There have been many conflicts with regard that whether India is a federal state of not. But, when we see about the characteristics of federal state then we find that one of the characteristics specifically mentions about the distribution of taxes. Thus, a federal state always has a distribution of powers. Indian Constitution specifies about the distribution of revenues where exclusive powers are given to the State, to collect taxes and exclusive powers rest with Union in relation with taxes.

There are three lists namely, central, state and concurrent lists, where distribution of taxes is there in various entries. So, framers of the Constitution have definitely made the distribution appropriately.

The importance of such a distribution is very clear, as with the distribution only, Government will come to conclusion as how has been distributed to each states and how much it should be kept in consolidated fund of India to meet future needs. So, it's very important to see that equal distribution is made of revenues with respect to their contribution.

Distribution of revenues thus, leads to clarity and leaves no scope for any confusion. With the help of distribution, we meet justice. Also, the relationship between center and state grows and the Government doesn't go only unitary but equal participation of State is also there in colleting taxes. So, distribution of revenue leads to a better form of Government as the provisions with regard to distribution can be changed according to needs and circumstances if any conflicts between the distributions arise.

The distribution of revenues is from Article 278 till Article 281 in the Indian Constitution. The project gives importance to various restrictions imposed on State Government in levying taxes, distribution of revenues, finance commission and analysis.

Distribution of Revenues Between Union And States

There are few Articles in the Indian Constitution which specifically focuses on distribution of revenues.

They are:

Article 268: Duties levied by the Union but collected and appropriated by the States:

This Article was amended by the Constitution (seventh amendment) Act, 1956 with effect from 1st November 1956. Article 268 (1) provides that stamp duties and excise on medicinal and toilet preparation which are mentioned in Union List, the collection of duties shall be made by the State which shall be levied by the Union Government of duties shall be made by the State which shall be levied by the Union Government. The proceeds of any such duty leviable within any State in any financial year shall not form part of the consolidated Fund of India but shall be assigned to that State.

Article 268-A: Service tax levied by Union and collected an appropriated by the Union and States:

This Article was inserted by ninety-fifth Amendment Bill, 2003 which was passed by both the Houses of Parliament – Lok Sabha on 6-5-2003 and Rajya Sabha on 8-5-2003 . Article speaks that taxes on services shall be levied by the Government of India which shall be collected by the States. Such tax shall be appropriated by the Government of India and the States.

Article 269: Taxes levied and collected by the Union but assigned to the States:

This Article was lastly amended by the eightieth amendment with effect from 1st April, 1996. Taxes which shall be levied and collected by the Government of India which are included in this Article: (a) the consignment of goods which takes place in the course of inter-state trade or commerce, (b) sale or purchase of goods which takes place in the course of inter-state trade or commerce.

Case: Goodyear India Ltd. V. State of Haryana

In this case, the question was in relation with two sales tax act which speaks on consignment of goods. Section 9(1) (b) of the Haryana General Sales Tax Act, 1973 and Section 13AA of the Bombay Sales Tax Act, 1959 is the tax on consignment goods and these provisions are beyond the respective State Legislatures as the power vests with the Parliament. And so, it was held to be invalid. Clause 3 of this Article provides that Parliament may formulate principles for determining that when such sales and purchase or consignment takes place in the course of inter-state trade or commerce.

Case: State of Andhra Pradesh v. National Thermal Corporation Ltd

The Supreme Court considered section 3 and 6 of Central Sales Tax Act, 1956. Supreme Court held that a movement of goods after completion of the transaction of sale within the State, does not constitute inter-State sale. Bench has also laid down few principles for considering inter-State trade or commerce:
1) Existence of a contract of sale incorporating a stipulation, express or implied regarding inter-State movement of goods;
2) Goods must actually move from one State to another pursuant to such contract;
3) Such movement of goods must be from one State to another, where the sales conclude.

Article 270: Taxes levied and distributed between Union and States:

This Article was lastly amended in eightieth amendment which was in effect from 1st April, 1996. This Article specifically provides that taxes on income other than agricultural income and corporation tax shall be levied and collected by the Union and is distributed by the Union and States . The revenue which shall be transferred to the Sates is unconditional and the States shall be free to use their income as and when they like. In spite of the large transfer, the fact remains that States are not happy and the main reason being that due to political reasons, the States do not make adequate efforts to impose more tax. The tax proceeds shall not form a part of consolidated fund of India but shall be distributed among States.

Case: T.M. Kanniyan v. I.T.O

Supreme Court gave a judgment with regard to income tax and said that the income tax attributable to Union territories forms a part of the Consolidated Fund of India. It is not necessary to make any distribution of income tax with respect to Union territories as those territories are centrally administered through the President.

Article 271: Surcharge on certain duties and taxes for purposes of the Union:

This Article corresponds to S. 137 and S. 138(1) of the Government of India Act, 1935. Article basically speaks that Parliament is empowered to levy a surcharge from time to time as it's the parliament who has imposed a surcharge and so it won't be precluded to surcharge in another form. All proceeds from such surcharges are to form part of the Consolidated Fund of India and are not liable to be distributed among the states. No one can prevent Parliament to impose a surcharge.

Article: 272: Taxes which are levied and collected by the Union and may be deistributed between the Union and the States:

This Article has been omitted by the Constitution Act, in eightieth amendment.

Grant – In – Aid:

Article 273: Grants in lieu of export duty on jute and jute products:

Under the Government of India Act, the Central Governement shared the net proceeds of the jute export duty with the jute growing provinces. Under this Constitution, the States are not entitled to any such share.

The Provision specifies that for a period of 10 years from the commencement of the Constitution, the jute growing states of West Bengal, Bihar, Orissa and Assam will receive grants-in-aid from the Union in lieu of the above share of the jute export duty to the extent of sums specified by the President with the consultation of Finance Commission.

Article 275: Grants from the Union to certain States

This Article was amended in twenty-second Amendment which came in effect in 1969. Parliament is empowered to make such grants, as and when it is necessary to the States which are in need of financial assistance. Special grants may also be made to promote welfare schemes for Scheduled Castes and Scheduled Tribes.

Article 282: Expenditure defrayable by the Union or a State out of its revenues:

This Article corresponds to (i) Section 150 of the Government of India Act, 1935; (ii) Article 1, Section 8(1) of the Constitution of the United States, and (iii) Section 81 of the Commonwealth of Australia Constitution Act, 1900. This Article provides that the spending power of the Union or State Legislature is not limited to the legislative powers. Thus, they can spend more money but the purpose should be public. Criticism: This Article has very wide wings. How this money is to be utilized, is not mentioned in this article. So, any political party can misuse the money in name of public purpose.

Case: Cf. Narayanan Nambudripad, kidangazhi Manakkal v State of Madras

Supreme Court has decided that the exercise of religion is a private purpose. But, if the States themselves take the management of such religious endowment in the interest of public order, mortality, or health, then it is for pubic purpose.

Restrictions of The States Power To Levy Taxes

Article 276: State's power to Levy taxes on Professions and Trades:

Article authorizes a state or other local authority to levy taxes on professions etc. where List 2, Entry 60 speaks of. Clause 2 of this Article specifies the fixed limit of Rs. 250 per annum for taxes on professions, calling etc. Later, Constitution raised the limit to Rs. 2500.

Case: Quilon Municipality v. H&C. Ltd.
Here, Kerela Profession Tax, 1958 was held to be ultravires because it violated Article 276 and also encroaching upon the Union firld of income tax inasmuch as it exceeded the permissible limit which was there Rx. 250 at that time.

Case: B.M. Lakhani v. Municipal Committee
Here 2 questions were raised: (a) whether a suit for refund of tax, which was ultra vires the municipality, paid to the municipality was maintainable, and (b) if the suit is maintainable, whether the levy of tax by the municipality was valid in law. Thus, Supreme Court held that the suit for refund of tax in excess of the amount permitted by Article 276 was maintainable. And, for second question, there was a bar against the levy in excess of the amount specified in the Constitution and not a mere question of levy of taxes under an inapplicable entry.

Criticism: (a) This Article comes in overlapping situation with Union list but still Constitution permits such kind of overlapping. (b) Even if the matter may not fall in the law made by the State relating to taxes, for the benefit of States of a municipality, district board, local authority etc. shall not be invalid on the grounds that it relates to a tax of income.

Article 286: State's power to Levy Taxes

Article 286 gives the power to levy taxes on sale or purchase of goods other than newspapers belonging to States. But, there are few Union laws like imports and exports and taxes on sale or purchase of goods, other than newspapers in the course of inter-State trade or commerce. So, to avoid such overlapping,

Article 286 subjects the States power to levy sales tax to the following restrictions:-

Article 286 (1) (a): No State can tax a sale or purchase taking place outside the State This Article specifically prohibits a State to impose a tax on the sale or purchase of goods where such sale or purchase takes place outside the State. But, clause 2 of this Article clearly lays down the principles for determining when a ale or purchase takes place outside the State.

Article 286 (1) (b): No State can tax a sale or purchase taking place in the course of import and export:
This Article prohibits a State to impose a tax on the sale or purchase of goods when such sale or purchase takes place in the course of import of the goods into or export of the goods out of the territory of India. Parliament may by law formulate principles for determining when a sale or purchase takes place in the course of import and export of

determining when a sale or purchase takes place in the course of import and export of goods.

Case: K. Gopinath v. State of Kerela
There were cashewnuts, which were purchased and imported by the C.C.I from African suppliers, which were sold by C.C.I to local users. SC held that the sale by the C.C.I were not in the course of import and was not covered by the exemption of Central Sales Tax Act, 1956. There being no direct or inserverable link between transactions of sale and import of goods on account of nature of understanding between the C.C.I. and purchasers as also be the reason of canalizing scheme for import by C.C.I. the sales do not go in exemption.

Entry 92A Union List: No state can tax a sale or purchase taking place in the course of Inter-State trade and commerce:
The power to impose tax on sale or purchase is exclusively vested with the Parliament. Section 3 of Central Sales Tax Act, 1956 provides that: A sale or purchase of goods shall be deemed to take place in the course of Inter-State trade or commerce if the sale or purchase – (a) occasions the movement of goods from one Sate to another; or (b) is effected by a transfer of documents of title to the goods during their movement from one State to another.

Article 286(3): Taxes on sale or purchase of goods of special importance:
Section 14 of the Central Sales Tax Act, 1956 declares a number of goods to be of special importance in Inter-State trade or commerce. Section 15 thus, imposes restrictions on taxation of sales of such goods.

Article 286 (3) (b): Taxes on the sale or purchase of goods in the course of Inter-State trade or commerce specified in sub clauses (b), (c) or (d) of clauses (29-**A) of Article 366:**
Clause 29-A of Article 366 provides for tax on sale or purchase of goods on transfer of property in goods involved in execution of a works contract, on delivery of goods on hire-purchase or any system of payment by installments, transfer of right to use any goods for any purpose for cash, deferred payment or any other valuable consideration. Thus, State law is restricted to impose any tax on above things.

Article 277 And Article 279
Article 277: Savings
This article speaks about any taxes, duties, cesses or fees which immediately before the commencement of the Constitution, were being lawfully levied by the Government shall be continued for the same purposes notwithstanding that above things are mentioned in Union list, unless the contrary law has been provided.
According to Durga Das Basu, the object of this article is to prevent dislocation of the finances of local government and authorities by reason of the coming into force of new constitutional enactments disturbing heads of taxation on lines different from those which existed before the commencement of such constitutional changes.

It is presumed that the taxation is meant for the benefit of the public which results from expenditure incurred or from schemes undertaken by State or local Government authorities. The scope of the Article is limited and it has no application where there has been no shifting in the allocation of power as between the Union and the State under the Constitution.

Case: Amravati Municipality v. Ramchandra
The municipality of Amravati, under a law passed before the Constitution came into operation, imposed terminal tax on goods, except gold and silver, imported in or exported outside municipal limits by rail or road. The power to impose this kind of tax

exported outside municipal limits by rail or road. The power to impose this kind of tax after the commencement of the Constitution was given to the Parliament under Entry 89 of List I. after the commencement of the Constitution, an amending notification of the municipality of 1959 made gold and silver also subject to the terminal tax. The Court held that, the action of the municipality is unconstitutional on the ground that Article 277 could neither permit increase in the rate nor could its incidence be altered.

It must be noted that article 372 is a general provision and article 277 is a special provision. Article 372 saves all pre-constitutional valid laws and article 277 is confined to only taxes, duties cesses or fees. Article 372 must be read subject to Article 277.

Case: Hyderabad Chemical and Pharmaceutical Works Ltd. V. State of Andhra Pradesh
The appellant were manufacturing medicines in which they had to use alcohol. They were working under licenses granted under the Hyderabad Abkari Act and the rules made there under. They were required to pay certain fees to the State Govt. for the supervision. There after, the Parliament passed the Medicinal and Toilet Preparations Act, 1955 under which they were not required to pay the fee. The petitioner challenged the levy of fees by the State Govt. after the passing of the Central Act, 1955. By virtue of entry 84 of list 1 and VIIth Schedule and Art. 277, no charge could be levied by the State. It was held that after the passing of the law by the Parliament, the Hyderabad Act must be deemed to have been repealed.

There is also a difference between tax and fee. A tax is an imposition made for public purpose, without reference to any services rendered by the State or any specific benefit. Whereas, fee is a payment levied by the State in respect of services performed by it for the benefit of the individual. It is levied on a principle just opposite to tax. Tax is paid for common benefit conferred by the Government on all tax-payers, whereas a fee is payment made for some special benefits.

Article 279: Calculation of net proceeds, etc

This article defines the net proceeds of a tax. It means all the proceeds of tax reduced by the cost of collection. The certificate of the Comptroller and the Auditor General of India of net proceeds of a tax in a State shall be final.

Finance Commission
Article 280 of the Indian Constitution speaks about finance commission. The idea of Finance Commission has been adopted from the model of the Common-wealth Commission of Australia. The expert committee on the Financial Provisions of the Constitution recommended the setting up of a Finance Commission. The Finance Commission in India is an innovation of far reaching importance as it attempts to make the Indian fiscal system federal in character. It is worth noting that in assessing the needs of the States and determining the proportions in which the States, individually, should share the central assistance, the Finance Commission has been guided inter-alia, by the principle that the scheme of distribution should attempt to lessen the inequalities between the states The framers of the Constitution ensured that the transfer of funds from the Centre to the States should be made neither in such a manner as nor to impair the autonomy of the States. Article 280 required the President to appoint a Finance Commission within two years from the commencement of the Constitution and thereafter at the expiration of every fifth year or at such earlier time as the President might consider necessary.

According to the Finance Commission Act, it has all the powers of a civil court for summoning the witnesses, requiring production of any document, requiring any person to furnish information on any point which the Commission regards as useful or person to furnish information on any point which the Commission regards as useful or relevant to any matter under its consideration.

Constitution of Finance Commission:

According to the Finance Commission Act, 1952, the Commission is to consist of a Chairman and four other members appointed by the President. The Act further says that, the Chairman of the Finance Commission shall be selected from amongst persons who had experience in public affairs and the members shall be selected from the following categories:
Who are qualified to be appointed as judge of a High Court; or
Who have special knowledge of the finance; or
Who had wide experience of financial matters and in administration; or
Who had special knowledge of economics.
Importance of Finance Commission:
The Finance Commission is capable of settling many complicated financial problems which affect the relationship between the Union and the States. The recommendations of the last 12 Finance Commissions have proved that the Commission has settled many complicated problems and the present system of allocation of finance between the Union and the States is almost the result of these recommendations. While making recommendations, Finance Commission will take all relevant matters into account including the state of finances of Centre.
Functions of Finance Commission:
The Commissions first function would be of the nature of arbitration, and therefore the Commissions decisions will be final. There are few duties described by Art. 280(3):
The distribution between the Union and the States of the net proceeds of the taxes which are to be, or may be, divided between them, and the allocation of the respective shares of such proceeds;
The principles to govern the grants-in-aid of the revenues of the States out of the Consolidated Fund of India;
The measures needed to augment the State Consolidated Fund to supplement the resources of the panchayats in the State on the basis of the recommendations made by the State Finance Commission;
The measures needed to augment the State Consolidated Fund to supplement the resources of the municipalities in the State on the basis of the recommendations made by he State Finance Commission;
Any other matter referred to it by the President in the interest of the sound finance.

Various Finance Commissions:
Originally, the Finance Commission was intended to cover all the financial transfers from the Centre to the States under Articles 269, 272, 275, and 282. I fact the First and Second Finance Commission recommended financial assistance to cover both the revenue and the capital requirements of the States, but the establishment to the Planning Commission led to the bifurcation of this function and the Finance Commission's role became limited to the non-plan expenditure. There have 12 finance commissions till now. The last Finance Commission is established in 2003 where the Chairman of that Commission is C. Rangarajan. It is only expected that the Finance Commissions shall apply only 2 yardsticks: one of the tax effort of the State, and another is the efficiency and economy in formulating its recommendations. But, A.K. Chanda in late seventies in his book mentioned that: it feels that neither of the yardsticks have been applied, as the tax potential varies from State to State and it is beyond the resources of, and the time allocated for, a Finance Commission to undertake the assessment, also it is unable to evaluate the relative administrative efficiency of the States, as neither the statistical material nor the time needed is available for making such in-depth study. So, what I can infrige from his statement made at that time was that, Finance Commission has failed to fulfill its purpose, which

made at that time was that, Finance Commission has failed to fulfill its purpose, which is contrary to the views made by S. R. Bhansali, who said that Finance Commission has been a backbone to many problems. Thus, I feel that Finance Commission has come up to a great help in solving the distribution of revenues, and will be of great help in future also.

Conclusion

This paper work basically deals with the distribution of taxes. So, my paper work focuses on the various ways in which distribution of revenues takes place, also the role of finance commission, and certain restrictions of State in levy of taxes. The idea of Finance Commission is very unique. It is very important to have a separate body recommending in issues related financing. The framers of the Constitution have correctly put note of the finance commission. The distribution of revenues have been properly dealt as neither the rules are rigid nor it's confusing. The idea of dividing the taxes has been properly dealt. Though, the collection of main revenues is dealt by Union Government, but still, there are quite number of taxes which are dealt only by State. The distribution in few revenues is though overlapping but the ends of justice do meet. I can clearly note that Parliament's rights are not tied up. Every law is subject to Parliaments new contrary law. Thus, Indian Constitution gives wide powers to parliament and it is not rigid neither same. So, according to future needs one can also change the said rules of law. The procedural aspects of this distribution might be confusing or rather difficult but the theoretical aspects are very clearly laid down by the Indian Constitution.

The author can be reached at: sweetahmdkoko@legalserviceindia.com / Print This Article

Articles of Yesteryears

Click on the link Below to check articles submitted in previous years:
Latest Articles - Law Articles 2017 - Law Articles 2016 - Law Articles 2015 - Law Articles 2014 - Law Articles 2013 - Law Articles 2012 - Law Articles 2011 - Law Articles 2010 - Law Articles 2009 - Law Articles 2008 - Articles 2007 - Law Articles 2006 - Law Articles 2000-05 - Archive

Lawyers in India - Search By City

Delhi	Mumbai	Kolkata	Chennai
Chandigarh	Pune	Siliguri	Jamshedpur
Allahabad	Nagpur	Durgapur	Hyderabad
Lucknow	Nashik	Janjgir	Coimbatore
Noida	Ahmedabad	Jaipur	Eluru
Gurgaon	Surat	Ludhiana	Belgaum
Faridabad	Indore	Dimapur	Cochin
Jalandhar	Agra	Guwahati	Rajkot
Vapi	Jalgaon	Amritsar	Jodhpur