DECENTRALISED URBAN GOVERNANCE IN INDIA
Implications for Financing of Urban Infrastructure

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Section I
Introduction

Decentralisation initiative in India is often considered to be a process purposefully adopted as a result of its need arising out of various political, social and economic factors. However, a different school of thought considers decentralisation a fall out of the globalisation and liberalisation process, the World over. Much of the literature on decentralisation, normative and empirical, is based on industrial countries and assumes the existence of institutions that are usually very weak in developing countries. Urban decentralisation- devolving powers and responsibilities to the municipal bodies (the city governments) was a result of the increasing pace of urbanisation, particularly in the larger cities. The opening up of the Indian economy to the World market has led to the creation of what is often referred to as "Global Cities". These cities became the hub of industrial and economic activities and attractive destinations for the foreign direct investments (FDIs). The urban areas in general and the larger cities in particular became the hub of industrial and economic activities after the local market got mingled up with the global market. The larger cities often referred to as the Global Cities attracted most of the foreign direct investments as well as short-term portfolio investments. As a consequence, it became inevitable for the city governments- municipal bodies to provide better infrastructure facilities to the citizenry in general and foreign investors in particular. It has now become a major challenge for the civic agencies, particularly in the larger cities to provide internationally competitive infrastructure facilities to attract the FDIs flowing into India. The inter- city competitiveness to attract FDIs has made the investors even more demanding regarding the performance of the city governments. Consequently, with the Indian market being opened to the World market, decentralisation became inevitable to make the local bodies more accountable to the stakeholders. The larger cities became hub of economic activities because they were able to provide the basic minimum infrastructure requirement for overall development. The increasing flow of investments into the city needed adequate infrastructure support in the form of transport, basic amenities and housing. As a consequence, there was a need to devolve powers and authorities to the lower tiers of government- the municipal bodies that are largely responsible for the provision of infrastructure facilities within city limits. However, decentralisation has its in built negative implications as well. Studies over the World have revealed that devolving fiscal powers to lower tiers of government aggravates regional disparity. Moreover, uncontrolled borrowing powers to local bodies might lead to increased debt burden on the National Government.

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Decentralisation in India

Municipal administration in India has a fairly long history. Some form of municipal authority appears to have been in existence during the period of Indus Valley Civilisation. More comprehensive initiative towards this end was adopted during the British period. The Charter of James II in 1687 empowered the establishment of municipal corporations by East India Company. By 1726, Mayor's Courts were established in the Presidency Towns of Madras, Bombay and Calcutta. The decentralisation initiative- devolving powers, functional responsibilities and authorities to the urban local bodies in India virtually started with the Seventy- fourth Constitution Amendment Act 1992 that came into effect from 1st June 1993. However, starting from the Royal Commission on Decentralisation in 1906, a number of Commissions and Committees have been appointed both by the Central Government and various State Governments for examining various issues relating to municipal affairs. Concern had been expressed from time to time at various meetings of the Central Council for Local Government and Urban Development in the Conference of All India Council of Mayors (AICM). Thus in 1962 a resolution passed at the 2nd Meeting of the AICM, it was proposed that "…… the Central Government should appoint a Commission to study the existing patterns of Municipal Corporations Act; evolve broad principles of corporate city improvement in India and draft a model legislation for all corporations in India. However, Decentralisation as it is through the Constitution Seventy- fourth Amendment Act, 1992 (CAA) is considered to be a watershed development in urban policy initiatives in India. This is due to the fact that for the first time in the history of urban governance, the municipal bodies were provided the Constitutional Status of the third tier of government. It is however, well known that the local governments in India are confronted with poor finances, over- controlled local governance and multiplicity of agencies often with overlapping functional and geographical jurisdictions. With the increase in responsibilities as a result of the devolution of eighteen functions through the 12th Schedule of the 74th CAA, empowerment of the ULBs became inevitable. Moreover, the decline in the budgetary support from the higher tiers of Government, as a result of the second generation of reforms that aimed at reducing state fiscal deficits, made devolution of powers to ULBs imperative. It is more than a decade that the decentralisation initiative is in place after the second generation of reforms triggered during the early nineties.

The basic objective of decentralisation as one can deduce form the earlier discussion is to empower the municipal bodies both administratively as well as financially. Moreover, it also aims at analysing the impact on municipal service delivery. However, much of the discussion on decentralisation reflects a curious combination of strong pre-conceived beliefs and limited empirical evidence, particularly in developing countries (Litvak, Ahmad and Bird 1998). As a result, the objective of the present paper is to analyse the impact of the decentralisation initiative in India on the resource mobilisation capacity of the municipal bodies and the mechanism for financing urban basic services. In this context, the views would be duly substantiated by empirical evidence. In doing so the decentralisation process is captured through a decentralisation index constructed for the purpose. A major issue in analysing the impact of decentralisation is the fact that it is not defined easily. It takes many forms and has several dimensions. Keeping in view the limitation of information available in Indian context, the study would take into account all the possible ways of capturing the decentralisation initiative. With this background the present paper is an attempt to analyse some of the implications of decentralisation as it happened in India.

Literature has revealed that Decentralisation has three broad implications. These are mobilisation and allocation of public resources, service delivery and macro- economic stability. The present study analyses the impact of decentralisation on resource mobilisation capacity of municipal bodies both w.r.t to tax and non- tax revenue. Further, the impact of decentralisation is analysed on the role of state government, domestic financial institutions and bilateral and multilateral agencies towards providing funds for basic services. In the absence of adequate data from any other domestic financial institutions, the Housing and Urban Development Corporation (HUDCO) Ltd. has been considered to be the representative of these institutions. Other than the Life Insurance Corporation (LIC) of India, not many of these institutions are involved in financing urban basic services. However, LIC's role has also remained insignificant particularly after HUDCO started funding urban infrastructure projects in 1989-90. LIC's role was more as a result of governments' commitment towards some priority sectors. To address the issue in a systematic fashion, the paper has been divided into following five sections. The introductory discussion is followed by a discussion of the conceptual and theoretical issues in measuring decentralisation and the relevance of the decentralisation index in the current context. The third section discusses the trend and pattern of investments undertaken for financing urban basic services. In this context, the paper would discuss the pattern of expenditure by the Government, domestic financial institutions like Housing and Urban Development Corporation (HUDCO) and donor agencies. The fourth section studies the impact of the decentralisation on the pattern of financing urban basic services in India. This is done by developing a pooled model of cross section and time series data of the financing pattern of urban services in India. The impact has been measured through a decentralisation index developed for the purpose. The fifth section similarly analyses the implication of decentralisation on the resource mobilisation capacity of the municipal bodies. This is done for all the three tiers of local bodies, i.e, nagar panchayats, municipalities and municipal corporations as defined in the 74th CAA. The sixth and the final section summarises the results of the analysis.

Section II
Measuring Decentralisation- Conceptual Issues

The issue of conceptualization and measurement of decentralisation have raised several debates among the scholars. The problem lies with the fact that, very often, operational indicators are designed without reference to any clear conceptual definitions. As a result, various decentralisation measures have been constructed based on the legal, functional and financial aspects. Stephens (1974), Stonecash (1981, 1985) and Zimmerman (1981) provide decentralisation with respect to financial, functional and legal aspects of the states and the local governments of the United States. To devise an operational measure of decentralisation one has to capture the meaning of the very concept. "Decentralisation implies that the sub-national (or sub-state) units of governments have the discretion available to them to engage in effective (as opposed to illusory) decision making affecting their area". Concepts of local autonomy and their discretion are keenly attached with this concept. At the same time, it is a behavioral concept that can, presumably, be affected by structural chacteristics, e.g., local government, informally having high degree of discretion, can be considered decentralized, despite lying in a highly centralized system.

Surveys on the local decision making processes are often used to build up the information base, which is brought closer to the conceptual meaning for the construction of operational measures of decentralisation. As a result, certain degree of subjectivity normally involved in the survey process affects the actual measure. Nevertheless, most studies find the behavioral measures of decentralisation more reliable as compared to the legal and structural measures. According to Oates, "Fiscal Measures are a reasonably satisfactory proxy for what really needs to be measured, namely, the amount of independent decision making power in the provision of public services at different levels of governments". Local spending as a percentage of total (i.e., state and local) spending and own revenue of the local government as a percentage of total own revenue of the state and local government are most commonly used as fiscal (behavioral) measures of decentralisation.

These behavioral measures have their own drawbacks. Firstly, the grant component, both in local spending and revenue, creates the technical problem of double counting and to avoid this problem grants are usually counted as expenditure by the recipient government (when spent) but not by the granting government. The type of tied grant, on the other hand, limits local governments' discretion in using it and thus hampers the very essence of the process of 'independent decision making'. This problem may be countered by separating out general grants from conditional or tied grants. In other words, a break up of grants into tied and untied grants could reflect the local governments' expenditure autonomy. Thus Decentralisation can be measured from two perspectives- legal or administrative perspective and fiscal or financial perspective. Varied indices of decentralisation have been used in several European and North American context. However, in the Indian context, very few studies have been conducted mainly due to lack of availability of functional and financial data of municipal bodies.

Measuring Decentralisation in Indian Context

The initiative by the Eleventh Finance Commission (EFC) was the first towards measuring decentralisation in Indian context. Decentralisation, as envisioned in the Seventy- fourth Constitution Amendment was taken as an important criterion that commanded 20% weight in estimating the amount of EFC grants to the states for the municipal bodies. [1]The EFC measured decentralisation on the basis of the following criteria:

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[1] The other criteria, used for the devolution of EFC grant to the states for the ULBs, are urban population (40 %), geographical area (10%), distance from highest per capita gross state domestic product (20%), own revenue

- Enactment of state municipal legislation in conformity with the 74^{th} CAA, 1992.
- Intervention/restriction in the functioning of the municipalities.
- *De-jure* assignment of functions to municipalities vis-à-vis the Twelfth Schedule of the Constitution of India.
- *De-facto* assignment of functions to municipalities by way of rules, notifications and orders of state government
- *De-jure* assignment of taxation powers to municipalities.
- Exercise of taxation powers by municipalities.
- Constitution of Finance Commission of states and submission of action taken reports.
- Action taken on the major recommendations of the Finance Commission of states.
- Election to the municipalities.
- Constitution of the District Planning Committees.

But, the entire process was not transparent. Moreover, there is no particular agency being assigned the responsibility of collecting and documenting the data related to the above-mentioned criteria. Oomen (1998) evaluated the progress towards fiscal decentralisation on the basis of the report of the State Finance Commissions of Kerala, Punjab and Rajasthan. He used the following ratios for the purpose-

(i) expenditure decentralisation which is percentage of local government spending to total state government expenditure,

(ii) revenue decentralisation ratio which means the percentage of locally raised revenue to total state government revenue and

(iii) financial autonomy ratio which is the locally raised revenue to the total local expenditure.

The study noted that in 1996-97, the decentralisation ratio deteriorated in two states, except, Kerala. It also observed that compared to the industrially developed countries where local governments normally accounted for 20 to 35 percent of the total government spending, the fiscal decentralisation in India remains a distant goal. The process of rural fiscal decentralisation in India is depicted in a study with the help of certain indicators of fiscal decentralisation, for example, expenditure decentralisation. Expenditure decentralisation is defined as the ratio of expenditure of Panchayati Raj Institutions (PRIs) to total rural expenditure by PRIs, state and central government. Revenue decentralisation is similarly, defined as the ratio of own revenue of PRIs to total own revenue of local, state and central government generated from rural India (Jha 2002)

Construction of Decentralisation Index- Some Germane Issues

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efforts of municipalities in a state (5%), using state's own revenue as an indicator and own revenue efforts of municipalities in a state using gross domestic product as an indicator (5%). [Report of the Eleventh Finance Commission, June 2000]

In this section, we try to delineate the decentralisation process in urban India across various states. As it has been mentioned earlier that the concept of autonomy, both with respect to expenditure responsibilities and revenue generation capacity, of the local government is crucial to the concept of decentralisation. However, one of the implementation rules for fiscal decentralisation as tabulated by Bahl (2001) puts devolution of financial powers as a follow- up measure to functional devolution. On the revenue side, a measure of autonomy must capture the extent to which local bodies can raise their revenue independently while on the expenditure front a measure of autonomy must reflect the extent of the right and the capacity of the ULBs to allocate their resources.

The concept of revenue autonomy is very much useful and it is defined as the share (or ratio) of own income (tax as well as non-tax) of the ULBs to the total income. Transfer or grants from the higher levels of government are the second important constituent of the revenue of the ULBs as they enhance the weak financial capacity of the municipalities on the one hand and present incentives for ULBs to increase their income on the other. Here the concept of revenue dependency comes into the picture, which is defined as the share of grants in the ULBs' total income. From the very definition, it is discernible that these indicators help us to understand the dependence of the ULBs on the higher levels of governments to meet their expenditure needs. Revenue autonomy and revenue dependency are the two sides of the same coin in the sense that if revenue from own sources rises, the relative share of grants in the total income of the ULBs falls and vice-versa. This has been established by a comparative study of 31 developing and OECD countries that find a stable negative relationship between sub-national fiscal autonomy and dependency. But, it is important to note here that in India, for PRIs, a fall in revenue autonomy is coupled with a fall in the revenue dependency in the nineties implying, thereby, that sources of income other than own revenue and grants have become more important. Shared taxes and loans, with the latter raising the debt liabilities of the PRIs in the future, are the main constituents of those 'other' sources. [Jha, 2002]

A break up of grants into tied and untied part and, then, the ratio of untied grant in the total grant could provide us some more insight into the aspect of local government autonomy. In recent years another important development, having serious implications for the financial arrangement of the ULBs, is the proposition of alternative modes of finance through the public private partnership and accession of capital market funds. [Bagchi, 2001] Hence the indicator referring to the right and capacity of the local government to access capital market could, also, reflect the local autonomy. But the lack of availability of appropriate fiscal data of the ULBs, in the Indian context, comes into the way of analyzing the above two indicators. On expenditure side, we try to evaluate the decentralisation process by constructing an indicator, depicting share of ULBs' revenue expenditure funded out of their own revenue. Another indicator giving the percentage of local expenditure under ULBs' discretion could be useful to capture successful and effective decentralisation. But, again non-availability of relevant data restricts our study.

Measures of Decentralisation Used in the Present Study

In this context, we also construct two decentralisation indices. Revenue expenditure decentralisation index which is defined as the ratio of revenue expenditure of the ULBs to total expenditure for overall urban development by the ULBs, state governments and the central government[2]. Revenue decentralisation is, similarly, defined as the ratio of own revenue of the ULBs to total own revenue of local, state and central governments generated from the urban areas[3]. However, the impact of decentralisation has been studied by constructing a composite decentralisation index which is basically a weighted average of the revenue decentralisation (RDI) and revenue expenditure decentralisation (EDI) indices. Moreover, certain parameters capturing the legal and administrative processes of the ULBs have been taken into account and incorporated in the model to capture the overall process of decentralisation in India as implemented through the 74th CAA, 1992. Some of the legal and administrative parameters as required in the 74th CAA and subsequently incorporated in the state municipal legislation for measuring decentralisation in India have been discussed in the following section.

Legal/Administrative Index of Decentralisation

The 74th CAA, 1992 assumes very special significance as it has brought about some principal changes in the urban fabric of India. But, the limited availability of secondary data on the changing perspectives limits the construction of administrative/ legal index of decentralisation. Constitutional stipulation regarding the regularity of elections, in the 74th CAA, is an important step towards the recognition of peoples' voice and, hence, the implicit incorporation of them into the municipal governance system. The states having two rounds of municipal elections after 1994[4] are assigned a numerical score of 2. Similarly, a numerical score of 1 is assigned to the states having only one round of municipal election since 1994.

The 12th Schedule (a part of 74th CAA) proposed a functional domain for the ULBs. Still, in many states the functional domain of the ULBs continues to be equivocal. The basic rule for fiscal decentralisation for efficient devolution of powers to lower tiers needs that devolution of funds should follow devolution functions of functions. As a consequence, tardy devolution of functional responsibilities on the one hand impinges the crux of the decentralisation process and on the other hand delays financial devolution. The progressiveness in the direction of devolution of functions to the municipalities as per the 12th Schedule by the state government is enamored in a numerical scale of 0 to 5. The states, who have fully devolved the functional responsibilities in the spirit of the

[2] We take central government's revenue expenditure net of its expenditure on account of grants-in-aid and contributions to the states and union territories. Similarly, for obtaining state governments' revenue expenditure we subtract the compensation and assignment to the local bodies and PRIs and grants-in-aid and contribution from their total revenue expenditures.

[3] Own revenue of the state governments and central government is net of shared taxes, transfer of grants and disbursements from other than the central government.

[4] The 74th CAA, 1992 came into force on 1st June 1993. The constitutionally stipulated deadline for passing the Conformity Legislation for all the state governments was 1st June 1994.

Schedule, are attributed a numerical score of 5. In the same scale, the states, for which the difference between the functional responsibilities to be devolved and what are actually devolved is greater than or equal to 7, receive a numerical score of 0. Similarly, scores of 4, 3, 2 and 1 are assigned respectively for a difference of 1, 2, 4 and 6 between the Constitutional list of functions to be devolved and actual devolution.

Table 1: State Level Decentralisation Indices**

States	A	B	C	D	E	F	G##	H
Andhra Pradesh	2	2	5	0	0	NA	0.24	0.200
			(6 months)*	10#				
Assam	1	1	5	9	1	NA	0.02	0.138
			(1 month)*	9#				
Gujarat	2	1	0	2	1	0	0.56	0.147
			(Not Submitted)	5#				
Haryana	2	2	0		0	NA	0.07	0.200
			(Not Submitted)					
Himachal Pradesh	1	1	5	4	1	NA	0.02	0.154
			(5 months)*	1#				
Karnataka	1	2	3	3	1	1	0.11	0.146
			(14 months)*	2#				
Kerala	2	2	4	5	1	1	0.08	0.147
			11 months)*	0#				
Madhya Pradesh	2	2	4	3	1	NA	0.11	0.163
			(8 months)*	2#				
Maharashtra	1	2	1	1	1	0	2.26	0.170
			(26 months)*	7#				
Orissa	2	1	4	0	1	0	0.06	0.181
			(7 months)*	15#				
Punjab	1	2	4	4	0	NA	0.29	0.165
			(9 months)*	1#				
Rajasthan	2	2	5	0	1	0	0.27	0.185
			(3 months)*	15#				
Tamilnadu	1	2	5	5	1	1	0.46	0.148
			(5 months)*	0#				
Uttar Pradesh	2	2	3	4	0	1	0.12	0.155
			(13 months)*	4#				
West Bengal	2	2	4	5	1	1	0.45	0.148
			(8 months)*	0#				
A: No. of municipal elections held after 1994								
B: Constitution of State Finance Commissions								
C: Promptness in the execution of action on the basis of SFC Reports (Not Submitted:0; 0 to 6 months:5; 6 to 12 months:4; 12 to 18 months: 3; Over 18 months:2								
D: Progressiveness in devolution of functions as per 12th Schedule of the 74th CAA (Complete devolution:5; difference (#) of 1:4; difference of 2: 3; difference of 4 & 5:2; Difference of 6 & 7:1;								

Difference of Over 7:0;
E: Constitution of the District Planning Commission (Already Constituted:1; Not yet constituted:0
F: Constitution of Metropolitan Planning Committee (Already Constituted or at least enacted legislation: 1; Otherwise: 0)
G: Financial Index of Decentralisation (Ratio of own revenue of municipal bodies to total own revenue of the municipal, state and Central Government generated from the urban areas (as in 1997-98)
H: Composite Score of Decentralisation (weighted average of A, B, C, D, E, F and G)
**: Position as in 2001
*: No. of months taken to submit the Action Taken Report; #: Difference between devolution as per Constitutional provision and actual devolution; ##: As in 1997-98 since data pertaining to this is not available for later years.

Source: Eleventh Finance Commission Report; Singh (2001); Sivaramakrishnan (2000); NIUA Research Study Series 70 (1998)

The mandatory constitution of the Finance Commission by the state governments once in every five years is the only positive feature of the 74th Amendment pertaining to the finances of municipalities. The states, which have already constituted the second generation of Finance Commissions, obtain a numerical score of 2. On the other hand, the states only having first SFCs constituted are given a score of 1. In this context, we also evaluate the states on the basis of their promptness in the submission of Action Taken Reports (ATR) on the basis of report submitted by the respective SFCs. In a numerical scale of 5, states are assigned a maximum score of 5 for submitting their ATR within six months of submission of SFC report while the states, which is yet to submit it's ATR, get a score of zero. Similarly, scores of 4, 3, 2 and 1 are assigned for submission of ATRs within a period of 12, 18, 24 and 30 months respectively.

The Constitutional stipulation of fresh elections to municipalities within six months after supersession and a specified normal period of five years for the elected members of the municipal bodies provides for the Constitutional right to exist for these bodies. But, as mentioned earlier, that one of the major shortcomings of the 74th CAA is that it did not specify the time limit for establishing new genre of local bodies, after the Amendment came into force. Despite constituting Election Commissions in the states, very few states held elections within prescribed time limit. [Sivaramakrishnan, 2000] Tamil Nadu held the election in 1996 only. In all the states under consideration, except Karnataka, Maharastra and Tamil Nadu, there were two rounds of municipal elections and, so, they have been assigned a score of 2 as compared to 1 received by the aforesaid states. The Constitution Amendment provided an excellent opportunity to clearly delineate the functional domain of the municipalities. But, very few states have, indeed, utilized this opportunity. Only the states of Kerala, West Bengal and Tamil Nadu have made a comprehensive law devolving functions to the municipalities. [Sivaramakrishnan, 2000; Singh, 2001] These states have been assigned a full score of 5. In the same scale, Karnataka and Madhya Pradesh get a numerical score of 4 and 3 respectively, reflecting their moderate progressiveness in devolving functions to the municipalities. Andhra Pradesh on the other hand has devolved only 8 of the functions listed in the 12th schedule to the municipalities and, hence, receives a score of 0.

Most of the states constituted the Finance Commissions and submitted their report. There has not been any reluctance in this regard presumably because states hoped this would facilitate increased central assistance. SFCs are constituted once in five years and their second term was due in 1999. All the above-mentioned states, except Gujarat, have set up second generation of SFCs and they are assigned a numerical score of 2 and Gujarat receives a score of 1. But, as mentioned earlier, the enthusiasm that was shown by the state governments in constituting the SFCs lacked at the time of implementing the recommendations therein since the implementation of those recommendations would have put substantial pressure on the finances of the states already suffering from huge deficits. However, we try to ascertain the responses of the state governments by evaluating their promptness in submitting the ATRs. Andhra Pradesh and Tamil Nadu submitted the ATRs within six months of submission of SFCs' reports and are assigned a maximum score of 5. But states like Maharastra took 26 months to submit the ATR and, hence, get the score of 1 in the scale of 5. Gujarat has not submitted the ATR yet and receives a score of 0. West Bengal and Madhya Pradesh submitted their ATR within 8 months and hence are assigned a score of 4. The financial index of decentralisation is the ratio of own revenue of the municipal bodies to total own revenue of the local, state and and the Central Government generated from the urban areas. The composite decentralisation score (index) is a weighted[5] average of the individual decentralisation features as mentioned in Table- 1. Putting more weights to the financial indicators of decentralisation has changed the comparative positioning of the states so far as the response to decentralisation is considered. Andhra Pradesh, Haryana, Orissa, Rajsthan and Maharashtra seem to be on the higher side in the context of response to financial, administrative and political decentralisation. However, as a whole, India experienced lackadaisical implementation of the decentralisation initiatives as one can derive from the above analysis.

Section III

Financing Urban Basic Services: Trend and Pattern

Urban basic services in general and urban water supply and sanitation (UWSS) sector in particular has severely under-performed against expectations in India. Inadequate quantity and inferior quality of UWSS has deleterious impact on the urban population by increasing their morbidity and also resulting in decline in the labour efficiency. Environmental implications relating to the inadequacies of urban services can, also, be well understood. In other words, these developments have serious macro- economic implications as well as repercussions for the overall growth prospect of the economy. This problem assumes greater significance in the context of adoption of New Economic Policy (NEP) by the Government of India in an attempt to integrate the Indian economy with the rest of the world and, hence, in the process to achieve higher economic growth. Quite understandably, the urban centers have a major role to play in the process and thus put tremendous pressure on the level of basic amenities. Consequently, a substantial amount of investment is needed to augment the facilities related to environmental services, for keeping pace

[5] The weights are based on the extent of importance to each indicator as revealed through discussions with the municipal officials and elected representatives at various points of time. The weights are A= 20%; B= 20%; C= 20%; D= 10%; E= 5%; F= 5% and G= 20%

with the demand for the same. In this regard, the present section would try to understand the nature and extent of investments in basic amenities.

Financing of basic amenities in India has largely remained within the purview of public sector. Though the state governments largely made the required capital investments in projects related to basic amenities, the maintenance of the utilities were the responsibility of the city governments. As a consequence, there was an urgent need for financial strengthening of urban local bodies. Before going into the detail analysis of the implications of decentralisation on financing urban basic services in India, this section would discuss the trends and pattern of expenditure undertaken by the Central Government and state governments. It would also discuss in detail the role of financial institutions in financing urban development in general and urban basic services in particular. The fundamental differences between the financing of infrastructure projects and that of other industrial activities accrue to the basic features of these services. Public policies and plan documents of most developing countries consider these services as "public utility service". Some of the inherent characteristics of these services, like, externality, non-excludability, inelastic price demand, huge capital investments with long gestation period, uncertainty of return etc. force them to remain within the purview of the public sector. As a consequence, the very idea of private sector involvement in the provision of these services is considered to be an anathema (Bagchi 2001).

During the pre independence period, the central government was not interested in making capital investments for the provision of these services. The then city governments were not financially strong enough to take responsibilities for these provisions either. British government was also reluctant in improving city governments' financial position as the later were thought to be the stronghold of the national movement for independence. So, the government relied on local agencies that could share the costs for major capital projects. These resulted in gloomy state of basic amenities ever since the pre independence period. However, in the post independence period, these services began to be provided by the local governments and parastatal agencies developed for specific purposes. Broadly, the state governments through (a) own departments (e.g., Public Works Department/ Urban Development Department), (b) state level boards (e.g. WS&S Boards/ housing boards etc.), (c) statutory and non-statutory bodies at the city level (e.g., Metropolitan WS Boards/ Development Authorities) and (d) local bodies, undertook the responsibility of providing these services. Specifically, given the possibility of two-part system of responsibilities, the capital works for these services, in many states are undertaken by the concerned state government departments whereas the maintenance responsibility lies with the local governments. However, there are larger municipal corporations in the states that are yet to abolish octroi which also undertake capital investment financing for these services.

State plan funds and budgetary allocation are the major source of fund for the capital investment in water supply, sewerage and other municipal services. Largely it is the state level boards that are normally responsible for executing the state and central projects. For projects undertaken by the boards on behalf of the municipal bodies, the responsibility of arranging funds is that of the latter and these are financed normally through a combination of loans and grants. Grants are provided by the state government while loans come from the government owned financial institutions, like, LIC, HUDCO etc. The institutional finance for the urban basic services is a very recent phenomenon and limited in volume. Normally, government owned Development Finance Institutions (DFIs) provide financial assistance for this purpose. This type of financial arrangement is characterized by 'directed credit regime' in which different financial institutions are mandated to invest in specific priority sector. However,, with the opening up of the economy, the distinct division that existed between a bank and a DFI gradually seems to be abolished. Also, the high statutory liquidity ratio requirements for the banking sector made funds available for priority purposes. Another important development in the context of ongoing financial sector reform is the 'compulsion' before the DFIs to mobilize resources through market borrowing without government guarantees. In the urban sector, however, this has been true to a limited extent for the HUDCO only (Bagchi 2001).

State Government Expenditure: Trend & Pattern:

The analysis in this section focuses on making a pre and post decentralisation comparative assessment of state governments' expenditure on Urban Development (UD), in general and urban water supply (UWS) sewerage and sanitation and assistance to municipal bodies[6], during the decade of nineties. We divide the entire decade of nineties into two sub-periods: pre decentralisation period (1990-91 to 1994-95)[7] and post decentralisation period (1995-96 to 1999-00) in an attempt to capture the comparative role of state governments during the pre and post decentralisation phase.

Table 2 provides the per capita (PC) expenditure on UWS during both the pre and post decentralisation period. The corresponding growth rates during these two periods are provided in Table- 3. Out of 17 states, 8 states have experienced decline in the growth rate of PC expenditure on UWS in the post decentralisation period. Tamil Nadu, West Bengal, Rajasthan and Assam have registered significant decline in the growth rate in the later sub-period. In real terms, also, PC expenditure on UWS for the above-mentioned states has shown decline. On the other hand, states of Andhra Pradesh, Goa, Gujarat and Orissa have recorded an increase in the real PC expenditure on UWS during the later sub-period. Among them, this increase is maximum for Orissa. Interestingly, states like Karnataka, Kerala and Punjab have not incurred any direct expenditure, specifically, for these purposes.

Table- 2: State Government Expenditure on Urban Development & Urban Services

	PC Expenditure on UWS			PC Expenditure on UD			PC Expenditure on Assistance to LBs			PC Expenditure on UWSS		
	1990-91	1995-96	1999-00	1990-91	1995-96	1999-00	1990-91	1995-96	1999-00	1990-91	1995-96	1999-0
Andhra Pradesh	9.03	8.57	8.46	21.88	10.79	5.14	0.13	2.60	2.11	9.88	13.64	15.2
Assam	4.51	5.12	3.63	16.61	29.72	21.33	0.00	0.00	0.00	27.89	14.44	16.0

[6] various state governments provide assistance to local bodies for water supply, sanitation and sewerage purpose. But, no further (rural/urban) break up, relating to state governments exclusively to the ULBs, is available in the Finance Accounts, which forces us to study this assistance as a whole.

[7] Though the 74th CAA came into force on 1st June 1993, it is assumed that it might have taken at least a year for it to have some impact.

Bihar	7.80	11.18	15.36	9.44	7.17	21.68	0.33	0.42	1.26	8.93	6.67	6.4
Goa	222.42	216.50	226.81	38.97	41.76	35.88	0.00	0.00	0.00	64.03	106.14	138.4
Gujarat	1.45	2.42	4.00	16.14	18.30	39.31	0.00	0.00	0.00	12.42	13.23	38.8
Haryana	0.00	14.64	0.00	11.74	22.82	27.54	0.00	0.00	0.00	17.85	34.30	31.0
Himachal Pradesh	188.81	237.98	0.00	34.98	53.17	48.66	4.50	23.10	0.00	80.89	101.93	0.0
Karnataka	0.00	0.00	0.00	8.12	30.60	16.25	21.84	41.85	50.32	8.48	17.67	19.9
Kerala	0.00	0.00	0.00	4.60	6.58	50.98	0.00	0.00	0.00	14.12	13.00	14.7
Madhya Pradesh	9.82	6.34	6.76	22.63	16.12	20.96	1.51	2.62	2.52	15.66	17.42	18.0
Maharastra	1.00	0.22	0.21	17.67	30.04	22.88	12.32	3.58	29.37	16.85	14.83	21.6
Orissa	21.30	18.04	34.48	23.37	20.92	35.61	2.26	12.16	6.80	9.67	15.19	19.2
Punjab	0.00	0.00	0.00	-2.85	13.13	14.20	0.00	0.00	0.00	12.03	17.81	13.9
Rajasthan	74.95	114.57	93.80	10.82	17.45	86.16	1.28	2.23	1.98	37.08	54.70	49.3
Tamil Nadu	21.29	19.06	6.18	22.81	12.50	16.32	1.82	2.82	2.20	16.50	17.27	14.7
Uttar Pradesh	5.84	7.45	0.00	4.85	4.12	6.18	2.38	0.16	0.00	9.28	6.44	0.0
W.B.	2.24	2.19	1.13	57.67	41.71	104.36	0.00	0.00	0.00	6.44	6.84	11.7
India	0.03	0.69	0.80	3.31	0.73	2.02	0.09	0.00	0.03	0.77	1.78	2.0

Source: State Finance Accounts for Corresponding Years

The trend in PC expenditure on UD as shown in Table 2 reveals that the PC expenditure on UD by eleven of the seventeen states have shown higher growth during the post- decentralisation period. Among them the increase have been substantial for the states like Bihar, Gujarat, Kerala, Orissa, Punjab, Rajasthan, West Bengal. In the post decentralisation period, Rajasthan and Kerala heavily increased their expenditure on UD. On the other hand, states, like, Andhra Pradesh, Assam, Karnataka, Maharastra and Tamil Nadu have recorded a decline in the PC expenditure on UD in the post decentralisation period. The same trends get reflected in the real PC expenditure at four points of time. Broadly, one can thus conclude that most of the states have been continuing to play a major role in the financing of projects related to UD. The expectation that decentralisation initiatives would reduce the fiscal burden of the various state governments has come out as a distant reality.

Most of the states, including the states that do not spend at all for UWS and sanitation-sewerage facilities, provide some assistance to the local bodies (both rural and urban) for this purpose. In states like Andhra Pradesh, Karnataka, Madhya Pradesh, Orissa, Tamil Nadu, Rajasthan the PC assistance has declined in the second sub-period, while in Bihar, Maharastra it has increased significantly (Table 2). Variations in the growth rates of PC assistance between the two sub-periods, also, confirm the above scenario. The trend in PC expenditure on water supply, sewerage and sanitation by the various state governments is shown in Table- 2. In as many as six states, (i.e. Bihar, Gujarat, Kerala, Maharastra, Orissa and West Bengal), there has been a decline in the level as well as growth rates of real PC expenditure. This trend is in conformity with the trend of PC expenditure on UWS and sanitation facilities. It is also evident from the above analysis that the states that have reduced their expenditure on UWS schemes, provided more assistance to local bodies for urban schemes.

Table- 3: Pre and Post- Decentralisation Growth in State Expenditure

	PCE on UWS		**PCE on UD**		**PCE on Asst. to LBs**		**PCE on UWSSS**	
STATES	**90-91 & 94-95**	**95-96 & 99-00**	**90-91 & 94-95**	**95-96 & 99-00**	**90-91 & 94-95**	**95-96 & 99-00**	**90-91 & 94-95**	**95-96 & 99-00**
Andhra Pradesh	5.13	10.01	-7.49	-8.59	155.27	5.17	15.61	8.44
Assam	0.82	-11.94	4.61	-8.97	0	0	-17.38	2.75
Bihar	19.8	8.51	-9.34	24.1	-30.02	34.59	-7.27	-1.52
Goa	-2.48	1.38	-4.43	-2.37			9.03	8
Gujarat	-2.37	11.03	-8.34	23.21			15.78	33.66
Haryana	167.3	8.07	0.75	4.17			29.72	-4.15
Himachal Pradesh	2.97	0	-1.2	0.84	68.66	0	2.92	
Karnataka	0	0	3.84	-18.02	15.32	5.23	15.56	1.4
Kerala	0	0	5.48	56.31			-2.61	2.6
Madhya Pradesh	-0.06	-0.24	-11.85	3.64	7.03	-7.83	5.71	0.8
Maharastra	-0.87	-4.59	-0.16	-5.4	-14.3	63.31	-4.39	10.13
Orissa	-3.24	20.12	-4.7	12.84	23.53	-8.34	7.19	8.37
Punjab	0	0	-16.8	10.74			0.57	-4.54
Rajasthan	11.79	-1.33	-2.52	71.4	5.73	-3.82	7.88	-0.28
Tamil Nadu	18.47	-34.99	-18.38	-2.41	14.13	-6.93	10.57	-6.95
Uttar Pradesh	0	0	-10.59	0	-37.05	0	-8.19	
W.B.	14.39	-15.82	-2.3	22.41			8.8	16.22

Source: State Finance Accounts for Corresponding Years

HUDCO and Financing of Urban Infrastructure

The institutional finance for urban infrastructure is relatively recent and limited in character. Gradually changing organizational structure for managing urban infrastructure and the supporting financing system, during the second half of the nineties, has increased the importance of the institutional finance. Cost recovery, financial viability, accountability etc. have become keywords in this framework. Substantial reduction of the budgetary allocation and, hence, adherence of low priority to socially desirable but financially unremunerative schemes having a substantial component of subsidy are the important features of this changing policy perspective. But the pressure of the growth of the urban settlements on the urban infrastructure in general and urban basic services in particular induced the Government of India to entrust the task of financing urban infrastructure to HUDCO which is currently the leading public financial institutions. In 1989-90, HUDCO opened infrastructure finance window to provide financial assistance for the urban infrastructure projects.

HUDCO finances up to 85 percent of the project cost in case of public agencies and 100 percent in case of direct borrowing by the Government. Where as for the private and co-operative agencies it finances 70 percent of the cost. The loan can be repaid within a period of 5 to 15 years, with different rates of interest, which increase with the duration of the repayment period. Specifically, structure of interest rates depends on the type of the urban infrastructure schemes. In recent past, the interest rates have moved between 16.5% and 19% for commercial purposes depending on the nature of the agency. The interest rates for urban utility infrastructure for all cities range between 15% to 16%. However, it is important to note here that, these rates were much lower when HUDCO opened its infrastructure finance window. Increased cost of resource mobilisation, stoppage of equity support from the government, compulsions for making the infrastructure projects financially viable have forced HUDCO to reduce the amount advanced to some of its social sector projects and/or charging higher interest rates. (Kundu et.al., 1999). The financial discipline imposed by the RBI has made the state governments restrict their guarantee only to the larger municipal corporations. As a result, the cities with strong economic base that are attracting private investment from within as well as outside the country are also appropriating a disproportionate share of the subsidized HUDCO funds. These trends get reinforced if we analyze the spatial and sectoral distribution of HUDCO loan for the urban infrastructure.

The major areas of operation for HUDCO have always been the urban water supply and sanitation sector since its inception of the infrastructure finance window. Table 4 provides the sector wise disbursal of HUDCO loan for urban infrastructure at the all India and state level during the nineties. In the first twenty years, significant proportions of the total loans were for the urban water supply[8]. In late nineties there has been remarkable shift from urban water supply to other infrastructure projects[9]. Two broad features are revealed from these tables. Firstly, the less developed states like, Orissa, Rajasthan, West Bengal, Himachal Pradesh, Bihar and Assam receive major HUDCO loans for water supply schemes. However, it is not the case for sewerage schemes. On the other hand, developed states like Tamil Nadu, Karnataka, Gujarat and specially Maharashtra are major recipient of HUDCO loans for other infrastructure projects as well as for sewerage schemes.

Table 4 depicts the spatial distribution of urban infrastructure schemes and related loans during the nineties. Four developed states of Gujarat, Maharastra, Karnataka and Tamil Nadu accounted for around 40 percent of the total loans sanctioned by HUDCO[10] However, the share of these states in number of schemes for urban infrastructure projects ranged between 12 and 26 percent during 1970 to 1996. This signifies the relatively higher costs of infrastructure projects in those states. Contrarily, for the backward states, namely, Bihar, Orissa, Rajasthan, Madhya Pradesh and Uttar Pradesh the percentage figure of the loan amount was around 25 percent during 1970 and 1996. The situation further worsened in the late nineties, as the corresponding figure remained around 10 percent. As mentioned earlier, increasing recognition of the cost recovery aspect and consequent adoption of financially viable projects by HUDCO have led to this adverse scenario.

Table- 4: Spatial & Sectoral Distribution of HUDCO Loans

	Share of loans for Water Supply			**Share of loans for Sewerage and Sanitation**			**Share of Loans for Other Infrastructure**		
	1990-91	**1995-96**	**1999-00**	**1990-91**	**1995-96**	**1999-00**	**1990-91**	**1995-96**	**1999-00**
Andhra Pradesh	0.00	90.38	0.00	0.00	9.62	0.00	100.00	0.00	100.00
Assam	72.65	100.00	0.00	0.00	0.00	100.0	27.35	0.00	0.00
Bihar	0.00	100.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00

8 64.7% of total cumulative loans sanctioned during 1970 to 1990 has gone for urban water supply
9 which include loan for area development, transport and miscellaneous purposes
10 The corresponding cumulative figure for the period between 1970 to 1990 was around 60 percent.

Goa	0.00	0.00	100.00	0.00	0.00	0.00	0.00	0.00	0.00
Gujarat	0.00	0.00	42.39	62.10	0.00	0.00	37.90	100.00	57.61
Haryana	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	100.00
Himachal Pradesh	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Karnataka	0.00	10.10	5.02	0.00	0.00	10.45	0.00	100.00	84.53
Kerala	100.00	0.00	0.00	0.00	0.00	5.96	0.00	27.10	94.04
Madhya Pradesh	0.00	0.00	19.71	0.00	0.00	0.00	0.00	100.00	80.29
Maharastra	9.29	0.00	1.40	5.75	0.00	0.00	84.96	100.00	98.60
Orissa	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Punjab	0.00	80.70	0.00	0.00	60.35	0.00	100.00	31.30	0.00
Rajasthan	0.00	49.17	0.00	0.00	4.60	0.00	0.00	52.85	100.00
Tamil Nadu	100.00	0.00	45.26	0.00	19.72	0.00	0.00	68.89	54.74
Uttar Pradesh	0.00	0.00	0.00	0.00	0.00	0.00	100.00	100.00	100.00
W.B.	100.00	0.00	0.00	0.00	0.00	98.47	0.00	0.00	1.53
India	45.48	12.55	13.13	3.65	8.89	20.36	50.87	61.52	66.51

Source: HUDCO

An analysis of the pre (1990-91 to 1994-95) and post decentralisation (1995-96 to 1999-2000) comparative growth profile of per capita HUDCO loan sanctioned for urban infrastructure is shown in Table- 5. At the all India level, per capita HUDCO loans sanctioned and corresponding growth rate has experienced an increase in the post decentralisation period. Per capita HUDCO loan assistance for the developed states, like Gujarat (substantial increase), Maharastra, Tamil Nadu and Karnataka increased over the years during the nineties. Moreover, some backward states like Rajasthan and Madhya Pradesh also experienced substantial increase in the per capita HUDCO loans sanctioned. However, most of the backward states have registered a decline in the growth of loans sanctioned by HUDCO for urban infrastructure. Hence, the entire analysis corroborates the lax attitude of HUDCO towards the backward states in general and small and medium towns in particular. To be specific, among the backward states the HUDCO's loan assistance has remained confined only to the large cities, particularly to the state capitals.

Table- 5: Pre and Post- Decentralisation Growth of HUDCO Loan Sanction

	PC Loans for UIPs		**Growth**	**PC Loans for UIPs**		**Growth**
	1990-91	1994-95	Pre Decent.	1995-96	1999-00	Post decent.
Andhra Pradesh	4.5	2.24	0	17.05	2.83	-37.63
Assam	26.82	9.13	-44.92	7.53	58.87	0
Bihar	0	0	0	2.5	0	0
Goa	NA	0	0	0	124.98	0
Gujarat	1.92	4.94	0	2.84	32.91	100.91
Haryana	0	0	0	0	88.9	0
Himachal Pradesh	0	0	0	0	0	0
Karnataka	0	86.95	0	7.28	90.23	82.81
Kerala	12.48	82.32	92.75	33.43	78.64	24.48
Madhya Pradesh	0	0	0	0.01	15.48	588.65

Maharastra	18.25	0	0	1.37	32.4	138.78
Orissa	0	0	0	0	0	0
Punjab	2.75	9.36	0	18.94	0	0
Rajasthan	0	16.68	0	27.99	45.86	18.81
Tamilnadu	11.8	14.23	16.52	22.28	58.57	48.59
Uttar Pradesh	2.99	1.42	0	9.8	4.56	-18.45
West Bengal	10.09	0	0	0	66.2	0

UIPs: Urban Infrastructure Projects

Source: HUDCO

External Assistance for Urban Services

From 1980s onwards, external assistance, mainly from the World Bank, and other foreign agencies have been coming in for the urban infrastructure in general and urban basic services in particular. A substantial portion of this assistance, more than 53 percent has been for the urban water supply and sanitation programme (NIUA, 1998). But, the developed states have again turned out to be the major recipient of this assistance. Out of the 15[11] completed externally aided projects, till date, 9 of them are located in the developed states (Table 6). Currently, there are 18 ongoing projects, which are in different stages of implementation. Six of these are located in the developed states. Even, in the backward states, it is only the state capital and/ or the major cities that receive some type of external assistance. (Table 6).

An analysis of Table- 6 also reveals that there are 18 ongoing projects that are at various stages of implementation. One can bring out the following four major features of external aids from the following table-

❖ Firstly, out of a total of 18 ongoing externally aided projects for urban development or improvement/ augmentation of urban services, 15 (83.33%) are in the state capitals.

❖ Secondly, of the total 15 ongoing projects located in the state capitals, 6 (40.00%) are in the state capitals of the developed states of Karnataka, Maharashtra and Tamilnadu.

❖ Thirdly, out of a total of 15 completed projects, 8 (5333%) are located in the developed states. Moreover, 6 (40.00%) of these are aimed for the overall urban development of the state capitals only.

❖ One can observe the decline in the share of externally aided urban development, urban water supply and sewerage and sanitation projects that are aimed towards the whole state from a 60.00 percent (9 out of 16 completed projects) to 16.66 percent (3 out of 18 ongoing projects)

This shows that there has been a significant decline in the share of external assistance for urban development going to the other cities, particularly, the small and medium towns after the decentralisation initiative. The externally aided projects have largely gone to the larger cities as seen from the share of ongoing projects going to the state capitals. Thus, one can very broadly conclude

[11] See www.nic.in for the detail of all these projects.

from the above discussion that in the backdrop of declining public assistance, the flow of external aid for the urban infrastructure projects is a welcome development. However, the backward states and small cities and towns have largely remained out of the domain of the external assistance. Moreover, these funds for the urban development and improvement fo urban services for the state as a whole has also gone down as seen from Table- 6.

Table- 6: Spatial Distribution of Externally Aided Urban Development Projects

	STATE CAPITAL				**WHOLE STATE/ OTHER CITIES**				**TOTAL**			
	COMPLETED		**ONGOING**		**COMPLETED**		**ONGOING**		**COMPLETED**		**ONGOIN**	
	NoP	*%*	*NoP*	*%*	*NoP*	*%*	*NoP*	*%*	*NoP*	*%*	*NoP*	*%*
AP	1	16.67%		0.00%		0.00%		0.00%	1	6.67%	0	0.0
Assam		0.00%		0.00%		0.00%		0.00%	0	0.00%	0	0.0
Bihar		0.00%		0.00%		0.00%		0.00%	0	0.00%	0	0.0
Delhi		0.00%		0.00%		0.00%	1	33.33%	0	0.00%	1	5.5
Goa		0.00%		0.00%		0.00%		0.00%	0	0.00%	0	0.0
Gujarat		0.00%		0.00%	2	22.22%		0.00%	2	13.33%	0	0.0
Haryana		0.00%		0.00%		0.00%		0.00%	0	0.00%	0	0.0
HP		0.00%	1	6.67%		0.00%		0.00%	0	0.00%	1	5.5
Karnataka		0.00%	3	20.00%		0.00%		0.00%	0	0.00%	3	16.6
Kerala		0.00%		0.00%	1	11.11%		0.00%	1	6.67%	0	0.0
MP		0.00%		0.00%		0.00%		0.00%	0	0.00%	0	0.0
Maharastra	3	50.00%	1	6.67%	1	11.11%		0.00%	4	26.67%	1	5.5
Manipur	1	16.67%	1	6.67%		0.00%		0.00%	1	6.67%	1	5.5
Meghalaya		0.00%	1	6.67%		0.00%		0.00%	0	0.00%	1	5.5
Orissa		0.00%		0.00%		0.00%		0.00%	0	0.00%	0	0.0
Punjab		0.00%		0.00%	1	11.11%		0.00%	1	6.67%	0	0.0
Rajasthan		0.00%	3	20.00%	1	11.11%		0.00%	1	6.67%	3	16.6
Sikkim		0.00%	1	6.67%		0.00%		0.00%	0	0.00%	1	5.5
Tamilnadu	1	16.67%	2	13.33%	1	11.11%	2	66.67%	2	13.33%	4	22.2
UP		0.00%		0.00%	2	22.22%		0.00%	2	13.33%	0	0.0
WB		0.00%	2	13.33%		0.00%		0.00%	0	0.00%	2	11.1
TOTAL	**6**	**100.00%**	**15**	**100.00%**	**9**	**100.00%**	**3**	**100.00%**	**15**	**100.00%**	**18**	**100.0**

Source: www.nic.in

Private Participation in the Provision of UBSs[12]:

Private sector involvement in infrastructure services in general and water and sewerage projects in particular has become more of proving a point rather than really looking at this as an alternative mode for financing these services. Some major factors that one can notice regarding private participation in financing urban services are-

[12] See Bagchi (2001) for a detail discussion of public private partnership in financing capital investments in basic amenities as well as maintenance.

❖ These initiatives have largely remained confined to the maintenance of urban basic services through service contract or management contract.

❖ These initiatives have to a large extent remained confined to the developed southern and western states of Maharashtra, Gujarat, Karnataka and Tamilnadu.

❖ Involvement of private investments for financing capital investment in urban services like water supply and sewerage have remained limited.

This is largely due to the fact that the water supply and sanitation sector in the developing countries in general and India in particular, lacks a commercial approach of provision. In other words, these services are largely considered to be public services to be provided free of cost. As a consequence, cost recovery in these services has remained significantly low. Subsequently, the sector has been caught in a vicious circle. Low service levels leads to low willingness to pay as a result low cost recovery. This in turn leads to low funds for investments and subsequently low level of services.

It is because of the above factors, the sector has become absolutely unattractive for private investments. The lack of a commercial approach in the provision of these services has left the sector vulnerable and risk prone. This has ultimately resulted in low level of private investments. However, in the face of inadequate public sector resources to meet the infrastructure investment requirement of cities and towns, alternative financing modes have been explored to some extent. Private sector participation in the provision of urban infrastructure in general and basic amenities in particular is one such mode. Several Indian cities have been experimenting with this mode. Tirupur Water Supply and Sewerage Project (TWSSP) is such an example where a Special Purpose Vehicle (SPV) by the name of New Tirupur Area Development Corporation Limited (NTADCL) was formed through equity contribution from Government of India, Government of Tamilnadu, domestic financial institutions like HUDCO and ILFS, private water utility companies and FIRE- D Housing Guarantee (HG) Program fund[13].

There are 28 water and environmental sanitation related projects in which private public partnership has been initiated. But out of them, 20 projects are in the developed states. Moreover, even if these projects are located in the backward states they have largely remained confined to the state capitals or other big cities of these states. There are 44 projects with private public partnership in solid waste treatment and disposal facilities. More than 50 percent of the projects are again in the developed states. 30 out of those 44 projects are in the big cities. This clearly implies that with the decentralisation initiative in place in the form of 74th CAA 1992, it is largely going to be the larger cities that are going to be benefited out of this. One can attribute this to two basic factors- one political and the other financial or economic in nature. the developed states in general and the big cities in particular have been successful in exploiting the fruits of this type of alternative mode of financing basic amenities.

[13] See Bagchi (2001) for a detail discussion of the Tiruppur WSSP.

Section IV

Decentralisation: Implications for Infrastructure Financing

This section investigates the impact of decentralisation process on the per capita expenditure in urban infrastructure by the state governments[14] and HUDCO. We assume the following univariate models:

$PCEUI_{sg}$= a+bCDI[15] --------------- (1); where $PCEUI_{sg}$ is the per capita expenditure on urban infrastructure by the state governments.

$PCEUI_{hudco}$= a+bCDI---------------- (2); where $PCEUI_{hudco}$ is the per capita expenditure on urban infrastructure by the HUDCO. The results of these two regressions are summerised in Table 7 and table 8. It is evident from the table 7 that decentralisation has a negative impact on the per capita expenditure on urban infrastructure by the state governments. This result, further underpins the fact of declining budgetary support for the projects related to the urban infrastructure. The relevant coefficient is significant at 5-percentage level. In case of per capita HUDCO expenditure on urban infrastructure, also, the impact of decentralisation is negative. But the relevant coefficient is insignificant.

Table 7: Regression Results for Equations 1 and 2

Dependent Variable: Per Capita Expenditure on Urban Infrastructure
Independent Variable: Composite Index of Decentralisation
Method of Regression: GLS

	SG	HUDCO
1	*2*	*3*
CDI	-124.7519	-7.046109
	(-2.191)**	(-0.477)
Constant Term	191.3859	27.42951
	(8.061)***	(4.457)***
No. of Observation	112	112
Wald Chi	4.8	0.23
Prob.> chi 2	0.0285	0.6331

Note: Figures in the parenthesis are the corresponding z-ratios.
***: Coefficients are significant at 1 percentage level
**: Coefficients are significant at 5 percentage level
*: Coefficients are significant at 5-10 percentage level.
SG: State Governments.

In a similar fashion, we incorporate some of the legal/administrative aspects of decentralisation in our model presented in the equation (1) and (2). We redefine them as follows:

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[14] State governments' expenditures on urban infrastructure include expenditure on urban water supply, urban sanitation, urban development and assistance to local bodies, municipalities etc. for this purposes.

[15] For this part of the analysis, CDI= (RDI* Mean RDI of all states) + (EDI* Mean EDI of all states); Where RDI= Revenue Decentralisation Index and EDI= Expenditure Decentralisation Index (these indices have been defined in the earlier sections)

$PCEUI_{sg}$= a+bCDI+D_1+D_2;--------------------(3)

Where D_1=1 for the year in which SFCs has been constituted and the following years

0, otherwise.

And D_2= for the year in which the ATR was submitted and the following years.

0, otherwise.

PCEUI $_{hudco}$= a+bCDI+D_1+D_2;-----------------(4) where dummy variables are defined in the same way as in equation (3).

The impact of decentralisation (fiscal) on state government expenditure in urban infrastructure, again, turns out to be negative and the relevant coefficient is significant at 5-percentage level. But the coefficients of the two dummy variables, despite being positive, are insignificant. In case of per capita expenditure by HUDCO on urban infrastructure, the coefficients corresponding to CDI is negative but insignificant, whereas the coefficients related to the dummy variable representing constitution of SFCs is positive and significant. (??).

Table 8: Regression Results for Equations 3 and 4

Dependent Variable: Per Capita Expenditure on Urban Infrastructure

Independent Variables: Composite Index of Decentralisation, dummy variable (dum1) relating to the constitution of the SFCs and dummy variable (dum2) relating to submission of ATRs.

Method of Regression: GLS

	SG	HUDCO
1	*2*	*3*
CDI	-136.1971	-11.64153
	(-2.420)**	(-0.830)
Dum1	63.08755	38.69651
	(1.419)	(3.492)***
Dum2	38.80724	-9.888495
	(0.588)	(-0.601)
Constant Term	163.2596	13.83058
	(5.876)***	(1.997)**
No. of Observation	112	112
Wald Chi	8.86	13.62
Prob.> chi 2	0.0313	0.0035

Note: Figures in the parenthesis are the corresponding z-ratios.

***: Coefficients are significant at 1 percentage level

**: Coefficients are significant at 5 percentage level

*: Coefficients are significant at 5-10 percentage level.

SG: State Governments.

Section V

Decentralisation: Implications for Resource Mobilisation by ULBs

We use the same Composite Decentralisation Index (hereafter, CDI) used in the previous section [as defined in the earlier section] combining previously derived two decentralisation indices, i.e., RDI and EDI. We calculate the respective mean values on the basis of the numerical values of EDI and RDI for the period covering 1990-91 to 1997-98, for each of the state under the study. Then the following formula has been used to composite RDI and EDI:

CDI= (RDI* Mean RDI) + (EDI * Mean EDI);

Where I=states (14 states)

T= time period (1990-91 to 1997-98)

The CDI, thus, derived is again a financial measure of decentralisation. To appraise the impact, if any, that the decentralisation index has on the resource mobilisation capacity, i.e. on the tax and non-tax revenue, for the each category of the ULBs, the following univariate models have been assumed:

PCTR= a+b CDI------------(1A)

PCNTR= a+b CDI----------------(2A)

The method of regression, used here, is pooled regression[16] and GLS (Generalized Least Square) technique is applied to estimate the coefficients of the model. The results are summerised in Table 9 and Table 10.

Table- 9: Regression Results for Equation 1A
Dependent Variable: Per Capita Tax Revenue
Independent Variable: Composite Index of Decentralisation
Method of Regression: GLS

	NPs	Municipalities	M.Corps.
1	*2*	*3*	*4*
CDI	11.3543	33.48533	143.3211
	(2.647)***	(6.051)***	(4.494)***
Constant Term	6.095522	19.02675	46.21993
	(3.409)***	(8.247)***	(3.476)***
No. of Observation	112	112	112

[16] When dealing with the cross section and time series data, where for the typical case the number of individual is large and the number of time periods is small, so that sharp inferences about the coefficients are not possible, it is a common practice in applied work to pool all the data together, and estimate a common regression. The basic motivation for pooling time series and cross section data is that if the model is properly specified, pooling provides more efficient estimation, inference and possibly prediction. [Gujarati, 1995; Johnston. J & J. Dinardo, 1997]

Wald Chi	7.01	36.62	20.2
Prob.> chi 2	0.0081	0.0000	0.0000

Note: Figures in the parenthesis are the corresponding z-ratios.
***: Coefficients are significant at 1 percentage level
**: Coefficients are significant at 5-percentage level
*: Coefficients are significant at 5-10 percentage level.

Table- 10: Regression Results for Equation 2A
Dependent Variable: Per Capita Non-Tax Revenue
Independent Variable: Composite Index of Decentralisation
Method of Regression: GLS

	NPs	Municipalities	M.Corps.
1	*2*	*3*	*4*
CDI	4.808419	21.21101	71.73847
	(2.558)**	(8.529)***	(11.021)***
Constant Term	3.119182	8.90304	7.035946
	(3.980)***	(8.587)***	(2.593)***
No. of Observation	112	112	112
Wald Chi	6.54	72.75	121.47
Prob.> chi 2	0.0105	0.0000	0.0000

Note: Figures in the parenthesis are the corresponding z-ratios.
***: Coefficients are significant at 1 percentage level
**: Coefficients are significant at 5-percentage level
*: Coefficients are significant at 5-10 percentage level.

It is evident from the Table 9 that the CDI has significant positive impact on the tax revenue generation capacity of each of the category of the municipal bodies. The intensity of impact is greatest for the municipal corporations while the same is the least for the NPs. Each of the coefficients are significant at 1 percentage level.

Table 10 depicts the impact of decentralisation on the non-tax revenue generation capacity of each tier of the ULBs. Here also, the impacts are significant and positive and the intensity of impact ensue the same trend as reflected earlier in case of tax revenue generation capacity. However, the numerical values of the coefficients of the CDI in case of non-tax revenue are less than those for the tax revenue, across the three categories of municipal bodies. Also, the coefficients are significant at 1 percentage level for the municipalities and the municipal corporations. While it is significant at 5 percentage level in case of the NPs. This implies the relative greater impact of the decentralisation process on tax revenue generation capacity as compared to the non-tax revenue generation capacity of the municipal corporations.

In the following sections, we try to improve our model by attempting to incorporate some of the constitutional stipulations (as given in the 74th CAA, 1992) with respect to the ULBs and, thus, capturing, to some extent, the aspect of legal/administrative decentralisation. We redefine our model, as given by the equation (1A) and equation (2A), as follows:

$PCTR= a+bCDI+cD_1+d\ D_2$------------------------(3A)

Where $D_1=1$ for the year in which municipal election was held in each state and the following years since elected municipal governments, legally, have the tenure of five years 0, otherwise.

And $D_2=1$ for the year in which the ATR was submitted and the following years.

0, otherwise.

$PCNTR= a+bCDI+cD_1+d\ D_2$----------------(4A) where the dummy variables are defined as in equation (3). Table 11 and Table 12 summarise the above regression results.

Table 11: Regression Results for Equation 3A

Dependent Variable: Per Capita Tax Revenue

Independent Variables: Composite Index of Decentralisation, dummy variable (dum1) relating to the election of the municipalities and dummy variable(dum2) relating to submission of ATRs.

Method of Regression: GLS

	NPs	Municipalities	M.Corps.
1	*2*	*3*	*4*
CDI	11.16613	32.74872	140.3288
	(2.622)***	(5.964)***	(4.453)***
Dum1	3.784985	3.314432	49.00545
	(1.017)	(0.760)	(1.919)*
Dum2	2.910962	6.040374	-43.67632
	(0.571)	(0.946)	(-1.182)
Constant Term	4.693557	17.19842	34.86658
	(2.345)**	(6.433)***	(2.313)**
No. of Observation	112	112	112
Wald Chi	9.66	40.02	24.7
Prob.> chi 2	0.0217	0.0000	0.0000

Note: Figures in the parenthesis are the corresponding z-ratios.
***: Coefficients are significant at 1 percentage level
**: Coefficients are significant at 5-percentage level
*: Coefficients are significant at 5-10 percentage level.

Table 12: Regression Results for Equation 4A
Dependent Variable: Per Capita Non-Tax Revenue
Independent Variables: Composite Index of Decentralisation, dummy variable (dum1) relating to the election of the municipalities and dummy variable(dum2) relating to submission of ATRs.
Method of Regression: GLS

	NPs	Municipalities	M.Corps.
1	*2*	*3*	*4*
CDI	4.665215	21.11455	70.47188
	(2.500)**	(8.485)***	(11.055)***
Dum1	1.118897	-0.7836103	1.288379
	(0.686)	(-0.397)	(0.249)
Dum2	2.077428	2.332012	15.35763
	(0.930)	(0.806)	(2.055)**
Constant Term	2.572795	8.927605	4.947774
	(2.933)***	(7.369)***	(1.623)
No. of Observation	112	112	112
Wald Chi	9.22	73.83	133.82
Prob.> chi 2	0.0265	0.0000	0.0000

Note: Figures in the parenthesis are the corresponding z-ratios.
***: Coefficients are significant at 1 percentage level
**: Coefficients are significant at 5-percentage level
*: Coefficients are significant at 5-10 percentage level.

In case of the tax revenue generation capacity of the ULBs the impact of fiscal decentralisation continue to be significant and positive for all categories of the ULBs and, the magnitude is highest for the M.Corp. and least for the NPs. All these coefficients are significant at 1 percentage level. The coefficients of the dummy variables relating to the municipal elections are positive for all tiers of ULBs but the strength of the coefficient is greatest for the M.Corp both in terms of the numerical value of the coefficient and level of significance (it is significant at 10 percentage level). The numerical value of the coefficient of the first dummy variable for the municipalities is less than that for the NPs, with both of them turn out to be insignificant. The dummy variable corresponding to the submission of the ATR has positive impact, except for the M.Corp., on the tax revenue generation capacity although each of these coefficients are insignificant. From the above analysis, it can be concluded that, the larger ULBs in general and M.Corp. in particular, have been able to accrue the maximum benefits, in whatever extent it is, of decentralisation process both in fiscal and legal/administrative senses. This is reinforced by the fact that the numerical difference among the coefficients of the CDI with respect to the univariate model and the redefined model is largest for the M.Corp. Another interesting observation that can be made from the regression results is that, although the coefficients of the two dummy variables are, in general, insignificant, the dummy variables related to the municipal election appear to be relatively more important[17] in case of the tax revenue generation capacity of the ULBs.

Analysis relating to the non-tax revenue generation capacity reveals that the fiscal decentralisation initiatives have positive impacts on the above. As in case of tax revenue, the coefficients, except for the NPs, are significant at 1 percentage level for the non-tax revenue. Also, the numerical values of the coefficients of CDI, for each category of the municipal bodies, are lower for non-tax revenue than that for tax revenue. The coefficients of the dummy variables relating to the municipal elections are positive, barring municipalities, for the municipal bodies. But all of them are insignificant. On the other hand, the dummy variable related to the submission of the ATR has positive impact on the non-tax revenue generation capacity for all the municipal bodies, with the corresponding coefficient is significant for the municipal corporations at 5% level. Similarly, despite the coefficients of the two dummy variables being insignificant, the dummy variable relating to the submission of ATR seems to be relatively more important factor[18] affecting the non-tax revenue generation capacity of the ULBs. In a way, this also shows that the impact of the decentralisation initiatives, both from fiscal as well as legal/administrative perspectives, on the non-tax revenue generation capacity of the ULBs, has been the highest for the largest of the municipal entities, the municipal corporations.

Section VI
Concluding Observations & the Way Forward

The above analysis thus, reveals that the problem relating to the financing of urban infrastructure in general and urban basic services (UBSs) in particular has aggravated in the recent past. There has been substantial decline in the governments' budgetary support for this purpose. The developed states and, especially, the larger cities and towns were the major destinations for the domestic institutional funds as well as external assistance. Approach of full cost recovery for the UBSs, as envisaged in the Eighth Plan and consequently in the Ninth Plan, and imposition of strict financial discipline on the state governments by the RBI would result in further concentration of funds in the developed states and the larger cities. Also, ULBs, with the infirm financial position, were unable to take up the responsibility of financing and provisioning of UBSs. But, ULBs assuming maximum responsibility in the provision of these UBSs and, in the process, financing a healthy proportion of the required resource requirements would nave been a feasible option. The 74th CAA and the ensuing decentralisation initiatives are hailed as meaningful steps for achieving this objective, with greater infusion of accountability among the local elected officials in one hand and enhanced resource capacity of the local bodies on the other.

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[17] It is evident from the z-ratios that the probability of accepting the null hypothesis that coefficient of dum_i (I=1,2) is equal to zero is maximum in case of the second dummy variable, except for the municipalities.
[18] Here, the z-ratios show that the probability of accepting the null hypothesis that coefficient of dumi (I=1,2) is equal to zero is maximum in case of the first dummy variable, for all the ULBs.

The above analysis manifests that the decentralisation initiatives have some positive impact on the financial health of the ULBs. But, relatively larger local bodies, with strong financial base, are being benefited most from these initiatives. At the same time we have to keep in mind the fact that most of the state governments, despite being given some excellent opportunities through constitutional provisions, have done very little to improve the financial position of the ULBs as a whole. In some cases, they preferred to disburse financial assistance to the ULBs for improvement purpose. However, it will simply be inopportune to arrive at a pessimistic conclusion pertaining to the potency of the decentralisation initiatives. Moreover, eight to ten years of experiences are too small to jump into such conclusions.

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