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Federalism in India: Centre-State Relations, Constitutional Provisions, and Emerging Challenges

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ABSTRACT: The Indian Constitution establishes a federal system with a strong central government while providing significant powers to the states. Centre-state relations are governed by the distribution of legislative, administrative and financial powers set out in the Seventh Schedule and related articles. Over the decades these relations have been shaped by constitutional amendments, the recommendations of Finance Commissions, and the working of institutions such as the Inter-State Council and the Goods and Services Tax Council. While the formal framework has remained stable, tensions have arisen over the use of Article 356, the allocation of financial resources, and the implementation of centrally sponsored schemes. An examination of constitutional provisions and institutional practice indicates that cooperative mechanisms have expanded, yet questions of fiscal autonomy and political coordination continue to influence the operation of Indian federalism.

KEYWORDS: Indian federalism; centre-state relations; Seventh Schedule; Finance Commission; Article 356; Goods and Services Tax; Inter-State Council

I. INTRODUCTION

The Constitution of India creates a federal polity in which powers are divided between the Union and the states, yet the balance is weighted toward the Centre. Legislative subjects are distributed across the Union List, the State List and the Concurrent List in the Seventh Schedule (Constitution of India, 1950). The Union possesses residuary powers, and Parliament may legislate on state subjects under specified conditions. This design reflected the concerns of the Constituent Assembly about national unity and the need for coordinated economic planning. Centre-state relations have therefore involved both the formal allocation of powers and the practical arrangements through which those powers are exercised.

Financial relations occupy a central place in the working of Indian federalism. The Constitution provides for the sharing of tax revenues and for grants-in-aid, with the Finance Commission recommending the distribution of resources every five years. Administrative relations are governed by articles that permit the Union to give directions to states and that establish mechanisms for coordination. Political practice has added further dimensions, including the role of the Governor, the use of President's Rule, and the operation of centrally sponsored schemes. An assessment of centre-state relations requires attention to both the constitutional text and the institutions that have developed to manage intergovernmental coordination.

II. CONSTITUTIONAL DISTRIBUTION OF POWERS

The Seventh Schedule divides legislative authority into three lists. The Union List contains subjects of national importance such as defence, foreign affairs, banking and inter-state trade. The State List includes public order, police, public health, agriculture and local government. The Concurrent List covers matters such as criminal law, marriage, education and forests, on which both Parliament and state legislatures may legislate, with Union law prevailing in the event of conflict (Constitution of India, 1950). Residuary powers rest with Parliament. Article 249 permits Parliament to legislate on a state subject if the Council of States passes a resolution that such legislation is necessary in the national interest. Article 250 allows Parliament to legislate on state subjects during a proclamation of emergency.

Administrative relations are set out in Articles 256 to 263. States are required to exercise their executive power so as to ensure compliance with Union laws. The Union may give directions to states for this purpose and, in certain circumstances, may assume executive authority. Article 263 provides for the establishment of an Inter-State Council to inquire into and advise upon disputes between states and to discuss subjects of common interest. These provisions

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create a framework in which the Centre possesses significant supervisory powers while states retain primary responsibility for a wide range of domestic functions. The practical balance between these powers has varied with political circumstances and with the recommendations of successive commissions.

III. FINANCIAL FEDERALISM AND THE ROLE OF FINANCE COMMISSIONS

Financial arrangements constitute one of the most important dimensions of centre-state relations. The Constitution assigns the more elastic sources of revenue, including income tax and customs duties, primarily to the Union, while states receive a share of these revenues on the recommendation of the Finance Commission. The Commission also recommends grants-in-aid to states that require assistance (Constitution of India, 1950, Articles 270, 275, 280). Successive Finance Commissions have increased the share of the divisible pool transferred to the states. The Fourteenth Finance Commission, whose award covered the period 2015–2020, raised the states' share from 32 per cent to 42 per cent of the divisible pool (Fourteenth Finance Commission, 2015). This change enlarged the volume of untied resources available to states.\

Despite the increase in tax devolution, states have continued to express concern about the proliferation of centrally sponsored schemes. These schemes, funded largely by the Union, often come with detailed guidelines that limit state discretion in design and implementation. The volume of such transfers has at times offset the flexibility gained through higher tax devolution (Rao & Singh, 2005). Own-source revenues of states, derived mainly from sales tax (later subsumed under the Goods and Services Tax for many items), excise on alcohol, and stamps and registration, vary widely across states. Differences in revenue capacity and in the cost of providing services have made equalisation an enduring issue in the recommendations of Finance Commissions.

IV. GOODS AND SERVICES TAX AND COOPERATIVE FEDERALISM

The introduction of the Goods and Services Tax in 2017 marked a significant change in fiscal federalism. The tax replaced a number of central and state indirect taxes and created a dual structure in which both the Union and the states levy GST on a common base. Decisions on rates, exemptions and administrative procedures are taken by the GST Council, a body in which the Union and the states are represented (Constitution (One Hundred and First Amendment) Act, 2016). The Council operates on the principle of weighted voting, with the Union holding one-third of the votes and the states collectively holding two-thirds. This arrangement has been described as an instance of cooperative federalism because major decisions require a substantial measure of agreement between the Centre and the states.

The transition to GST involved a commitment by the Union to compensate states for any revenue loss arising from the change for a period of five years. Compensation was to be funded by a cess levied on specified goods. While the Council provided a forum for regular consultation, differences emerged over the adequacy of compensation and over the classification of certain items. These differences illustrated both the potential of the institutional mechanism and the continuing tensions that arise when revenue interests diverge. The GST experience therefore offers evidence of both the expansion of cooperative institutions and the persistence of fiscal disagreements within the federal system.

V. USE OF ARTICLE 356 AND POLITICAL DIMENSIONS

Article 356 permits the President, on receipt of a report from the Governor or otherwise, to assume the functions of the state government if satisfied that the government of the state cannot be carried on in accordance with the Constitution. The provision has been invoked on numerous occasions since 1950. In several instances its use was criticised as politically motivated, particularly when a state government belonged to a party different from the party in power at the Centre (Austin, 1999). The Supreme Court, in S. R. Bommai v. Union of India (1994), held that the satisfaction of the President is subject to judicial review and that the majority of a state government should ordinarily be tested on the floor of the assembly. The judgment narrowed the scope for discretionary use of the article.

Even after the Bommai decision, questions concerning the role of the Governor and the circumstances in which President's Rule may be imposed have continued to arise. Governors are appointed by the President and hold office during the pleasure of the President. In practice, the office has at times been perceived as an instrument of central influence. Reports of commissions appointed to examine centre-state relations, including the Sarkaria Commission (1988) and the Punchhi Commission (2010), recommended greater restraint in the use of Article 356 and clearer conventions governing the appointment and functioning of Governors. These recommendations have informed subsequent practice, yet the potential for political contestation remains inherent in the constitutional design.

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VI. INTERGOVERNMENTAL INSTITUTIONS AND COORDINATION

Several institutions have been created to facilitate coordination between the Centre and the states. The Inter-State Council, established under Article 263, provides a forum for discussion of policies and for the resolution of inter-state disputes. Although the Council has met only intermittently, it has considered reports on centre-state relations and has offered recommendations on subjects of common concern (Inter-State Council Secretariat, 2018). Zonal Councils, created under the States Reorganisation Act, 1956, bring together states in each region to discuss matters of shared interest. The National Development Council, which included the Prime Minister, Union ministers and chief ministers, served for many years as a platform for approving five-year plans and for reviewing development strategies.

Sectoral councils and conferences of state ministers have also contributed to coordination in areas such as health, education and agriculture. These bodies lack statutory authority, yet they have enabled the exchange of information and the development of common approaches to implementation. The effectiveness of such mechanisms has depended on the willingness of both the Union and the states to use them for substantive discussion rather than for formal consultation alone. Where political alignment between the Centre and a majority of states has been high, coordination has generally been smoother. Where governments of different parties have held office, the same institutions have sometimes become arenas for the articulation of divergent priorities.

VII. EMERGING CHALLENGES IN CENTRE-STATE RELATIONS

Several challenges have become more visible in the working of Indian federalism. Fiscal stress experienced by some states has heightened demands for a larger share of central taxes and for greater flexibility in the design of centrally sponsored schemes. Differences in the rate of economic growth and in revenue capacity across states have made the task of equalisation more complex. The recommendations of Finance Commissions have sought to address these differences through horizontal distribution formulas that take account of population, area, income distance and forest cover, yet debates over the appropriate weights assigned to each criterion have continued (Fourteenth Finance Commission, 2015).

Political federalism has also presented challenges. The presence of regional parties in several states has increased the number of actors whose consent is required for major national initiatives. At the same time, the Union has retained significant leverage through its control over residual legislative powers, through the design of centrally sponsored schemes, and through the office of the Governor. Managing these cross-cutting pressures has required continuous negotiation. The experience of the GST Council demonstrates that institutionalised cooperation is possible, yet it also shows that cooperation does not eliminate underlying differences over resources and policy priorities. Maintaining a workable balance between national coordination and state autonomy remains an ongoing task for Indian federalism.

The distribution of legislative powers has remained largely stable since the adoption of the Constitution, yet successive amendments have adjusted the boundaries between the lists. Education, forests and weights and measures were transferred from the State List to the Concurrent List, reflecting a judgment that national coordination was desirable in these fields. Such transfers have enlarged the area in which both levels of government may legislate and have increased the occasions on which questions of repugnancy arise. The Supreme Court has held that, where a state law is repugnant to a central law on a concurrent subject, the central law prevails to the extent of the inconsistency, unless the state law has received the assent of the President. This rule preserves the supremacy of Parliament while still permitting states to experiment within the limits set by central legislation.

Financial devolution through the Finance Commission has been the principal instrument for addressing vertical and horizontal imbalances. Vertical imbalance arises because the Constitution assigns the more buoyant taxes to the Union while states bear substantial expenditure responsibilities in areas such as health, education and agriculture. Horizontal imbalance arises from differences in revenue capacity and in the cost of providing comparable services across states. The Fourteenth Finance Commission increased the states' share of the divisible pool and modified the criteria used for horizontal distribution, giving greater weight to income distance and introducing a factor for forest cover (Fourteenth Finance Commission, 2015). These changes enlarged the volume of untied funds available to states and altered the relative shares received by individual states.

Centrally sponsored schemes have remained a significant channel of resource transfer. Although the share of tax devolution rose after the Fourteenth Finance Commission award, the Union continued to finance a large number of schemes in sectors that fall primarily within state responsibility. Guidelines attached to these schemes often specify

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design features, beneficiary selection criteria and monitoring arrangements. States have argued that such conditions reduce their ability to adapt programmes to local circumstances and that the requirement of matching contributions strains their budgets. Efforts to rationalise the number of schemes have been undertaken at various times, yet the overall volume of scheme-based transfers has remained substantial. The tension between the flexibility afforded by tax devolution and the direction exercised through centrally sponsored schemes has therefore persisted.

The GST Council has provided a structured forum for negotiation between the Union and the states on indirect taxation. Decisions on rates and exemptions require a three-fourths majority of the weighted votes, giving both the Union and the states an effective voice. In the initial years of operation the Council reached agreement on a wide range of procedural and rate-related matters. Disagreements nevertheless surfaced over the classification of certain commodities and over the adequacy of compensation payments when revenue collections fell short of expectations. These episodes demonstrated that the institutional mechanism could accommodate divergent interests, yet they also showed that fiscal federalism continues to require ongoing adjustment when revenue outcomes differ from projections.

The judgment in S. R. Bommai v. Union of India (1994) established important limits on the use of Article 356. The Court held that the President's satisfaction is justiciable and that the floor of the legislative assembly is the proper place to test the majority of a state government. Subsequent invocations of the article have been fewer, and courts have examined the material on which the President acted. The office of the Governor, however, has continued to attract controversy. Because Governors are appointed by the Centre and may be removed at its pleasure, questions have arisen about the impartiality of their reports and about the timing of their interventions in state politics. Commissions on centre-state relations have recommended that Governors should be persons of eminence outside active politics and that they should be appointed after consultation with the state chief minister. These recommendations have not been fully incorporated into binding convention.

Intergovernmental coordination has relied on both constitutional and extra-constitutional bodies. The Inter-State Council has considered issues ranging from the implementation of Finance Commission awards to the management of inter-state river waters. Its meetings have been infrequent, yet the discussions have provided an opportunity for chief ministers and Union ministers to address matters that cut across state boundaries. Sectoral conferences of ministers have performed a similar function in fields such as agriculture, health and school education. The effectiveness of these forums has varied with the political composition of state governments and with the priority attached to consensus by the Union government of the day. Where a large number of states have been governed by parties different from the party at the Centre, the same institutions have sometimes served as platforms for the articulation of alternative policy positions.

Differences in economic performance across states have added a further dimension to centre-state relations. States with higher rates of growth and stronger revenue bases have been better placed to finance their expenditure responsibilities, while states with lower revenue capacity have remained more dependent on central transfers. Finance Commission formulas have sought to mitigate these disparities through equalisation components. Debates have nevertheless continued over the relative importance that should be given to need, cost disability and fiscal effort. These debates reflect the difficulty of designing a distribution formula that commands broad acceptance while still providing incentives for revenue mobilisation and expenditure efficiency.

The constitutional framework has proved durable, yet its operation has required continuous institutional adaptation. The expansion of the Concurrent List, the creation of the GST Council, and the periodic revision of tax devolution shares illustrate the capacity of the system to accommodate new policy challenges. At the same time, the persistence of concerns about the use of Article 356, the design of centrally sponsored schemes, and the coordination of development programmes indicates that the balance between national direction and state autonomy remains subject to negotiation. The quality of that negotiation depends on the regular functioning of intergovernmental institutions and on the willingness of both levels of government to treat differences of priority as matters for discussion rather than for unilateral resolution.

VIII. CONCLUSION

Centre-state relations in India rest on a constitutional framework that combines a strong Union with substantial state responsibilities. The distribution of legislative, administrative and financial powers, the recommendations of Finance Commissions, and the operation of institutions such as the GST Council and the Inter-State Council have shaped the practical working of federalism. Cooperative mechanisms have expanded, particularly in the fiscal domain, yet tensions

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over the use of Article 356, the volume and design of central transfers, and the coordination of development programmes have persisted. The record indicates that the constitutional provisions provide a durable foundation, while the quality of centre-state relations continues to depend on the use made of intergovernmental institutions and on the willingness of both levels of government to accommodate differing priorities within a shared framework.

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