GDP in Brazil and 6 % of GDP in South Africa.
- **Ineffective State Financial Commissions:**
 - Governments have not set up **State Financial Commissions (SFCs)** in a regular and timely manner even though they are required to be set up every five years. Accordingly, in most of the States, SFCs have not been **effective in ensuring rule-based devolution of funds to Local governments**.

What are the Suggestions?

- MCs need to adopt **sound and transparent accounting practices** with proper monitoring and documentation of various receipt and expenditure items, and explore different innovative bond and land-based financing mechanisms to augment their resources.
- The rapid rise in urban population density, however, calls for **better urban infrastructure**, and hence, requires greater flow of **financial resources to Local governments**.
- With the revenue generation capacity of municipal corporations declining over time, dependence on the devolution of taxes and grants from the upper tiers has risen. This calls for **innovative financing mechanisms**.
- Municipalities in India need to balance **their budgets by law**, and any municipal borrowing needs to be approved by the State government.
- In order to improve the **buoyancy of municipal revenue**, the Centre and the States may share one-sixth of their **GST (Goods and Services Tax)**.

UPSC Civil Services Examination Previous Year Question (PYQ)

Q. In India, the first Municipal Corporation was set up in which one among the following? (2009)

- (a) Calcutta
- (b) Madras
- (c) Bombay
- (d) Delhi

Ans: (b)

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