



A Blueprint for Urban Fiscal Devolution

Recommendations to XVI
Finance Commission



September 2025

About Janaagraha Centre for Citizenship and Democracy

Janaagraha is a Bengaluru-based not-for-profit institution working to transform the quality of life in India's cities and towns. It defines quality of life as comprising quality of infrastructure and services, and quality of citizenship. To achieve its mission, Janaagraha works with councillors and citizens to catalyse active citizenship in city neighbourhoods, and with governments to institute reforms to city-systems. Janaagraha has worked extensively on urban policy and governance reforms for over two decades including on JnNURM, and with the XIII, XIV, and XV Finance Commissions, the Comptroller and Auditor General of India, NITI Aayog/Planning Commission, the Ministry of Housing and Urban Affairs (MoHUA), as well as the state governments of Odisha, Uttar Pradesh, Tamil Nadu, Rajasthan, Karnataka, and Assam. Find out more at www.janaagraha.org.

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List of Abbreviations

ADC	Autonomous District Councils
AFS	Audited Financial Statement
AG	Accountant General
API	Application Programming Interface
ATR	Action Taken Report
BBMP	Bruhat Bengaluru Mahanagara Palike
BDA	Bangalore Development Authority
BE	Budget Estimate
BMR	Bangalore Metropolitan Region
BMRCL	Bangalore Metro Rail Corporation Limited
BMRDA	Bangalore Metropolitan Region Development Authority
BMTC	Bengaluru Metropolitan Transport Corporation
BSCL	Bhopal Smart City Limited
BSRP	Bengaluru Suburban Railway Project
BWSSB	Bangalore Water Supply and Sewerage Board
CAA	Constitutional Amendment Act
CAG	Comptroller and Auditor General of India
CAP	Capital Action Plan
CDA	Cuttack Development Authority
CII	Confederation of Indian Industry
CIIS	City Infrastructure and Institutional Improvement Scheme
CRUT	Capital Region Urban Transport
CWAS	Center for Water and Sanitation
DAY	Deendayal Antyodaya Yojana
DBT	Direct Beneficiary Transfer
DoE	Department of Expenditure
DPIIT	Department for Promotion of Industry and Internal Trade
DPR	Detailed Project Report
DUR	Detailed Utilisation Report
FC	Finance Commission
GDP	Gross Domestic Product
GFC	Garbage Free Certificate
GHMC	Greater Hyderabad Municipal Corporation
GO	Government Order
GPDP	Gram Panchayat Development Plan

GPS	Global Positioning System
GSDP	Gross State Domestic Product
GTC	Grant Transfer Certificate
GVA	Gross Value Added
HP	Himachal Pradesh
HPEC	High Powered Expert Committee
HR	Human Resources
ICAI	Institute of Chartered Accountants of India
IFMIS	Integrated Financial Management and Information System
IT	Information Technology
KSDB	Karnataka Slum Development Board
KSRTC	Karnataka State Road Transport Corporation
KUWSDB	Karnataka Urban Water Supply and Drainage Board
LFA	Local Fund Audit
LFAD	Local Fund Audit Department
LG	Local Government
MCF	Million-Plus Cities Challenge Fund
MLA	Member of Legislative Assembly
MoHUA	Ministry of Housing and Urban Affairs
MoPR	Ministry of Panchayati Raj
MP	Member of Parliament
MPC	Million-Plus Cities
MRTS	Mass Rapid Transit System
NBC	National Building Code
NGT	National Green Tribunal
NITI	National Institution for Transforming India
NIUA	National Institute of Urban Affairs
NMAM	National Municipal Accounting Manual
NMPC	Non-Million-Plus City
NMT	Non-Motorised Transport
NRW	Non-Revenue Water
NSO	National Statistical Office
NUDM	National Urban Digital Mission
NULM	National Urban Livelihoods Mission
ODF	Open Defecation Free
OSR	Own Source Revenue
OSRTC	Odisha State Road Transport Corporation
OWSSB	Orissa Water Supply and Sewerage Board

PFM	Public Finance Management
PM	Prime Minister
PMU	Programme Management Unit
PRI	Panchayati Raj Institution
RDD	Rural Development Department
RE	Revised Estimate
RIDE	Rail Infrastructure Development Company
RLB	Rural Local Body
RLG	Rural Local Government
RSCL	Rourkela Smart City Limited
RUTP	Rural–Urban Transition Policy
SFC	State Finance Commission
SUDA	State Urban Development Agency
SWM	Solid Waste Management
TGS	Technical Guidance and Supervision
TP	Town Panchayat
TPS	Town Planning Scheme
UA	Urban Agglomeration
UFC	Union Finance Commission
UGD	Underground Drainage
ULB	Urban Local Body
ULG	Urban Local Government
UN	United Nations
UP	Uttar Pradesh
WATCO	Water Corporation of Odisha
WB	West Bengal
WSS	Water Supply and Sanitation

Summary of Recommendations



This section consolidates the key recommendations made in the report *A Blueprint for Urban Fiscal Devolution: Recommendations to XVI Finance Commission*, commissioned by the XVI Finance Commission (FC). The recommendations are grounded in empirical evidence, insights from the field, and the evolving landscape of urbanisation and urban governance in India. They are designed to support the XVI FC build on the reform momentum of previous Commissions, particularly the XV FC while addressing persistent challenges in the finances and governance capacity of Urban Local Governments (ULGs), as well as grant effectiveness.

Introduction

The 74th Constitutional Amendment Act (CAA), 1992, was a watershed moment in strengthening the institutional and functional salience of ULGs¹. It granted constitutional status to municipalities by inserting Part IXA. However, the 74th Amendment left the assignment of ULGs' revenue sources at the discretion of state governments. Since ULGs fall under the State List, with states responsible for determining both spending responsibilities and revenue powers, it is assumed that states bear the obligation to bridge the gap between what ULGs can raise and what they require to perform their functions. The expenditure responsibilities of ULGs far outweigh their revenue-generating capacities, leaving them heavily reliant on higher tiers of government for fiscal support.

The 74th Amendment has tried to correct this imbalance with Articles 280(3)(bb) and 280(3)(c), which mandate that the Union Finance Commission (UFC) recommend measures to augment the Consolidated Fund of a State to supplement the resources of panchayats and municipalities. This constitutional amendment formally acknowledged the fiscal claims of ULGs at the national level and provided a way for UFCs to address their financing needs. Today, the role of UFCs extends beyond fiscal transfers. Over the years, successive FCs have offered crucial reform direction to address systemic deficiencies in municipal finance and governance architecture. Rapid urban growth and the growing deficit in infrastructure and service delivery have made the case for increased funding to urban areas even more pronounced.

¹ While commonly referred to as Urban Local Bodies (ULBs) and Rural Local Bodies (RLBs), these institutions are constitutionally recognised and democratically elected governments. The continued use of the term 'Urban Local Bodies' underplays this status, reinforcing a perception of administrative subordination. Shifting to the terminology of 'Urban Local Governments (ULGs)' is not a matter of semantics but of recognising their rightful place as the third tier of governance, with the authority and responsibility to plan, govern, and deliver services. This terminological shift is essential to strengthening their institutional identity and embedding the spirit of decentralisation in India's federal architecture.

India's Urban Landscape

India is urbanising at an unprecedented pace, with the population in urban areas estimated to grow from 372 million in 2011 to over 800 million by 2050. According to the 2011 Census, India is 31% urban. Official data does not capture the current scale and speed of urban growth. The Ministry of Health and Family Welfare's (MoHFW) 2019 technical report on urban projections estimates that the urban population reached 34.5% in 2021. However, alternative methodologies estimate that the urban population is already closer to 45%². Official records currently do not capture the scale and speed of urban growth. The lack of updated and verified data on urbanisation, either in the form of a Census or a comprehensive list of statutory towns is a critical impediment to understanding urbanisation and its trends across states and regions.

This rapid urbanisation has created a significant gap in governance, with many urbanising areas still governed as Rural Local Governments (RLGs). According to the Ministry of Housing and Urban Affairs (MoHUA), there are currently 1,057 newly constituted ULGs³ with a population of approximately 26 million. However, many other settlements which exhibit urban characteristics remain classified as census towns and governed under rural administrative frameworks. This disconnect between urbanisation (the growth of population and economic activity in urban settlements) and municipalisation (the formal recognition of such settlements through the constitution of ULGs) lead to fast-urbanising areas that are underserved and lack basic infrastructure and service delivery.

The absence of a policy for transitioning rural local governments to urban local governments further exacerbates these challenges. Only one state, Odisha, has a detailed Rural–Urban Transition Policy (RUTP) while Rajasthan has introduced a draft bill to this effect. Transitions often occur in a fragmented and discretionary manner, rather than through a structured, policy-led process.

Recommendations:

- 1. Strengthen the Local Government Directory (LGD) as the single source of truth for all information related to local governments in India.** The Ministry of Housing and Urban Affairs (MoHUA) and the Ministry of Panchayati Raj (MoPR) should collaborate to regularly update and maintain the LGD with notifications of newly constituted ULGs. This would ensure accurate, real-time data on urban and rural settlements. The systems should also offer API-based access to this information, enabling seamless use by various government systems and stakeholders.

² United Nations, Department of Economic and Social Affairs, Population Division (2015). World Urbanisation Prospects: The 2014 Revision.

³ Basis reporting on www.cityfinance.in, as on 30-06-2025.

2. **An Urbanisation Premium of ₹20,000 crore should be instituted for the 2026–2031 period, contingent on states adopting a formal Rural–Urban Transition Policy (RUTP). This fund should be equally drawn from the XVI Finance Commission's grants to rural and urban local governments and allocated to states that have notified an RUTP and identified urbanising areas.** Two cohorts of local governments will be eligible for the Premium: (i) ULGs constituted between the 2011 Census and 30 September 2026, and (ii) Urbanising Gram Panchayats (GPs) identified, by 31 March 2027, as transitional areas by the state government

The RUTP must provide a clear, structured framework for transitioning rural settlements to urban governance, ensuring administrative upgrades and pre-notification improvements in infrastructure and services. The Urbanisation Premium should be used exclusively to fund these transitions, particularly in newly constituted ULGs and transitional areas.

- i. Year 1 allocation would be 10% of the total Premium and would be released to states upon notification of a RUTP. States can distribute it further to ULGs that are constituted between the 2011 Census and 30 September 2026.
- ii. Year 2 allocation would be 15% of the total Premium and its release would be contingent on the submission of 3-year Transition Plans, prepared for each transitional area in consultation with the concerned GP or ULG, to MoHUA.
- iii. Allocations for Years 3, 4, and 5 will be 25% of the total Premium for each year. Funds will be disbursed to newly constituted ULGs and transitioning GPs for the implementation of their respective Transition Plans.

Financing Needs and Fiscal Realities of ULGs

India's cities and towns require sustained investment in infrastructure and service delivery. However, there are no reliable, up-to-date estimates of urban investment needs. Previous assessments by McKinsey Global Institute in 2010, High-Powered Expert Committee (HPEC) in 2011 and by the World Bank in 2022 were standalone exercises that were not part of a systematic or regularly updated framework. More importantly, each was constrained by a common underlying limitation: the absence of standardised, granular, and comparable data across ULGs. As a result, even as India's urban footprint expands, governments across tiers lack the frameworks and capacities to assess how much to invest, in which sectors, over what timeline, and through what financing strategy.

The complexity of estimating urban investment needs is compounded by the highly fragmented nature of urban governance in India. Despite a constitutional mandate, most ULGs lack complete control over essential functions such as water supply, sewerage, urban transport, and housing. These often remain with parastatal agencies or departments that report directly to state governments. The significance of parastatals is also reflected in budget allocations. In Karnataka, between Financial Year (FY) 2020–21 and FY 2023–24, parastatals and ULGs each accounted for approximately 40% of the Urban Development Department (UDD) budget. In Odisha, between 2018–19 and 2025–26, parastatals received an average of 19% of the Housing and Urban Development Department (HUDD) budget.

Unlike elected local governments, parastatals are not subject to the same transparency and accountability frameworks. Most are not required to disclose budgets, financial progress, or project outcomes in the public domain. As a result, their fiscal operations remain opaque, further constraining a comprehensive understanding of urban investment flows.

Urban development is constitutionally a state subject and the 74th Constitutional Amendment envisioned a greater role for ULGs in shaping it. In practice, however, roles and responsibilities overlap across union, state, and ULGs. Limited information on parastatals and the absence of disaggregated city-level investment data restrict discussions on urban finance to ULG finances.

In FY 2021–22, aggregate municipal revenue was estimated at ₹2.08 lakh crore, or 0.77% of GDP — significantly below the High-Powered Expert Committee's target of 2.01% of GDP by 2031–32. Of this, ULGs generated ₹1.03 lakh crore in Own Source Revenue (OSR), amounting to just 0.38% of GDP. This was insufficient to meet their rising expenditure obligations: revenue expenditure stood at ₹1.13 lakh crore, while capital expenditure was only ₹0.55 lakh crore, indicating a substantial internal funding shortfall for infrastructure development.

There are also sharp disparities in the fiscal capacity of ULGs depending on their size. In FY 2021–22, ULGs with populations above 4 million (4M plus) generated 71% of their revenue from own sources, compared to just 37% for ULGs with populations below 500,000. Smaller ULGs remain more reliant on intergovernmental transfers and are therefore more fiscally vulnerable.

Grants from the Finance Commission (FC), Centrally Sponsored Schemes (CSS), and state programmes are essential sources of capital funding. However, most CSS and state grants are tied to specific schemes, limiting the discretion of ULGs in allocating funds according to local priorities. In this context, FC grants acquire added importance. As formula-based and largely untied transfers, they provide predictable and flexible funding that enables ULGs to bridge resource gaps, strengthen institutional capacity, and invest in ULG-specific priorities.

▲ Recommendations:

1. Institutionalise a bottom-up, standardised approach for estimating municipal investment requirements across India's diverse urban landscape.

MoHUA should play a central coordinating role in spearheading this reform. Its mandate should focus on developing and promulgating a national framework for systematically estimating infrastructure and service delivery gaps and associated resource needs, while actual assessments using such a framework are undertaken by states and ULGs.

2. Strengthen the accountability of parastatals for urban investments.

Where ULGs transfer funds to parastatals for service delivery functions such as water supply, they should retain financial control and decision-making authority through Service Level Agreements (SLAs). Regular public disclosure of parastatal finances and activities, including annual audits and performance audits, should also be mandated.

Where ULGs transfer Finance Commission grants to parastatals, such entities should be encouraged to publish audited annual accounts and budgets, in line with the disclosure requirements for ULGs. While not a precondition for release of funds, this measure would serve as a foundation for extending the practice of publishing audited annual accounts and budgets to parastatals such as water boards and transport corporations, many of which manage expenditures greater than those of ULGs.

Investing in Urban: Recalibrating Urban Quantum and Distribution

The allocation of grants to ULGs has steadily increased over successive Finance Commissions, yet the per capita share of urban grants remains insufficient to meet the demands of a growing urban population. Under the XIV FC, the share of local government (LG) grants in the divisible pool increased from 2.17% to 3.55% between 2015–2020. In contrast, the XV FC saw a decline in the share of LG grants in the divisible pool, from 5.00% in 2021 to 3.52% in 2026, averaging 4.23% over the period. The final year per capita allocation for LGs in 2025–26 was ₹672, slightly lower than the ₹674 recorded in the final year of the XIV FC (2019–20), despite a six-year gap.

On average, ULGs received 34% of the total local government grants during the XV FC period. This is below the urban population share which is expected to reach 38% by 2025. However, the interim report (2019) explicitly recommended increasing the share of ULGs in LG grants to 40% over the

medium term. Given that the most recent census is 14 years old, the XVI FC will face challenges in estimating the true extent of urbanisation. Projections suggest that India is rapidly urbanising, with urbanisation expected to reach 41% by 2031. Furthermore, the economic importance of urban areas is significant, with cities projected to contribute 75% of the country's GDP by 2030.

Historically, Centrally Sponsored Schemes (CSS) allocations have disproportionately favoured rural areas, both in absolute terms and on a per capita basis. In 2021–22, for example, while urban allocations peaked at ₹1.00 lakh crore, rural allocations totalled ₹2.28 lakh crore — more than two times higher. This disparity is even more pronounced on a per capita basis. However, current grant allocations fail to adequately reflect India's accelerating urbanisation and the increasing importance of cities to the country's economic future. Cities require significantly improved infrastructure and services to attract and retain investment and talent. Given the pace of urbanisation, the growing contribution of cities to national economic growth, and the scale of urban service delivery gaps, there is a compelling case for substantially increasing the share of grants allocated to ULGs.

Interestingly, the XV FC applied a fixed national rural–urban ratio uniformly across all states to determine the split of funds between rural and urban areas. However, this approach did not take into account the significant variations in urbanisation levels across states. By applying the national rural–urban ratio uniformly, the XV FC inadvertently skewed the distribution of grants within states. States with higher urban populations were disadvantaged in per capita allocations to ULGs, while less urbanised states received relatively more and vice versa for RLGs.

▲ Recommendations:

- 1. Maintain the share of local government grants in the divisible pool at a minimum constant rate of 4.23% for each year of the award period to better align with rising service delivery expectations and costs.**

While this may increase the total quantum of LG grants, it will help restore adequate per capita allocations, better aligned with the realities of service delivery on the ground.

- 2. Increase the share of ULGs to 40% of the total local government grants under the XVI FC, up from approximately 36% (₹1,55,628 crore) under the XV FC.**

This increase would raise per capita urban grants over five years, ensuring that urban areas receive a more equitable share of local government grants, in line with the growing urban population, their evolving needs, and their role in driving economic growth.

3. Adopt a differentiated approach for inter-state distribution of rural and urban grants. Urban grants should be based on each state's proportion of the total urban population, as per the 2011 Census, while rural grants should follow the traditional 90:10 ratio based on population and area.

This approach addresses the challenges of the XV FC's uniform application of a national rural-urban ratio, ensuring a more accurate and equitable distribution of grants based on actual urbanisation levels.

Eligibility Conditions for ULGs: Evolution of Reform Frameworks

Finance commissions have traditionally played a dual role: recommending measures to bridge the vertical and horizontal fiscal gaps at the third tier of government while also steering vital governance reforms to enhance transparency, accountability, and financial sustainability in ULGs. The XV FC introduced a significant shift by linking all urban grants, whether tied, untied, or performance-linked, to minimum eligibility conditions. These conditions were linked to key reforms, including the publication of audited annual accounts and service-level benchmarks (SLBs), growth in property tax collection, and the constitution of State Finance Commissions (SFCs). This approach has positively influenced the culture of compliance and transparency in ULGs.

The impact of these conditions was evident as 96% of ULGs uploaded their audited accounts on MoHUA's www.cityfinance.in, and 11 states⁴ constituting SFCs following the introduction of the XV FC's condition. However, smaller ULGs faced challenges in achieving property tax growth rates aligned with their state's GSDP growth rate. Additionally, some ULGs in certain states faced penalties for failing to meet the constitutional requirement of holding local elections. There is a need to build on these conditions to improve financial governance, with some tailored approach for different population categories of ULGs, as larger ULGs face fewer challenges compared to smaller ones.

▲ Recommendations:

1. Build on the mandatory eligibility conditions of the XV FC while also simplifying them to align with existing processes and avoid additional compliance burdens on ULGs. These conditions promote basic standards of transparency, financial discipline, and data availability in urban governance.

⁴ Information on the formation of State Finance Commissions (SFCs) is based on publicly available data as of March 2025.

2. Release basic grants in two instalments linked to following eligibility conditions:

i. For the first instalment (preferably by 31 May):

- a. Public disclosure of annual budget, approved by the council, on www.cityfinance.in.
- b. Annual availability (as relevant) of the applicable notification of SFC constitution, SFC report, action taken report, and yearly implementation report, without extending SFC recommendations beyond the original term.

ii. For the second instalment (preferably by 31 October):

- a. Public disclosure of audited accounts, including: (a) auditor's report; (b) balance sheet; (c) income and expenditure statement; (d) cash flow statement; (e) receipts and payments statement; (f) schedules to the balance sheet, income and expenditure statement; and (g) significant accounting policies, preferably in a machine-readable format, on www.cityfinance.in.
From third year onwards, grant disbursement to ULGs would be linked to public disclosure of audited accounts as per revised NMAM and adherence to government accounting standards.
- b. Public disclosure of Service Level Benchmarks (SLBs), on www.cityfinance.in.

iii. Only duly elected ULGs shall be eligible for the grants.

Differentiated Grant Architecture for ULGs

The 74th Constitutional Amendment envisioned a governance framework where ULGs would act as self-governing institutions, capable of independent planning and spending. The principle of subsidiarity also emphasises decentralisation and local autonomy, and suggests that decisions made closer to the ground, by those directly impacted, are often more effective and efficient.

This is evident from utilisation data of tied and untied grants, where utilisation of untied grants is at least 20% higher than tied grants. Rigid earmarking of end-purpose undermines allocative efficiency and local autonomy, contradicting the spirit of the 74th Constitutional Amendment. Furthermore, tied grants already dominate funding flows in terms of central and state transfers. For instance, in Karnataka, 91% of State Finance Commission grants (2020–25) were tied, mirroring the central trend.

ULGs with populations below 4 million particularly struggle with utilisation of tied grants. Between FY 2020–21 and 2023–24, their utilisation of tied grants remained below 50%, while ULGs above 4 million (4M+) achieved over 90%. This gap reflects not just fiscal constraints but deep variations in economic potential, revenue capacity, and institutional readiness across Indian ULGs. The

current grant architecture does not adequately reflect the vast differences. The XVI FC has a unique opportunity to redesign the grant architecture, based on a differentiated approach. This recommendation rests on three inter-related premises:

1. Cities must be recognised as economic centres

Urban areas contribute over 65% of India's GDP, a share expected to exceed 70% by 2030⁵. India's urban economic output is heavily skewed towards its metro cities. Nearly 10% of India's GDP is generated by just 5 metropolitan regions — Bengaluru, Chennai, Hyderabad, Kolkata, and Mumbai⁶. Though they represent just a fraction of the national population, they contribute disproportionately to national GDP and demonstrate 1.5 to 2 times higher economic output relative to their demographic footprint. Further, 80 cities with populations between 500,000 and 4 million like Visakhapatnam, Coimbatore, Vadodara, Jaipur, and Kochi are increasingly attracting investment, skilled workers, and are ahead in innovation. A 2022 CBRE report noted that Tier-2 cities provide a 10–35% cost advantage compared to their metropolitan counterparts⁷.

However, these ULGs are largely treated as implementing agencies rather than autonomous economic actors. Without clear economic strategies, delegated functions such as land-use regulation or building approvals operate in silos, contributing to fragmented, low-productivity urban growth. The grant framework must empower ULGs to act as drivers of national growth rather than passive implementers of schemes.

2. Grant architecture must address disparities in the revenue-generating capacity of ULGs

An analysis of the audited financial accounts of 4,800 ULGs (2021–22) from www.cityfinance.in shows that ULGs with population above 4 million generate over ₹10,000 per capita in own-source revenue (OSR), compared to ₹1,000–1,600 in small ULGs (below 500,000 population), a tenfold gap. Per capita property tax collections in ULGs below 500,000 population are just one-sixth of those in metro cities. While metros can partly finance capital investments from OSR, smaller cities are barely able to provide required services and infrastructure. In most cases, their only capital expenditure is funded by higher tiers of government (FC grants and Centrally Sponsored Schemes (CSS)). CSS with strict guidelines and limitations often take 'one size fits all' approach irrespective of ULG size or region and do not respond to local needs.

3. The grant architecture must reflect administrative, institutional capacity and accountability for performance

ULGs with population above 500,000 typically have functional planning, engineering, sanitation, and finance departments. In contrast, many smaller ULGs operate with 40–60% staff vacancies, lack qualified technical officers, and often do not have full-time commissioners. These smaller ULGs are often the most neglected segment in the urban hierarchy. Though they account

⁵ Subudhi, S., Bakliwal, S., & Bilgrami, S. (2023, March 10). Cities of the future: Reimagining and rejuvenating India's top 50 urban ecosystems [Report]. Boston Consulting Group. <https://www.bcg.com/publications/2023/india-cities-of-the-future>

⁶ Gandhi, S., & Pethe, A. (2017). Emerging challenges of metropolitan governance in India. *Economic and Political Weekly*.

⁷ Ghatak, K. (2023, March 14). Exploring the shift: GCCs moving to Tier-2 cities for cost and talent advantages. EY India. https://www.ey.com/en_in/insights/consulting/exploring-the-shift-gccs-moving-to-tier-2-cities-for-cost-and-talent-advantages

for 4,737 of India's ULGs and house nearly 59% of the country's total urban population, these towns have been consistently underrepresented in national urban missions such as AMRUT, SMART Cities, and Metro Rail programs. Further, they suffer from limited financial capacity, weak institutional frameworks, and a near-absence of capital investment planning or professional staffing. Uniform performance-based grants risk penalising these ULGs, which lack the institutional scaffolding to utilise and report on funds effectively.

▲ Recommendations:

1. Design 100% grants as untied, without mandating end-use.

This will empower ULGs to allocate funds according to local priorities. Promote the preparation of annual action plans and Capital Investment Plans (CIPs) to improve project selection, while requiring public disclosure of expenditure and projects to strengthen accountability. To ensure balanced investment, a spending cap could be introduced, limiting no more than 50% of FC grant utilisation in a single sector over five years. ULGs could utilise the grants across diverse sectors such as drainage, roads, water supply, solid waste management (SWM), sanitation, public health, street lighting, housing, education, parks and open spaces, slum improvement, and other civic infrastructure. Digital grant administration system could track projects and sectoral spending, enabling corrective action such as training, capacity building, or project preparation support when ULGs concentrate funds in too few sectors.

2. Adopt a differentiated approach to grant architecture for ULGs based on population categories and administrative and institutional capacity as well as accountability for performance.

ULGs will receive a mix of basic, output-linked, and outcome-based grants, tailored to their population category. This will ensure that larger ULGs are incentivised to perform, while smaller ULGs receive the support necessary for essential services. **Notably, 80% of the total urban grants will be allocated as basic grants by following below approach.**

i. Category I: Small ULGs with populations below 500,000 (4,737 in total)

We recommend **100% basic untied grants** to provide regular and stable financial support, with no output- or outcome-based conditions. These grants will be disbursed only to duly elected ULGs that meet the basic eligibility criteria. Once eligibility is met, no further conditions will apply to the grant's claim and usage. Being untied, these grants will allow ULGs to prioritise spending according to local needs across the 18 functions in the Twelfth Schedule of the Constitution.

ii. Category II: Medium and large ULGs with populations between 500,000 and 4 million (80 in total)

We recommend:

- a. 70% of the grant be basic** in nature and used by ULGs for any purpose except salaries and establishment costs.
- b. 30% of grants be output-linked to improve performance in four conditions:**
 - A. ULGs must demonstrate a minimum annual OSR growth of 7.5%.
 - B. Develop and publish an inventory of public land assets, including those held by the ULG, state agencies, and parastatals, and undertake their market valuation.
 - C. Develop and publish a Capital Investment Plan (CIP) to improve infrastructure project planning.
 - D. Publish select economic data annually from Year 1 to Year 5.

iii. **Category III: 7 Metros (Population above 4 million)**

To unlock their full economic potential and improve quality of life in these seven metros, we recommend that their FC grant be outcome-based. These ULGs already generate significant own revenue to meet basic expenditure needs and have the potential to generate more by achieving efficiencies from their robust and sizeable economic bases.

To drive this performance, we propose that the release of grants be linked to the following three parameters (and underlying conditions), each with different weights, evaluated as per targets aligned with the city's growth trajectory:

- a. Service Level Benchmarks (50%): Improving delivery of essential urban services.**
 - A. Publication of baseline service-level assessment across the four SLB sectors (or other additional sectors identified by the FC) and establishment of targets for a selected sector.
 - B. Publication of Performance Improvement Plan for improving services for the selected sector
 - C. Publication of Capital Investment Plan
 - D. Performance achievement against established targets for the selected sector
- b. Land and Planning (30%): Optimising urban form, and equitable and inclusive land development.**
 - A. Publish and notify zone-specific Development Control Regulations (DCRs) and Slum Proofing Action Plan (SPAP)
 - B. Publish public land inventory
 - C. Publish market valuation of the public land inventory
 - D. Demonstrate project implementation progress in core zone (affordable housing and DCRs)
 - E. Operationalise real-time monitoring dashboard for tracking progress

c. Economic Growth (20%): Enabling investment and fostering data-driven economy.

- A. Set up an Economic Development Cell (EDC) within ULGs
- B. Measure and report city-level economic data, including number of commercial establishments, commercial property tax collections, trade licenses issued, property registrations (value and volume), vehicle registrations (RTO), investments announced/implemented, commercial power consumption, number of MSMEs and number of startups.
- C. Reduce processing time for building permits (at least 80% of building permits are issued within 45 days by year 5).

At the beginning of the award period, MoHUA, Department of Expenditure (DoE), state governments, and ULGs will jointly establish baselines, outcome targets, implementation roadmaps, and monitoring and verification mechanisms for the outcome-based grant indicators. ULGs will report progress on indicators through the www.cityfinance.in, with data verified by independent third-party evaluators engaged by MoHUA. **Based on verified performance, grants will be disbursed in a single instalment in October each year.**

3. **Provide a 'Decentralisation and Capacity' grant of ₹20,000 crore (~5% of XVI FC's urban allocation) exclusively for ULGs with populations below 4 million to enable them to absorb and effectively utilise their share of the XVI FC's urban allocations and invest in strengthening institutional capacity, professionalising municipal finance, and planning functions, and advancing decentralisation under the 74th CAA. The grant should be shared 50:50 between states and ULGs,** with each level having a distinct role in enabling and implementing reform. State funds would create an enabling environment for ULG reforms by establishing Municipal Finance and Governance Reform Units, introducing shared service centres, and operationalising municipal finance and engineering cadres. ULG funds, in turn focus on planning, asset management, end-to-end digitalisation of finance and accounts, augmentation of OSR, and robust reporting of SLBs. Eligibility requires states to have constituted SFCs, acted on their recommendations, and publish a supplement with state budget on grants and transfers under various budget heads to ULGs as part of the state budget, as this ensures transparency in devolution, enables ULGs to track actual transfers, and enhances accountability of state governments in honouring SFC recommendations. 'Decentralisation and Capacity' grant should be disbursed annually on a per capita basis.

XVI FC Grant Administration for Efficient and Accountable Spending

The evolution of digital grant administration from the XIV to XV FC marked a significant shift. The introduction of the www.cityfinance.in and grant disbursement by mandating linking of ULG's bank account to PFMS streamlined the process, enabling quicker and more transparent decisions regarding the approval of ULG grant claims. However, despite these advancements, significant challenges remain. For MPCs and NMPCs, on average, ULGs received XV FC grants 11.64 months after the start of the financial year. Further, despite the significant value of public finances invested, ULGs, state, union and citizens are unable to link outlays to service delivery outputs achieved on ground.

These challenges are rooted in a combination of structural, procedural, and technological factors. Primary among them is the high administrative burden placed on ULGs and state agencies – arising not only from limited use and interoperability of digital systems, but also from overlapping processes, multiple reporting requirements, among others. Limited trust in ULGs' submissions leads to duplication of verification efforts, prolonging the process of grant release. Further, existing systems do not provide a comprehensive, real-time view of status of grant approval, its release, utilisation and physical progress, limiting predictability, accountability and informed decision-making.

The need for a more robust and seamless digital system to manage these grants is critical to improving service delivery, reducing delays, and ensuring greater accountability.

▲ Recommendations:

- 1. Establish a mechanism for rolling, automated transfers from the union to ULGs within 10 business days from the date of approval by the DoE, once ULGs become eligible.** Further, shift from batch-based disbursements (based on submissions by states when most ULGs qualify) to a continuous release model that rewards early compliance and improves fund flow predictability. Ideally, ULGs that make timely submissions should receive their first instalment in the first quarter of the financial year and second instalment in the third quarter.
- 2. Mandate MoHUA & DoE to develop end-to-end paperless digital grant administration system** by strengthening the existing grant administration system on www.cityfinance.in. This will expedite the grant release, reduce workload for ULGs, states and union government and enable tracking of funds from allocation to expenditure by leveraging digitisation and advancements

in financial management systems (PFMS, State IFMS, Municipal Finance systems). Digital grant administration system should have following functionalities:

- a. **Automatic transfer and verification of information for compliances** (Audited financial statements, Budgets, Service Level Indicators, Revenues, expenditure) through APIs from source systems such as PFMS, IFMS, Municipal Finance Systems for reducing the effort in collecting, uploading and verifying this information; In case information is not available in source systems, provide a simple interface for uploading compliances by ULGs and states, and verification on the system itself
 - b. **Online processes for (i) claiming of grant by ULGs, (ii) calculation of entitlement, (iii) processing of grants claims** at MoHUA and DoE
 - c. **Generation of sanction order and payment instruction through system** for release of the grants to ULGs through PFMS & State IFMS
 - d. **Expenditure for all FC grants through PFMS** to enable trackability of expenditure (even if ULG is transferring FC grants to any parastatals or other implementing agency) and recording of project information (i.e. Project ID, Name of project, new/ existing, geo-location, sector, size/ capacity, tendered amount, actual expenditure, status of project (ongoing, completed), contractor name, date of completion, photos etc.) on the system at the time **of the payment**
3. **Mandate public disclosure of grants from recommendation to utilisation for enhancing transparency, accountability, and quality of spending.** This will include public disclosure of (i) status of grant from recommendation to utilisation (Grant, allocation, status of compliance, grant released, expenditure occurred) and (ii) status of outputs/projects across project lifecycle (whether project has been approved, tendered, ongoing or completed and amount paid along with aforementioned project information as in 2.d) undertaken through XVI FC grants for each ULGs on a public dashboard on www.cityfinance.in. (This practice already exists for rural grants through <https://egramswaraj.gov.in/>)

01

Introduction



India's fiscal federal structure is organised across three tiers of government: the union, the states, and Local Governments (LGs), which include Rural Local Governments (RLGs) and Urban Local Governments (ULGs). The theory of fiscal federalism holds that expenditure responsibilities should be assigned to the lowest level of government capable of effectively delivering public services⁸, and revenue-raising powers should be aligned with these responsibilities, in accordance with the principle that 'finance follows function'⁹.

The 74th Constitutional Amendment Act (CAA), 1992 was a watershed moment in strengthening the institutional and functional salience of ULGs¹⁰. It granted constitutional status to municipalities by inserting Part IXA into the Constitution and outlined their structure, electoral mechanisms, and functional responsibilities. The Amendment also introduced the Twelfth Schedule, assigning eighteen functions¹¹ to municipalities, including public health, sanitation, water supply, urban planning, and urban poverty alleviation.

However, the 74th Amendment left the assignment of ULG's revenue sources at the discretion of state governments. Article 243X empowers state legislatures to authorise municipalities to levy taxes, duties, tolls, and fees, and to assign specific tax revenues to municipalities. Article 243Y requires State Finance Commissions (SFCs) to recommend principles for the distribution of state revenues between the state and their local governments, as well as for determining the grants-in-aid to municipalities.

Transfers and revenue-sharing arrangements between tiers of government are a critical feature of public finance, helping address the vertical and horizontal imbalance faced by local governments. Since ULGs fall under the State List, with states responsible for determining both spending responsibilities and revenue powers, it is assumed that states bear the obligation to bridge the gap between what ULGs can raise and what they require to perform their functions.

Despite the expanded functional domain granted by the 74th Amendment, ULGs have continued to experience persistent vertical fiscal imbalances. Their expenditure responsibilities far outweigh their revenue-generating capacities, leaving them heavily reliant on higher tiers of government for fiscal support. The 74th Amendment has tried to correct this imbalance with Articles 280(3)(bb) and 280(3)(c), which mandate that the Union Finance Commission (UFC) recommend measures to augment the Consolidated Fund of a State to supplement the resources of panchayats and municipalities.

⁸ Oates, W. E. (1972). *Fiscal federalism*. New York: Harcourt Brace Jovanovich.

⁹ Bahl, Roy. (1999). *Implementation Rules for Fiscal Decentralization*.

¹⁰ While commonly referred to as Urban Local Bodies (ULBs) and Rural Local Bodies (RLBs), these institutions are constitutionally recognised and democratically elected governments. The continued use of the term 'Urban Local Bodies' underplays this status, reinforcing a perception of administrative subordination. Shifting to the terminology of 'Urban Local Governments (ULGs)' is not a matter of semantics but of recognising their rightful place as the third tier of governance, with the authority and responsibility to plan, govern, and deliver services. This terminological shift is essential to strengthening their institutional identity and embedding the spirit of decentralisation in India's federal architecture.

¹¹ National Institute of Public Finance and Policy. (1992). *State transfers to the urban local bodies*. National Institute of Public Finance and Policy.

The 74th Amendment formally acknowledged the fiscal claims of ULGs at the national level and provided a way for UFCs to address their financing needs. In doing so, the amendment not only reaffirmed the responsibility of state governments towards municipal finances but also positioned the union government as a co-responsible actor. The amendment elevated the role of the UFC as a critical institution for addressing vertical fiscal gaps and enabling municipalities to effectively discharge their constitutionally mandated functions.

Importantly, the role of UFCs extends beyond fiscal transfers. Over the years, successive FCs have offered crucial policy direction on urban governance reforms. They have identified and attempted to address systemic deficiencies in municipal finance and governance architecture including challenges related to SFCs, poor quality of financial data, and weak revenue-raising capacity of ULGs. Their recommendations have contributed to bridging fiscal gaps while gradually strengthening the broader ecosystem of the third tier of governance in India.

1.1 Finance Commissions as Drivers of Reform for ULGs in India

Following the 74th CAA, successive Finance Commissions (FCs) gradually began addressing the fiscal needs of ULGs. The X FC was the first to allocate grants to local governments, although it was an ad-hoc allocation intended for further distribution by state governments. Since then, the allocation of grants to local governments has steadily increased across successive Finance Commissions, both in absolute terms and as a share of the Divisible Pool (DP). Local government¹² grants rose from ₹5,381 crore during the X FC period (1995–2000) to ₹4.36 lakh crore under the XV FC period (2021–2026), growing from 1.38% to 4.23% of the divisible pool.

Table 1: Grants-in-aid: Quantum and Share in Divisible Pool

Finance Commission	LG Grants (INR crore)	LG Grants as % of DP	ULG Grants (INR crore)	% Share of ULG in DP	% of ULG Grant in LG Grants
X FC (1995–2000)	5,381	1.38%	1,000	0.26%	19%
XI FC (2000–05)	10,000	0.78%	2,000	0.16%	20%
XII FC (2005–10)	25,000	1.24%	5,000	0.25%	20%

¹² In this report, usage of the term 'Local Governments' refers to both Rural Local Governments (RLGs) and Urban Local Governments (ULGs). In case of any specific references, either the word RLG or ULG is used.

Finance Commission	LG Grants (INR crore)	LG Grants as % of DP	ULG Grants (INR crore)	% Share of ULG in DP	% of ULG Grant in LG Grants
XIII FC (2010–15)	87,518	1.93%	23,111	0.51%	26%
XIV FC (2015–20)	2,87,436	3.06%	87,144	0.93%	30%
XV FC (2020–21)	90,000	4.31%	29,250	1.40%	33%
XV FC (2021–26)	4,36,361	4.23%	1,55,628	1.51%	36%

With the exception of the XI FC period, where the share of LG and ULG grants dipped, there has been a steady increase in both allocation and share to ULGs. Further, different FCs have approached devolution formulas differently and have introduced new elements in the design of grant architecture.

Although not required to allocate grants to local governments under its specific terms of reference, the X FC recommended 100% untied grants to ULGs. These were to be distributed among states based on their share of slum population, using urban population figures from the 1971 Census. The X FC stipulated that state governments should prepare suitable schemes and issue detailed guidelines for the utilisation of grants. No amount was to be used for expenditure on salaries and wages.

The XI FC continued with untied grants but marked a subtle shift by earmarking a small portion of the grant to build financial databases for local governments. For horizontal distribution across states, the XI FC recognised that states bore greater responsibility to develop local governments as institutions of local self-government after the 74th CAA and that there was a need to promote decentralisation. The Commission therefore introduced the Index of Decentralisation and considered revenue effort by ULGs for horizontal distribution, marking the beginning of an equity and efficiency-based approach to ULG grant design.

The XII FC continued the trend of 100% untied grants but recommended prioritising water supply and sanitation. It also revised the criteria for horizontal distribution by replacing the Index of Decentralisation with an Index of Deprivation based on minimum needs indicators and expanded the 'distance from highest per capita income' criterion to include urban areas, enhancing equity in inter-state allocations.

The XIII FC recognised the need for local governments to benefit from the buoyancy of union taxes while adhering to the constitutional mandate of recommending only grants-in-aid under Article 275. It proposed that the volume of grants-in-aid for year 't' be fixed at 2.5% of the divisible pool of year 't-1'. The XIII FC was also the first to introduce performance grants, allocating 35% of urban grants as performance-linked. While untied in usage, these were conditional on states and ULGs meeting nine procedural and institutional reform requirements on improving accounts, audits, and data availability in ULGs. The XIII FC also introduced institutional reforms such as the establishment of State Property Tax Boards and a standardised template for State Finance Commission reports.

Building on this, the XIV FC facilitated a paradigm shift in fiscal decentralisation, with a significant jump in the quantum of grants awarded to local governments. However, it moved away from linking grants-in-aid with a fixed percentage of the previous year's divisible pool, instead prioritising predictable and stable transfers to local governments. It also retained a 20% performance component in urban grants. However, the XIV FC significantly simplified performance conditions, reducing them to just three.

Despite these efforts, performance grants under the XIII and XIV FCs fell short of driving meaningful reforms due to key limitations:

1. A uniform, one-size-fits-all approach that did not account for the diverse capacities of ULGs.
2. The quantum of annual performance grants per state was too small to incentivise serious reforms.
3. The absence of a robust monitoring mechanism.

The XV FC marked a departure from previous approaches. Although it faced data limitations due to the delayed Census, it acknowledged that India was more urbanised than official records suggested. Accordingly, it allocated approximately 36%¹³ of local government grants to urban areas, the highest proportion in Finance Commission history, thereby exceeding the 2011 Census-based urbanisation rate.

The XV FC also adopted a differentiated approach based on city size. Category I cities i.e. Million-Plus Cities (MPCs) received 100% performance-based grants tied to outcomes in air quality, water, and sanitation. Category II cities i.e. the Non-Million-Plus Cities (NMPCs) received 60% tied grants for solid waste management, water supply, and sanitation, and 40% untied grants. Three special grants were also introduced for urban health services, incubation of new cities, and shared municipal services.

Importantly, the XV FC, while continuing the reform agendas of previous Commissions, introduced a major shift by linking all grants to reforms and compliance. All ULG grants, whether tied, untied, or

¹³ The 36% share of local government grants allocated to urban areas includes special/additional grants.

performance-based, were subject to eligibility conditions:

1. Publication of provisional and audited annual accounts.
2. Notification of a property tax floor rate and demonstrating growth in collections aligned with the state's GSDP.
3. Constitution of the State Finance Commission and presentation of an Action Taken Report (ATR) in the state legislature before March 2024.

These eligibility criteria led to remarkable progress: 96% of ULGs uploaded audited annual accounts on the MoHUA's www.cityfinance.in (hereafter referred to as CityFinance) and 11 states¹⁴ constituted SFCs.

The XV FC also institutionalised a structured digital grant management system through CityFinance, enabling trackability, transparency, and reduced administrative burden. This became the first systematic mechanism for managing urban fiscal transfers in India. By enforcing mandatory eligibility conditions and enabling a digital compliance ecosystem, the XV FC resolved data availability issues, providing a stronger foundation for the XVI FC to build upon.

This report seeks to support the XVI Finance Commission in strengthening urban fiscal devolution. Our recommendations advance the efforts of previous Commissions, particularly the XV FC, and are driven by the recognition that ULGs play a crucial role in India's economic growth. These recommendations offer a contextual and forward-looking framework for the coming years and are designed to unlock the full potential of India's urban local governments.

1.2 Scope of the Report

This report has been prepared as per the Terms of Reference (ToR) issued by the XVI Finance Commission to develop a set of design principles for the devolution of funds to ULGs. The proposed framework recognises the evolving nature of India's urbanisation and seeks to address the structural fiscal imbalances faced by ULGs, through a strategic, equitable, and reform-oriented approach to urban fiscal devolution.

While the primary focus is on strengthening the fiscal architecture of ULGs, the report acknowledges that fiscal devolution cannot be addressed in isolation. Effective fiscal devolution must be complemented by systemic improvements in governance, institutional capacity,

¹⁴ Information on the formation of State Finance Commissions (SFCs) is based on publicly available data as of March 2025.

transparency, and performance management to ensure that resources translate into improved urban outcomes.

Accordingly, the report aims to:

- 1. Analyse the rural-to-urban transition** to understand the implications of dynamic urbanisation on municipal boundaries, institutional frameworks, fiscal responsibilities, and associated challenges.
- 2. Propose a simplified, ULG-centric framework** for fund devolution that enables ULGs to respond flexibly to their local needs while ensuring financial sustainability and accountability.
- 3. Recommend a differentiated approach** to grant design, tailored to the typologies and capacities of ULGs particularly distinguishing between large metropolitan and smaller ULGs.
- 4. Simplify and standardise grant conditionalities** to facilitate timely transfers, reduce discretion, and promote fairness, while leveraging digital systems to streamline the grant disbursement and compliance process.
- 5. Improve expenditure efficiency, and strengthen transparency and accountability mechanisms** through improved financial and output reporting, audit practices, and performance-based monitoring systems.

The scope of the report includes a review of the evolution of urban grant architecture across successive Finance Commissions, particularly from the X to the XV FC. It analyses the current fiscal and institutional challenges faced by ULGs, explores differentiated devolution strategies, and proposes reforms to enhance transparency, accountability, and the digital governance of grants. While this report does not focus on detailed macroeconomic projections, it presents an indicative quantum of local government grants, including those earmarked for ULGs. These estimates provide a practical framework for the recommendations, recognising that final allocations will reflect broader macroeconomic and fiscal considerations.

The report remains mindful of its mandate and scope. It does not include legal drafting of constitutional or statutory amendments, or state- and city-specific implementation plans. The preparation of this report was also subject to certain constraints. Notably, there is limited availability of disaggregated data on ULGs, particularly with respect to their institutional capacities, economic contributions, and the share of Finance Commission and State Finance Commission grants in their overall revenue mix. In addition, utilisation data for FC grants at both the state and ULG levels is sparse or inconsistent. It is also challenging to construct a clear, state-wise picture of overall public spending directed toward the urban sector. Despite these limitations, the report endeavours to offer the XVI Finance Commission a grounded and reform-oriented set of design principles to guide the next generation of urban fiscal devolution in India.

1.3 Approach

This report draws on a combination of primary field research, institutional experience, expert consultations, and secondary data analysis to inform its recommendations.

As part of our primary research, we conducted field visits to 23 ULGs and 5 RLGs across eight states to understand the ground realities of urbanisation in India. These visits focused on the experiences of rural–urban transition and of ULGs in implementing XV FC grants. They also covered the public finance management practices across ULGs. Our sample included both newly-constituted ULGs and existing ULGs that have undergone recent administrative expansions. To supplement these site visits, we also conducted telephonic interviews with officials from select RLGs to better understand the dynamics of the rural–urban transition.

Further, we leveraged insights from the National Conference of Mayors and Chairpersons on Strengthening Urban Local Governments in India, held on November 26, 2024, at Bharat Mandapam, New Delhi, and organised by the XVI Finance Commission in collaboration with Janaagraha. The conference brought together elected representatives from ULGs across India to share their challenges and potential solutions in utilisation of XV FC grants, which have informed our understanding of the systemic and institutional issues facing ULGs.

In addition, Janaagraha's role as the Programme Management Unit (PMU) for the implementation of XV FC urban grants at the Ministry of Housing and Urban Affairs (MoHUA) has provided us with extensive, first-hand insights into the design, compliance, and fund-flow processes of this grant framework. These insights have directly informed our recommendations to the XVI FC. We have further drawn on the experience of our work in states such as Assam, Karnataka, Kerala, Odisha, Punjab, Tamil Nadu, and Uttar Pradesh to understand the capacity constraints, implementation challenges, and on-ground realities faced by ULGs. These insights have been a core pillar of our research.

To strengthen the technical and thematic aspects of our work, we partnered with The Convergence Foundation and Jana Urban Space Foundation, leveraging their domain expertise in economic development and land use planning respectively. These collaborations have been especially valuable in designing the outcome-based components of our grant architecture.

We also engaged in expert consultations with Mr SM Vijayanand, Former Chief Secretary and Chairperson of the Sixth State Finance Commission (SFC) of Kerala, Dr C Chandramouli, former Registrar General and Census Commissioner of India, and the team at Center for Water and

Sanitation (CWAS) and Transform Rural India Foundation to further ground our recommendations in administrative and sectoral realities.

Our research approach combined both qualitative and quantitative methods. We analysed data from the Census of India, the CityFinance which provides financial, performance, and institutional information on ULGs, and other publicly available financial data, including municipal, state and union budget documents.

1.4 Overview of Chapters

This report addresses the key design challenges facing the XVI FC in urban fiscal devolution. It begins by contextualising the persistent gaps between urbanisation (the growth of population and economic activity in urban settlements) and municipalisation (the formal recognition of such settlements through the constitution of ULGs), and goes on to unpack the structural deficiencies in municipal finance that constrain effective urban governance. It then traces how successive FCs have approached urban grants, highlighting both progress and ongoing limitations, and builds towards a reform-oriented grant architecture that is sensitive to the institutional capacities and economic potential of different ULG typologies. Importantly, the report builds on the reform momentum of previous FCs, including increased transparency, fiscal discipline, and improved governance through data availability and digital grant administration mechanisms that prioritise compliance, accountability, and ease of implementation. The chapters are structured to first lay out the context and diagnosis, followed by detailed proposals on quantum, distribution, eligibility, and administration of grants to ULGs.

Chapter 2 sets the context for India's urbanisation. It discusses the varying definitions of urban and their implications on determining the urbanisation rate of India. While drawing comparisons with global definitions and alternate techniques of capturing urban growth, the chapter comments on the potential scale of urbanisation at present. The chapter also highlights a critical issue about the dissonance between urbanisation and municipalisation and explains why this happens. It ends with recommendations on how to better track urbanisation and support timely and planned urbanisation.

Chapter 3 highlights three critical structural challenges facing municipal finance in India: the absence of updated and disaggregated estimates of investment requirements, the fragmented and opaque institutional landscape of urban expenditure, and the critical dependence on intergovernmental grants. Together, these challenges affect the accountability, transparency, and

long-term sustainability of urban public finance. The analysis sets the stage for a reimagined grant architecture under the XVI FC that incentivises reform and strengthens the financial capacity of local governments.

Chapter 4 traces the evolution of allocations to ULGs by successive Finance Commissions, examining how they have responded to the fiscal needs of ULGs. It analyses the quantum of grants, rural–urban distribution patterns, and horizontal allocation criteria, capturing both the successes and the limitations of past approaches. It also reviews the grant architecture adopted by previous Commissions, assessing their effectiveness through analysis of formulae, grant types, conditionalities, and end use. Drawing from this analysis, the chapter provides recommendations for the XVI FC on the total quantum of local government grants for the 2026–31, the urban share in these grants, formulas for horizontal distribution among states, and the guiding principles for grant architecture.

Chapter 5 examines how successive Finance Commissions have approached reform incentives, culminating in an analysis of the XV FC's paradigm shift to mandatory compliance. Building on this historical experience, we propose an improved eligibility framework for the XVI FC that maintains reform progress while addressing implementation challenges.

Chapter 6 addresses the core question of urban grant architecture under the XVI FC: the distribution of grants among ULGs within states based on their varying typologies and capacities. The chapter examines two key dimensions: (i) population-based classification of ULGs; and (ii) the types of grants best suited to enable meaningful urban outcomes for these ULGs. Through an analysis of inter-ULG disparities, institutional variations, and capacity differentials, the chapter proposes a differentiated grant architecture that builds on historical lessons while addressing contemporary urban governance challenges. The chapter recommends specific population categorisations and corresponding grant typologies for the XVI FC.

Chapter 7 reimagines the digital administration of urban grants under the XVI FC, building on lessons from the XV FC period. The chapter identifies core issues across the grant lifecycle, from burdensome compliance processes to fragmented data systems and limited public visibility. It proposes simplifying compliance and verification, enabling real-time rolling disbursements, and ensuring end-to-end digital integration with public disclosure. The recommendations are grounded in principles of fiscal autonomy, digital interoperability, and administrative ease to ensure timely, accountable, and effective utilisation of FC grants.

02

India's Urban Landscape



This chapter sets the context for India's urbanisation. It discusses the varying definitions of urban and their implications on determining the urbanisation rate of India. While drawing comparisons with global definitions and alternate techniques of capturing urban growth, the chapter comments on the potential scale of urbanisation at present. The chapter also highlights a critical issue about the dissonance between urbanisation and municipalisation and explains why this happens. It ends with recommendations on how to better track urbanisation and support timely and planned urbanisation.

2.1 Definition of Urban in India

According to the 2011 Census, India is 31% urban, with 318 million people (26%) in 4,041 statutory towns and 54 million (5%) in 3,892 census towns¹⁵. Statutory Towns (STs) are settlements defined as urban by state municipal legislation and governed by elected Urban Local Governments (ULGs), such as municipal corporations, municipalities, municipal councils, town panchayats, and cantonment boards. Census Towns (CTs)¹⁶, on the other hand, are settlements identified as urban by the Census of India but not officially notified as statutory towns by state governments.

The 74th Constitutional Amendment Act (CAA) provides the framework for the criteria to be used by state governments to notify a ULG. However, the criteria for classifying statutory towns are at the discretion of state governments. States use varying combinations of mainly four criteria — population, density, economic activity, and revenue generation, to designate or notify settlements as statutory towns. Each state applies these factors differently, creating unique definitions across India (refer to Annexure 2.1 for state-wise definitions). Further, states often use different qualifying thresholds even when applying the same criteria. For instance, while Tamil Nadu requires a population of 30,000 to convert a Gram Panchayat (GP) to a town panchayat, Telangana and Kerala set this threshold at 20,000 and Himachal Pradesh at 2,000.

The Census of India uses a population threshold of 5,000, to define an urban area — a definition deemed too stringent by a 2016 World Bank Report, which estimated that the country's urban population was already over 50%.

According to the 2011 Census, 54 million people (more than the population of South Africa¹⁷) lived in 3,892 census towns. Despite exhibiting urban density, however, these towns are governed as rural.

¹⁵ Census towns are settlements identified as urban by the Census of India.

¹⁶ The Census of India classifies those villages as Census Towns (CTs) which satisfy the following three conditions:

- A minimum population of 5,000
- At least 75% of the male main working population engaged in non-agricultural pursuits; and
- A density of population of at least 400 persons per sq. km.

¹⁷ Statistics South Africa. (2012). Census 2011 Statistical release (P0301.4). Pretoria: Statistics South Africa.

Rural local governments are neither mandated nor equipped to deliver urban-like services under the Eleventh Schedule of the Constitution, thus limiting their access to essential urban services such as networked water supply, sewerage, stormwater drainage, and street lighting. This significant gap between classification and governance leaves such areas underserved¹⁸. Therefore, how statutory towns are defined under municipal acts, and the transition process itself, has far-reaching consequences on the planned urbanisation of census towns and peri-urban areas.

2.2 Pattern of Urbanisation

Currently, India has close to 5,000 statutory towns — yet these towns do not function as isolated urban units. Instead, they demonstrate India's spatial pattern of urbanisation: clusters of cities and towns with overlapping economic and physical geographies.

The distribution of India's urban population is relatively balanced across city sizes, with approximately one-third living in cities with populations above 1 million, another third in cities with 100k-1 million, and the remaining third in cities with fewer than 100k.

Table 2: Population Category Wise Number of ULGs and Percentage Share of Population

ULG Population Category	Number of ULGs	Urban Population (%)
>4 million	7	15
1–4 million	36	17
500K–1 million	44	9
100K–500K	377	23
<100K	4,360	36
Total	4,824	100

Further, 50% of India's urban population lives within 60km of a city with a population over 1 million, and 92% live within 60km of a city with over 100K population.

¹⁸ Ashish. (2023, July 11). A column, a rebuttal, and what are census towns anyway? Econ for Everybody. Retrieved from <https://econforeverybodyblog.wordpress.com/2023/07/11/a-column-a-rebuttal-and-what-are-census-towns-anyway/>

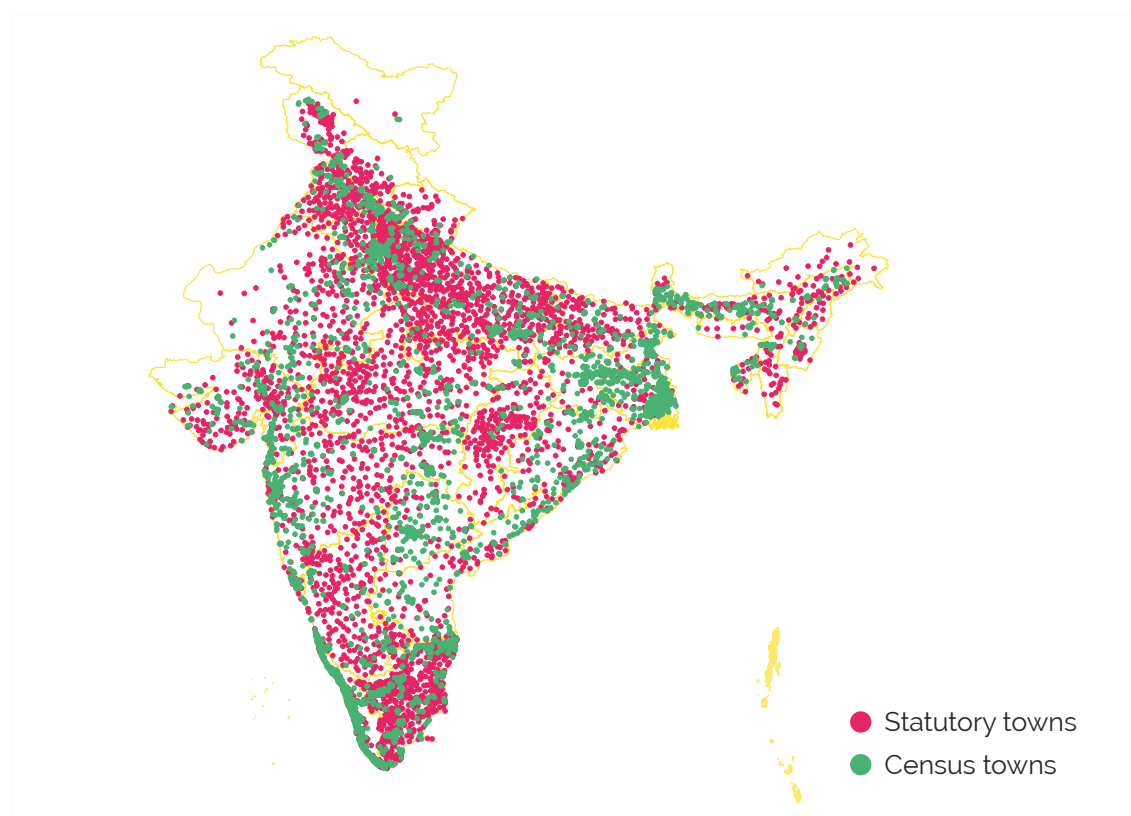


Figure 1: Distribution of statutory and census towns as per Census 2011

This spatial contiguity reveals the enormous potential for agglomeration economies. Urban clusters can drive job creation, platform and gig economies, and supply chain integration (e.g., farm-to-fork). They can also offer opportunities to reduce carbon footprints and scale innovations in transport, health, and commerce more efficiently across connected urban regions.

2.3 Current Extent of Urbanisation

India's urban footprint is expanding rapidly. Current estimates suggest that cities host over 800 million¹⁹. A 2019 technical report by the Ministry of Health and Family Welfare (MoHFW) on urban population projections estimated that the urban population in 2021 reached 34.5%. The UN's World Urbanization Prospects projects the urbanisation rate to increase to 41% by 2031. However, alternative methodologies using satellite data and morphological analysis suggest higher levels of urbanisation. The Global Human Settlements Layer (GHSL) of the Group on Earth Observations at the European Commission estimated that India was 63% urban in 2015, almost double the urbanisation rate of the 2011 Census. Other studies using demographic and spatial criteria estimate the current urbanisation rate at 45%²⁰.

¹⁹ United Nations, Department of Economic and Social Affairs, Population Division (2015). World Urbanisation Prospects: The 2014 Revision.

²⁰ Ibid

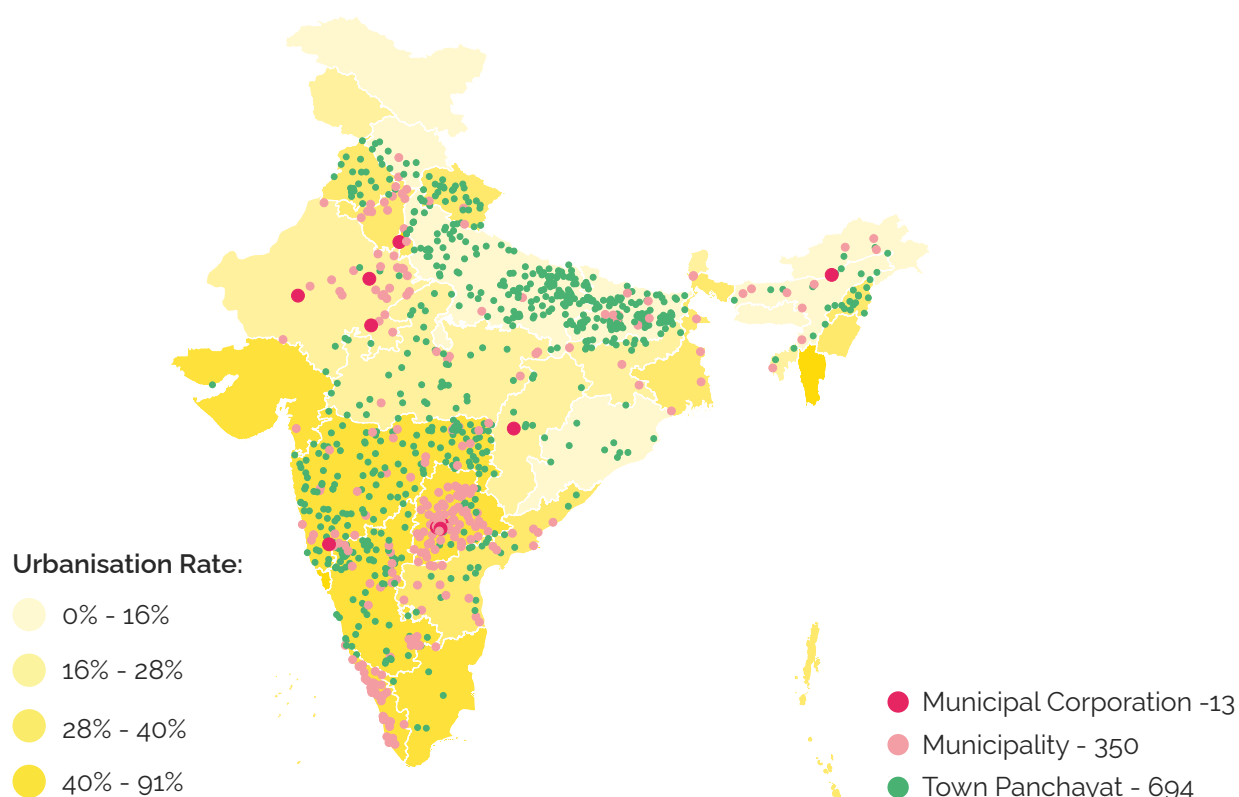


Figure 2: Distribution of newly constituted ULGs post 2011 Census

Official records currently do not capture the scale and speed of urban growth. The lack of updated and verified data on urbanisation, either in the form of a Census or a comprehensive list of statutory towns, is a critical impediment to understanding urbanisation and its trends across states and regions. The declaration of new ULGs or mergers follows an ad-hoc and opaque process, with state-level notifications not readily accessible, making it challenging to maintain accurate records of statutory towns.

Beyond the Census and state-level notifications, there are two centralised sources that compile information on statutory towns:

1. The Local Government Directory by the Ministry of Panchayati Raj (MoPR)

The LGD serves as the official register of local governments. However, it does not provide the comprehensive data required for policy planning. The directory is not systematically updated with new constitutions or de-notifications, and the corresponding Gazette notifications are often missing²¹. Critical identifiers such as Census codes, which are essential for data mapping and

²¹ For instance, several newly constituted ULGs in states such as Karnataka, Gujarat, and Telangana are not yet reflected in the LGD. Conversely, some cities that have been de-notified by state governments continue to be listed as active ULGs. In the case of Delhi, the LGD still shows the erstwhile three separate municipal corporations, even after their merger into a single entity. These instances are based on a review of the LGD conducted in January 2025.

integration, are inconsistently available. The directory also lacks detailed metadata, including area and ward-level information. The absence of consolidated, downloadable datasets and API access significantly limits the utility of the LGD for large-scale analysis and policy planning.

2. CityFinance, a platform by the Ministry of Housing and Urban Affairs (MoHUA)

CityFinance hosts MoHUA's official grant management system for XV FC grants, requiring ULGs to register to receive their annual funding. As of 30 June 2025, there are 1,057 new ULGs²² registered on the portal, (refer to Annexure 2.3 for a state-wise listing of number of ULGs constituted since 2011) with a total population of approximately 26 million. This is a significant increase from the number of ULGs in the 2011 Census. State governments update any newly constituted or de-notified ULGs on the platform to ensure that only eligible entities are included in grant calculations. This administrative necessity makes CityFinance a valuable data source on India's expanding urban footprint. However, states are not mandated to provide the details of the newly constituted ULGs in a timely or systematic manner, which makes it difficult to track the constitution of the ULGs and get detailed information about them.

Hence, there is a pressing need to strengthen the LGD as the single source of truth for all information related to local governments in India. The following are a few recommendations for strengthening the LGD:

- 1. The MoHUA and MoPR must jointly revise the Standard Operating Procedures (SoPs) for updating newly notified or de-notified LGs and coordinate closely with state governments to ensure that the LGD is a reliable and updated source on the number of local governments in India. This can be achieved through timely updates on the constitution, merger, and denotification of local governments.**
- 2. The LGD must maintain comprehensive, standardised data on each local government, including name, year of formation, area, population, shapefile of boundary, names of elected representatives and administrative heads, and number of zones or wards, etc.**
- 3. To enhance accessibility and integration, the LGD should also offer API-based access to this information should be made available to ensure seamless use by various government systems and stakeholders.**

Over time, this validated and dynamic list should be formally adopted as the authoritative dataset for determining the number and characteristics of ULGs and GPs particularly for calculations related to Finance Commission grants, such that future FCs do not struggle for base information.

²² Bihar serves as a striking example of this trend: while only 11% of the state's population lived in statutory towns as per the 2011 Census, the state now records ~14% living in notified urban areas. According to the Bihar Economic Survey 2022-23, the state has constituted 111 new nagar panchayats along with nine new nagar parishads.

2.4 The Disconnect Between Urbanisation and Municipalisation

While 1,057 new ULGs have been notified by states since the 2011 Census, data suggests that several settlements, despite exhibiting urban characteristics or meeting the criteria detailed in their state's municipal acts (refer to Annexure 2.1), continue to be governed under rural administrative frameworks. This highlights a persistent disconnect between urbanisation (the growth of population and economic activity in urban settlements) and municipalisation (the formal recognition of such settlements through the creation of ULGs). This disconnect is evident in our analysis of two datasets:

- 1. Census Towns: The majority of 3,892 census towns continue to be governed as rural.** Given the absence of a comprehensive, publicly available listing of census towns²³ and their governance status, we undertook an analysis of the notification orders of 97 newly constituted ULGs in Karnataka. We examined their composition, specifically whether they were formed from single or multiple GPs, whether entire GPs were absorbed into the new ULGs, and whether any of the areas previously held the status of 'census towns'. Our analysis revealed that only 24% of the census towns were upgraded to ULGs. Extrapolating this pattern nationally, it is highly likely that a significant proportion of the 3,892 census towns identified in the 2011 Census continue to be governed as rural settlements.
- 2. Large villages with urban characteristics:** India has approximately 24,000 large and very large villages²⁴, each with a population exceeding 5,000. As per the 2011 Census, these settlements together house 196 million people — around 16% of the country's population. However, despite their demographic scale and urban characteristics, these settlements are not recognised as urban. As a result, they are excluded from urban infrastructure, housing, and employment policies. Under an alternative definition, these settlements would account for over half of India's urban population — pushing the national urbanisation level up to 47%²⁵.

²³ One-to-one mapping of a census town with a gram panchayat is also not always possible because even though a census town is congruent to a village boundary, its congruence to a gram panchayat is not available.

²⁴ Jana, A., & S. A. (2019, January 23). India's missing middle: 24,000 'villages' with populations greater than towns lose out on policies for urban areas. Governance Newsletter. Retrieved from <https://www.indiaspend.com/indias-missing-middle-24000-villages-with-populations-greater-than-towns-lose-out-on-policies-for-urban-areas/>

²⁵ Ibid

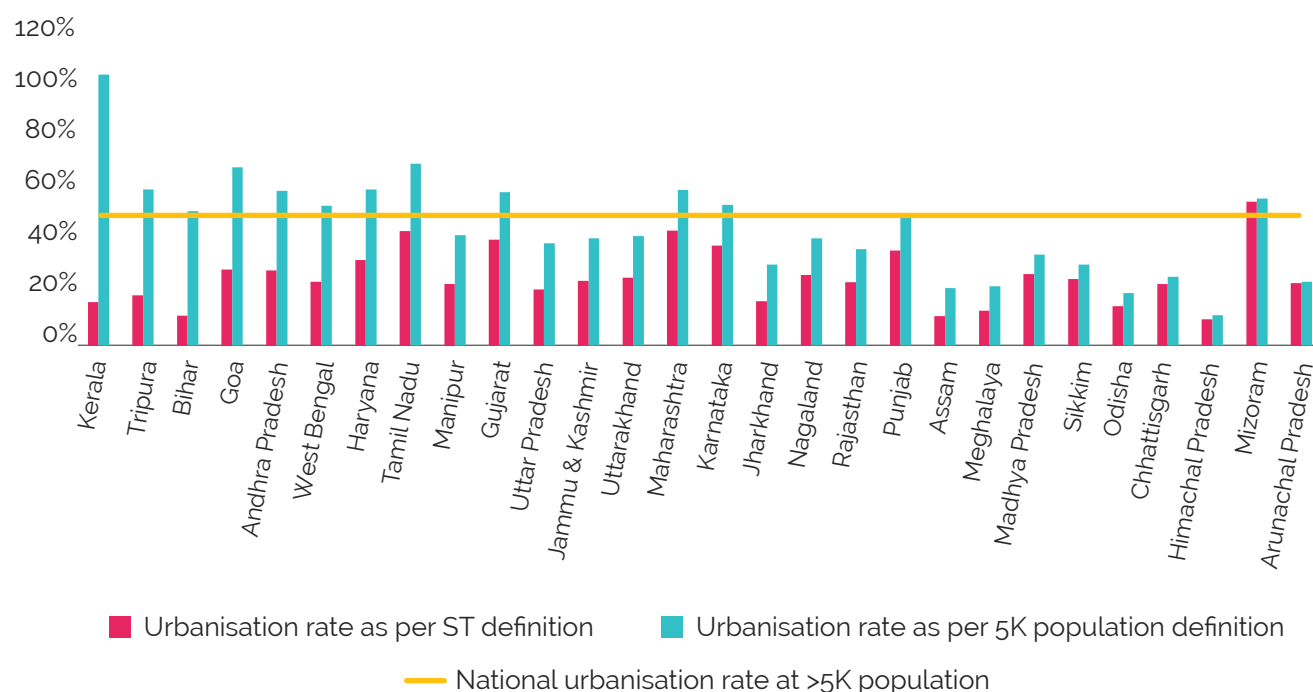


Figure 3: Urbanisation rate if the definition of urban is 5k+ population

In India, municipalisation is predominantly an ad-hoc and politically-determined process, rather than a systematic or planned one. A gram panchayat is reclassified as a statutory town only when the state government notifies it as a ULG. As previously detailed, state governments use varying combinations of four criteria to define urban areas: population, density, economic activity, and revenue. However, only 17²⁶ of the 28 states explicitly detail these criteria in their municipal laws. More critically, most municipal acts do not prescribe the steps required to transition rural settlements into statutory towns. In the absence of such procedures, municipalisation remains discretionary and fragmented, contributing to the broader pattern of unplanned urbanisation.

Our field interactions in nine states suggest that the process of transitioning from a gram panchayat to a ULG is typically initiated by the elected representatives of the area. The district administration then evaluates whether the area meets the eligibility criteria for ULG status. The final notification is issued by the state's Urban Development Department (UDD). Figure 4 illustrates this process and highlights that the decision to initiate the transition rests with the state's political leadership.

²⁶ Arunachal Pradesh, Bihar, Goa, Haryana, Himachal Pradesh, Jharkhand, Karnataka, Kerala, Maharashtra, Mizoram, Nagaland, Odisha, Sikkim, Tamil Nadu, Telangana, Tripura, and West Bengal, are the only states that explicitly define the criteria for areas to qualify as urban settlements in their municipal acts.

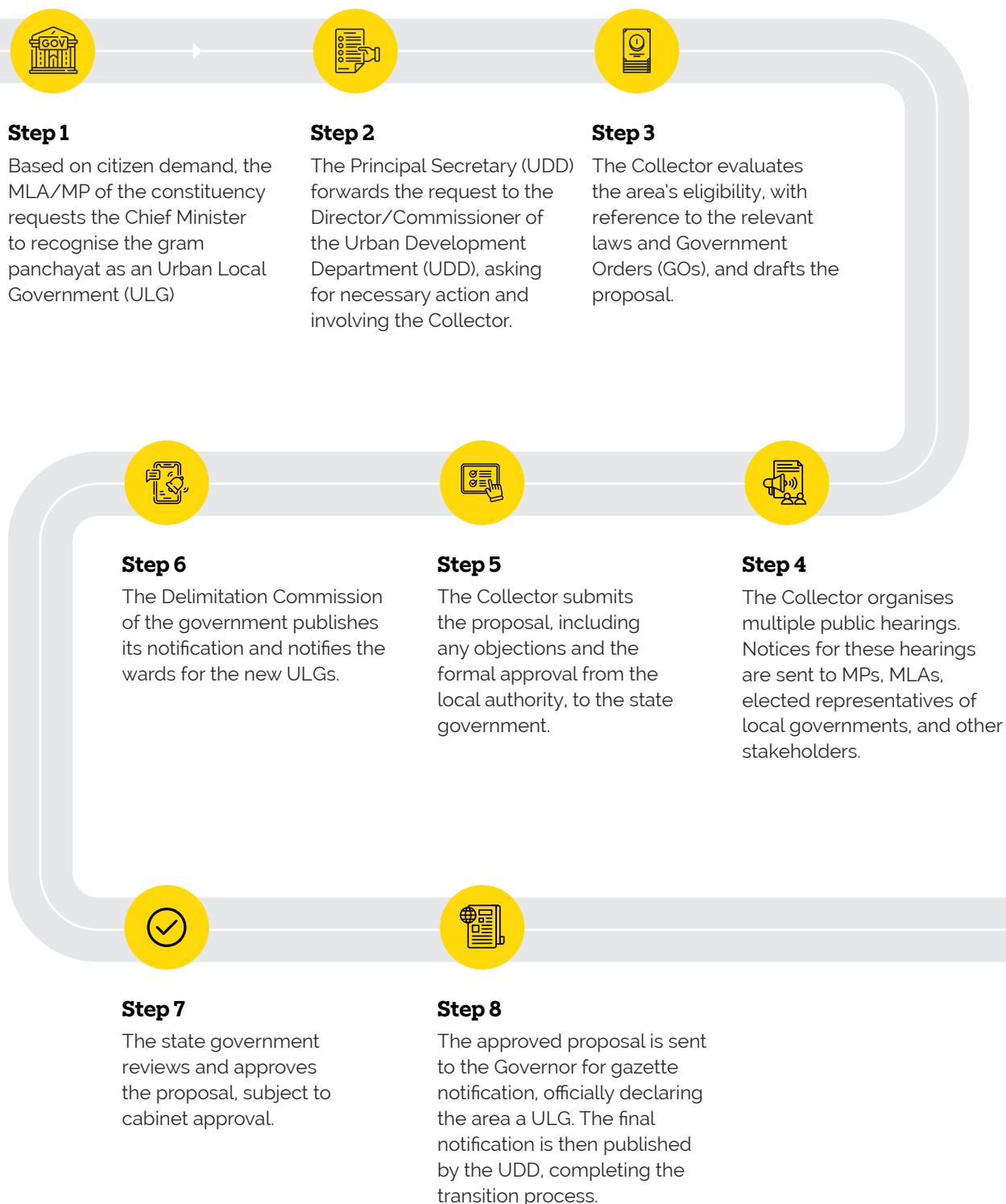


Figure 4: Commonly followed process for transition from RLG to ULG

However, this process and its associated decisions are not always straightforward. Transitions are often contentious and politicised, driven by conflicting interests among local actors, with some advocating for 'urban' status and others seeking to preserve a 'rural' identity.

2.4.1 Incentives and Disincentives of Transition

As outlined in the preceding section, the decision to pursue rural-urban transition is often driven by local stakeholders and how they weigh competing incentives and disincentives. Five key factors often drive this transition:

- 1. Citizen aspirations for improved services:** Urban areas were considered synonymous with better services, more organised infrastructure, reliable utilities, and access to basic amenities. In Himachal Pradesh, a growing transit settlement with 2,500 residents and a daily footfall of over 5,000 faced significant challenges with solid waste management, with only two part-time workers and no garbage collection system. Repeated notices from the National Green Tribunal (NGT) highlighted the urgency of the issue. With its limited resources and administrative capacity as a gram panchayat, the settlement sought town panchayat status to access municipal resources and enhance service delivery. During field visits, many ULGs expressed similar aspirations, hoping that the transition to a ULG would lead to better services and infrastructure.
- 2. Need for better governance structure and response rate:** In a gram panchayat in Tamil Nadu, conversations with local officials revealed the limited administrative capacity and autonomy at the village level. The panchayat secretary shared that while gram sabha meetings are held, citizen participation is minimal and often restricted to listening to the accounts being read aloud; there is little opportunity for citizens to suggest new projects. The panchayat secretary noted that, key decisions and project approvals, such as for roads, water connections, or streetlights, are handled by block-level authorities and line departments. This centralisation of functions delays grievance redressal and service delivery. In contrast, ULGs in the region have greater administrative autonomy and dedicated staff for core services like waste management, street lighting, and water supply, enabling them to respond to citizen needs more efficiently and with shorter turnaround times. Field visits to all the RLGs studied confirm that these governance limitations frequently lead to inefficiencies in service delivery and slower response times in rural areas²⁷.
- 3. Electoral considerations in boundary expansion:** The transition of growing peri-urban villages into statutory towns can concentrate voters with shared interests, potentially creating a reliable electoral bloc. By expanding a municipal boundary, elected representatives may be able to

²⁷ Interviews conducted in Kakori and Chinhat Gram Panchayats in Uttar Pradesh, and Bakaitari Gram Panchayat in Assam.

increase their influence over local urban affairs²⁸. For instance, in Madhya Pradesh, several gram panchayats were merged with an industrial town during its municipal upgrade, despite limited evidence of urban characteristics such as higher population density or increased demand for municipal services. According to authorities, the transition was driven more by political pressure from elected representatives than by substantial changes in the settlement's urban characteristics.

4. **Increased grants and funds for infrastructure development under direct control of local government:** While union and state government allocations for welfare programmes are higher for GPs, the funds received directly by them for infrastructure development are significantly lower. In Tamil Nadu, for instance, a ULG spent up to ₹4,754 per person on capital infrastructure, while a GP with similar population spent as little as ₹45 per person, revealing a staggering 106-fold difference²⁹ (refer Annexure 2.6). A junior engineer in Telangana noted that large-scale projects previously out of reach could finally be taken up after the area was declared a municipality. Similarly, an elected representative from a town panchayat in Himachal Pradesh mentioned that as a GP, they lacked the resources to even install, let alone maintain, basic amenities like streetlights. These experiences demonstrate that the prospect of increased funding for infrastructure development often motivates rural settlements to seek urban status.
5. **Increase in land prices and rental income from municipal properties:** Newly constituted ULGs experience a sharp rise in land prices and rental values, driven by improved infrastructure, limited land availability, and the expectation of better civic amenities. In Himachal Pradesh, following a market reassessment, a newly notified ULG witnessed a staggering 3,000% spike in the rental value of municipal shops, from ₹50 per month to ₹2,000 per month. Similarly, in Uttar Pradesh, land parcels previously valued at ₹1,000 per sq. ft. were revalued between ₹1,700 and ₹2,000 per sq. ft. shortly after the urban notification.

Despite the benefits of transitioning from rural to urban governance for local governments and citizens, some stakeholders resist this change for the following reasons:

1. **Fear of loss of power by the elected representatives of GPs:** In GPs, the sarpanch holds significant power, with decision-making often driven by elected representatives. The transition, which often involves the merger of multiple GPs and new elections, is seen by local leaders as a threat to their authority. Moreover, ULGs operate within a more structured governance framework, where the executive body plays a central role in decision-making, diminishing individual political influence over administrative processes. This loss of authority is often the

²⁸ Mahesh, K. (2025, March 25). Govt announces 6 new municipalities, amendments to Municipalities and Panchayat Acts. The Times of India. Retrieved from <https://timesofindia.indiatimes.com/city/hyderabad/govt-announces-6-new-municipalities-amendments-to-municipalities-and-panchayat-acts/articleshow/119439864.cms>

²⁹ Six local governments (RLGs and ULGs) with comparable population sizes were selected from Tamil Nadu and Uttar Pradesh for FY 2021–22. Financial data including own revenue, grants from Central and State Finance Commissions, other receipts, and expenditure were compiled for RLGs from the MoPR by the XVI FC and was retrieved for ULGs from CityFinance. Percentage differences were calculated to highlight disparities in receipts and capital spending.

primary reason why sarpanches and pradhans resist the transition. Field observations from two newly constituted ULGs in Himachal Pradesh and Uttar Pradesh support this³⁰.

2. **Concerns over loss of funding for rural welfare programmes:** State and local leaders fear that transitioning to ULGs could result in a reduction in financial inflows³¹. In Bihar³², for instance, the mukhiya of a rural settlement expressed concern over the potential loss of welfare benefits following the proposed reclassification of the area as part of a nearby ULG. Programmes like the Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA), which currently provide guaranteed wage employment and discretionary funds to the panchayat, would no longer be available post-transition. According to the mukhiya, this shift would disproportionately impact households who rely on MGNREGA for stable income. Similar concerns extend to housing, drinking water, healthcare, and education schemes that target rural settlements.
3. **Stricter building development laws:** While building bylaws exist in GPs, their enforcement is often lax, unlike ULGs with stricter mechanisms requiring building permissions, licenses, development regulations, and compliance with the National Building Code (NBC) of India. These regulations are highly prescriptive, mandating uniformity in urban building forms, layouts, and safety norms to manage higher population densities and complex infrastructure requirements³³. For example, Odisha Municipal Act, 1950 clearly states that the construction/reconstruction of a building can only begin after obtaining permission from the executive officer of the municipal area whose decision is based on the particulars of site plan, ground plan, and building specification documents submitted by the applicant³⁴. Moreover, the executive officer has the power to refuse permission for the construction if the application does not comply with the specified requirements. In contrast, rural areas typically lack such detailed codes, and enforcement is weak, leading to more informal and unregulated construction practices. This often results in haphazard development and safety risks, especially as urban sprawl encroaches into rural fringes where norms are flouted.
4. **Higher financial burdens like increased property and other taxes:** The transition to ULGs often results in higher property taxes, water charges, and solid waste management fees, placing a financial strain on residents. This has proven to be a significant cause of resistance across states. For example, in a ULG in Assam, property tax increased from ₹50–100 to ₹500 after urban notification. In the same ULG, water supply, previously managed by the Public Health Department, shifted to the ULG, which now charges a user fee of ₹100 per household. Resistance to the transition due to these financial pressures was observed in all the ULGs we visited. However, 4 out of 23 ULGs shared success stories of how local leadership effectively convinced citizens to pay taxes and access services.

³⁰ Reference taken from Kandaghat (HP) and Mohanlalgarh (UP).

³¹ Ravi, S. (2023, March). What is "Urban/Rural" India? Economic Advisory Council to the Prime Minister. Retrieved from <https://eacpm.gov.in/wp-content/uploads/2023/07/15-What-is-Urban-Rural-India.pdf>

³² Van Duijne, R. J. (2019). Why India's urbanization is hidden: Observations from "rural" Bihar. *World Development*, 123, 104610.

³³ Shivalik Institute. (2024, March 22). Building codes and Indian cities. Shivalik Institute. Retrieved June 20, 2025, from <https://www.shivalik.institute/articles/building-codes-and-indian-cities>

³⁴ Odisha Municipal Act, § 264, Act No. 7 of 1950 (India).

- 5. Threat to citizen participation and local self-governance:** GPs are run by elected representatives, whereas cities are typically managed by bureaucrats³⁵. In GPs, development work is often driven by inputs from the gram sabha, village development plans (like GPDP), and other participatory mechanisms. In contrast, urban areas often lack structured and functioning platforms for citizen participation. In Odisha, the Panchayati Raj department expressed concern over the loss of these platforms for citizen participation, the region's 'rural identity,' and the resentment that could arise from the discontinuation of certain rural-specific services.

2.4.2 Type of Transitions

Whether a rural settlement transitions into a ULG depends on how the incentives and disincentives are determined in a given context. The drivers for urbanisation of a settlement vary and influence how it becomes urbanised (refer to Box 1 below). In practice, depending on how gram panchayats are integrated into the urban system, rural areas transition into urban areas in two main ways:

1. Transition of GPs into a new ULG

- i. Single GP Transition: A single GP transitions into a new ULG.
- ii. Multiple GP Merger: Multiple GPs merge to form a new ULG. This can occur in one of two ways:
 - a. Complete inclusion: Entire GPs become part of the newly formed ULG.
 - b. Partial inclusion: Only a section of a GP is incorporated into the new ULG.

2. Expansion of existing ULG jurisdiction (Mergers) (Refer to Annexure 2.7 and 2.8 for notification samples)

- i. Full Merger: An entire GP is merged into an existing ULG.
- ii. Partial Merger: Only a portion of a GP is merged into an existing ULG.

Box 1: Drivers of Urbanisation in India

Across India, rural settlements are undergoing significant demographic and economic shifts. For example, a newly constituted ULG in Madhya Pradesh, located far from the nearest city, has experienced urbanisation driven largely by its role as a market town. As a hub for agricultural trade, this transition has led to increased footfall and economic activity in the area. With a blend of both urban and rural characteristics, this settlement can be described as 'quasi-urban.'

³⁵ "Urban Trap", Down To Earth, 1–15 March 2025 edition. Quote attributed to Chandrashekhar Pran, founder of Teesri Sarkar Abhiyaan, a Ghaziabad-based non-profit working to strengthen Panchayati Raj institutions. The article discusses rural-to-urban transitions in Rajasthan.

Urbanisation is also occurring due to spillover effects from large metropolitan centres, particularly in peripheral regions. The Rangareddy district in Telangana exemplifies this trend. During a visit to a ULG established in 2014, we observed significant population growth. The 2011 Census recorded 28,000 residents, but authorities now estimate the population has surged to approximately 90,000. Recently, the town panchayat received notification about the merger of four new GPs into the ULG, as the GPs are contiguous with the built-up area, reflecting the town's expanding functional boundaries. This growth necessitates an expansion of administrative jurisdiction to effectively manage the evolving urban landscape.

Since 2011, Tamil Nadu reduced the number of ULGs, from 721 to 651. This shift reflects strategic decisions by the state to expand certain ULGs through mergers with adjacent RLGs and upgrading existing ULGs.

In a discussion with the Joint Commissioner of Municipal Administration, it was noted that the traditional process of upgrading a gram panchayat to a town panchayat is slow and often leaves urbanising rural settlements without essential services. To address this, the state has opted to merge these rural settlements with neighbouring towns and municipalities, recognising that administrative boundaries often do not align with realities on the ground, where distinctions between rural and urban areas have already blurred. Municipalities such as Karaikudi, Tiruvannamalai, Pudukottai, and Namakkal were upgraded to municipal corporations through mergers with adjacent gram panchayats.

While a detailed diagnostic of urban and rural governance models, functions, funding mechanisms, and service levels is beyond the scope of this report, it is important to highlight the unique challenges faced by transitional areas and why they require special attention.

2.5 Challenges of Transitional Areas and Newly Constituted ULGs

Whether a settlement is governed as rural or urban, its residents expect and deserve adequate public services. Historically, an urban status has been associated with improved living standards. However, in many urbanising and newly notified ULGs, this expectation remains unmet. This service deficit is not incidental; it is the result of deeper systemic issues that hinder a smooth and sustainable transition from rural to urban governance.

This section examines the distinct challenges that transitional areas face both pre-notification, when settlements exhibit urban characteristics but remain governed as rural, and post-notification, when areas are formally designated urban but lack the planning frameworks, institutional support, and financial autonomy to function effectively.

Pre-notification Challenges

Transitional areas are often overlooked due to the absence of a structured policy framework. There is no national or state-specific framework to guide their transition; no institutional preparedness, planning protocols, or fiscal support to ensure that service delivery keeps pace with urbanisation. As discussed earlier, most transitions are driven by local demand rather than by proactive planning. By the time an area is notified as urban, it has already outgrown the rural governance system but lacks the institutional foundations to function as a ULG.

Samanta (2014) describes this condition as 'denied urbanisation' — places take on the physical form of cities but continue to function with the capacities and standards of villages³⁶. Infrastructure remains rudimentary: unpaved roads, incomplete drainage networks, patchy street lighting, and minimal or absent sanitation and waste systems.

The 73rd and 74th Constitutional Amendments established distinct governance structures for rural and urban areas. Rural administrations are not equipped to provide the services required for dense urban settlements, but urbanisation does not wait for municipalisation, and many such areas remain governed by panchayats even after attaining urban characteristics. Research shows that even after a place meets urban criteria, basic amenities and services remain poor if it stays under a gram panchayat that lacks capacity³⁷. These challenges in transitional areas can be broadly categorised into two main issues:

1. Exclusion from relevant urban developmental schemes

Transitional areas often lack access to urban infrastructure investments. Since they are not notified as statutory towns, they do not meet the eligibility criteria for most urban development schemes. These settlements typically continue to receive benefits under rural schemes, which are not designed for dense, urbanising populations, while remaining excluded from urban schemes.

For example, central schemes such as AMRUT, which fund urban infrastructure, primarily target statutory towns. A rapidly growing settlement under a panchayat would therefore be ineligible. At the same time, rural schemes for housing or road construction are often inadequate for the needs of larger, denser populations. This mismatch leaves critical infrastructure gaps unaddressed.

³⁶ Samanta, G. (2014). The politics of classification and the complexity of governance in census towns. *Economic & Political Weekly*, 49(22). wiego.org.

³⁷ Panda, P. K. (2023, July 11). Odisha launches Rural-Urban Transition Policy. *The Raisina Hills*. Retrieved from <https://theraisinahills.com/odisha-launches-rural-urban-transition-policy/>

Moreover, if urbanising areas remain classified as villages, they lack the fiscal autonomy and institutional tools needed to raise resources or upgrade service delivery.

2. Unregulated growth from planning deficits

Planning gaps further compound the challenge. Urbanising areas are rarely integrated into city master plans or regional development strategies. Building regulations, where they exist, are often poorly enforced, resulting in unplanned and fragmented development. In many cases, urbanising gram panchayats are absorbed into expanding municipal jurisdictions without a development blueprint. In the absence of anticipatory planning, urbanisation proceeds in an uncoordinated and unregulated manner, undermining service delivery in the long term.

There is a clear need to incentivise states to proactively and systematically identify urbanising areas, guide them through planned improvements in infrastructure, services, and institutional capacity, and notify them through a structured process. This would help mitigate the risks of unplanned urbanisation.

A dedicated rural–urban transition policy is essential to address these challenges before they escalate into systemic crises. At present, only Odisha has notified such a policy, while Rajasthan has introduced a draft bill on this subject.

Box 2: Rural–Urban Transition Policies in Odisha and Rajasthan

Odisha's Rural–Urban Transition Policy, 2023

Odisha is the first state in India to introduce a dedicated Rural–Urban Transition Policy, approved in July 2023. The policy provides a comprehensive framework for the governance, infrastructure, and financing of fast-urbanising rural areas to facilitate planned rural–urban transition.

Key mechanisms of Odisha's policy include:

- a. Advance planning and infrastructure upgrades:** Rather than introducing abrupt changes, Odisha's policy establishes a transition phase during which accelerated investments are made in infrastructure and services. This phase begins with the identification of an area for upgrade and continues until the end of the current panchayat's term, ensuring the area receives necessary improvements well before being formally notified as urban.

- b. Gradual administrative change with community involvement:** The policy mandates that an area will only be declared urban once the term of the existing gram panchayat representatives expires, thereby avoiding mid-term disruptions. In the interim, preparations for municipal governance are initiated, including ward delimitation and the planning of the new urban administration, with active involvement from local stakeholders (officials, elected members, and community groups).
- c. Institutional coordination (hub-and-spoke model):** To address governance silos, Odisha's policy establishes coordination committees and a tiered institutional structure. A state-level steering committee chaired by the chief secretary, along with subject experts, guides the process. The policy proposes a hub-and-spoke model, with the State Urban Development Authority (SUDA) acting as the central hub and District Urban Development Authorities (DUDAs) and Development Authorities (DAs) serving as spokes for implementation.
- d. Special funding provisions:** A notable feature of the policy is the creation of a special budget for transition areas. By earmarking funds specifically for upgrading rural settlements to urban standards, the policy addresses the funding gap associated with the infrastructure needs of these transitioning areas. Odisha's government channels resources, with support from state schemes and potentially union grants, to build urban infrastructure in advance. As the area transitions into a municipality and gains the ability to levy taxes, reliance on special funding will decrease. However, the initial investment helps prevent the infrastructure deficit from widening during the transition.

Source: Voice of Odisha. (n.d.). Voice of Odisha. Retrieved 20 June 2025

Rajasthan's Rural–Urban Transition Bill, 2023

The Rajasthan Rural–Urban Transition Bill, 2023 provides a structured framework to guide the conversion of rural areas into urban centres. It enables transitioning settlements to access both rural and urban development funds during the transition period, ensuring resource adequacy and continuity, as well as a monitoring and evaluation framework.

The primary objective of the bill is to ensure that development occurs in a planned and sustainable manner, rather than through uncontrolled sprawl. The bill also identifies key tasks to be performed by settlements, including the preparation of a baseline study and a Settlement Transition Enabling Plan (STEP), which will identify transition projects and the necessary resources. Additionally, the bill outlines specific procedures and timelines for various stages of the transition process, including the initial identification and notification of transition areas, the preparation of development plans, the implementation of infrastructure projects, and the eventual integration into existing urban governance structures.

Pre-notification Challenges

The formal notification of a rural settlement as a ULG is often viewed as a turning point and is expected to address longstanding governance and service delivery deficits. In practice, however, it frequently marks the beginning of a new set of challenges. These newly constituted ULGs are expected to deliver urban-level services without the corresponding administrative, financial, or technical capacity.

In the absence of a structured transition framework, the shift to urban governance is often abrupt and incomplete. Rather than enabling development, this transition can leave newly notified areas at a disadvantage and may be perceived by communities as a penalty for urbanising.

The following are some of the key challenges faced by newly notified ULGs:

1. Lack of a standard transition process, hindering a smooth institutional setup

India lacks a standardised process for transitioning rural local governments into urban local governments. The governance architecture under the 73rd and the 74th Constitutional Amendments differ significantly and necessitate complex institutional restructuring during the transition from gram panchayats to ULGs. This includes dissolving the panchayat, transferring assets and liabilities, and conducting municipal elections.

In the absence of a structured transition process, institutional memory and accountability can break down. Gram panchayats often do not maintain formal asset records, making it difficult to verify ownership and ensure a smooth handover. When a gram panchayat is dissolved, public infrastructure such as roads, water tanks, and buildings may not be properly inventoried, valued, or legally transferred.

The roles and responsibilities of local, district, and state-level stakeholders are not clearly defined, delaying the establishment of effective urban governance.

For example, a newly constituted ULG in Himachal Pradesh had to pursue legal action to claim its office building from the parent gram panchayat, owing to a lack of administrative clarity and accountability. Such disputes delay service delivery and obstruct the operationalisation of urban governance.

2. Unstructured legal and regulatory shifts

The notification of a ULG can result in an abrupt shift in regulatory frameworks including building bylaws, zoning norms, and municipal taxation. These changes often take effect without adequate public awareness or institutional preparedness, leading to unregulated construction, legal disputes, and confusion among residents. In some cases, abrupt implementation without a defined period of transition has led to non-compliance and public resistance.

A few states, such as Tamil Nadu and Himachal Pradesh, have introduced transitional provisions under Section 375A of the Tamil Nadu District Municipalities Act, 1920³⁸ and the Himachal Pradesh Municipal Act, 1994, respectively. However, these remain the exceptions rather than the norm.

3. Poor staffing capacity

Rural institutional capacity often persists even after notification. Many ULGs function without dedicated technical staff, trained administrators, or financial experts. Delays in appointment of key officials such as executive officers or chief municipal officers are common. In Madhya Pradesh, one newly constituted ULG waited two years for an executive officer to take charge. In Telangana and Himachal Pradesh, deputed staff are frequently tasked with managing several ULGs simultaneously, spreading administrative capacity thin. These constraints compromise basic service delivery and hinder the development of ULGs as effective institutions.

4. Weak revenue base and inconsistent state support

ULGs are expected to generate substantial revenue through property tax, user charges, and other forms of own-source revenue. However, many newly constituted ULGs begin with minimal or no revenue streams. In states such as Telangana, Uttar Pradesh, and Himachal Pradesh, ULGs are exempt from levying property tax for three to five years post-notification. Such exemptions, while intended as a measure to ease transition, prevent ULGs from mobilising the resources necessary to deliver on their new mandates.

Further, state support to newly notified ULGs is inconsistent and often limited to one-time grants. In Uttar Pradesh, for instance, the Nagar Srijan Yojana allocated ₹550 crores to 242 new or expanded ULGs, based primarily on population and area. Tamil Nadu's VI State Finance Commission recommended an annual grant of ₹20 lakhs for each newly constituted town panchayat. Telangana provided a one-time grant of ₹2 crore to each new ULG. While these efforts are commendable, they remain ad hoc and insufficient to meet the long-term infrastructure and capacity needs of transitioning areas.

³⁸ In the case of Tamil Nadu, Section 375A empowers the state government to appoint special officers to discharge the functions of municipalities or town panchayats until elected councils assume office. This provision allows the government to maintain administrative continuity during the transition from rural to urban governance. Further, amendments to the Act have extended the tenure of such special officers in specific cases (e.g., Courtallam and Bhavanisagar) through government notification, offering the state flexibility in managing the interim governance arrangements of newly constituted or upgraded ULGs.

In many cases, newly notified ULGs receive no additional support at all. One ULG in Madhya Pradesh experienced a 56% increase in population after the merger of 15 gram panchayats, but received neither additional staff nor enhanced funding. Despite the dramatic population growth and the corresponding increase in service delivery expectations, its budgetary allocation remained unchanged. This effectively penalises the area for transitioning.

2.6 Enabling Planned Urbanisation

There are critical gaps in the transition from rural to urban governance. Many newly constituted ULGs lack not only financial resources but also the required staff and technical expertise, as several state governments have yet to sanction or deploy adequate personnel.

In the pre-notification stage, criteria for mergers and transitions must be standardised to ensure a systematic approach and reduce discretion. In the post-notification stage, states must be held accountable for providing timely financial, governance, and technical support.

To enable more effective transitions, state governments should be incentivised through a rural–urban transition policy that prioritises improved infrastructure and service delivery in urbanising areas.

2.6.1 Urbanisation Premium for Transitional Areas and Newly Constituted ULGs

The XVI FC is uniquely positioned to catalyse a long-overdue reform in the management of India's rural–urban transitions. By formally recognising these 'transitional local governments' as a distinct cohort, the XVI FC can incentivise states to manage rural–urban transitions in a planned, capacity-ready manner. **We therefore propose the establishment of an Urbanisation Premium amounting to ₹20,000 crore for the 2026–31 period. This fund should be equally sourced from the FC's allocations to rural and urban local governments, acknowledging the shared governance responsibilities such transitions entail.**

Objectives of the Premium:

1. Incentivise states to implement systematic, forward-looking policies to manage rural-to-urban transitions.
2. Address infrastructure and service deficits in transitional areas.

2.6.1.1 Eligibility for the Premium

The Premium will only be awarded to state governments that notify a Rural–Urban Transition Policy (RUTP). Two cohorts of local governments will be eligible for the Premium:

1. **ULGs constituted between the 2011 Census and 30 September 2026:** This cohort is selected to address two key concerns of the transition. First, it would provide support to ULGs constituted without a planned transition process. Second, it would allow states an 8-month period in the XVI FC's term to notify gram panchayat already identified for transition.
2. **Urbanising gram panchayats identified as transitional areas by the state government:** From 1 October 2026 to 31 March 2027, states must identify urbanising gram panchayats set for transition during the remaining term of the XVI FC. This would ensure that future transitions follow a structured process as per the RUTP.

These local governments would receive the Urbanisation Premium, over and above the regular XVI FC grants to those LGs.

2.6.1.2 Proposed End-use of the Premium

Infrastructure development is fundamental to sustainable and inclusive city-building³⁹. Core networked infrastructure — such as piped water supply, sewerage, stormwater drainage, street lighting, and solid waste management — forms the foundation for urban functionality and citizen well-being. These systems are critical to safeguard public health and environment: reliable water supply prevents contamination and waterborne diseases, while sewerage and drainage infrastructure manage waste and runoff, reducing the risk of flooding and disease outbreaks⁴⁰.

In addition to these essentials, cities require robust connectivity and accessibility to thrive. Infrastructure such as roads, public transport, and digital networks ensures the smooth flow of goods, people, and information, laying the groundwork for more resilient, innovative, and economically vibrant cities. Enhanced connectivity also fosters social inclusion by connecting communities to employment, education, and healthcare opportunities⁴¹.

We propose that the grant support investment in core infrastructure such as roads, walkways, footpaths, piped water, sewerage, drainage, street lighting, and solid waste management. The grant may also fund facilities that strengthen economic and social linkages, including local markets, bus terminals, and connections to health and education hubs.

³⁹ Fulgar, J. I. L. (2024, September 7). How infrastructure fuels new city development. Philippine Daily Inquirer. <https://business.inquirer.net/478698/how-infrastructure-fuels-new-city-development>

⁴⁰ Bittu, A. K., & Rao, P. S. N. (2024). Urban sanitation in Indian cities: A case study of Patna. South East European Journal of Public Health, 25(S2), 411.

⁴¹ Fulgar, J. I. L. (2024, September 7). How infrastructure fuels new city development. Philippine Daily Inquirer. <https://business.inquirer.net/478698/how-infrastructure-fuels-new-city-development>

2.6.1.3 Inter-state Distribution of Premium

To allocate the ₹20,000 crore Urbanisation Premium, we evaluated three possible formula basis:

1. Urbanisation potential of states, calculated as

- i. Projected 2021 urban population (MoHFW) minus 2011 statutory-town population
- ii. Projected 2021 urban population (MoHFW) minus projected 2021 statutory-town population

2. Current untapped urbanisation, captured by Census Town (CT) population, Census 2011

3. Total State population and area, Census 2011

Method 1 aimed to identify the urbanisation potential of a state by creating a proxy calculation based on the gap between a state's projected urbanisation level and its current urbanisation rate. However, we found that these projections are highly sensitive to model assumptions and fail to accurately reflect ground realities. In many instances, projected figures diverged significantly from actual urban growth trends, rendering them unreliable for equitable fund allocation (refer to Annexure 2.9).

Method 2 aimed to capture latent urbanisation based on the 2011 population of Census Towns (CTs). CTs are settlements with urban characteristics that are yet to be notified as statutory towns, making them a practical indicator of transition potential. However, since CT classification occurs before population counts and remains fixed until the next Census, this method reflects legacy definitions rather than real-time urban growth between Censuses⁴². It also risked skewing allocations toward states where CTs already represent a significant share of the urban footprint, as in Kerala (refer to Annexure 2.9).

We therefore propose using **Method 3**, which distributes the Urbanisation Premium based on a **state's population and area, weighted 90:10**, using data from the 2011 Census. While this method does not directly capture urbanisation potential, it offers a balanced and administratively simple approach that reflects both demand (population) and delivery complexity (area). Importantly, it accounts for both rural and urban characteristics, aligning with the grant's dual focus on transitioning and newly transitioned local governments. This approach ensures that no state is unduly advantaged or penalised due to data volatility or definitional ambiguities (refer to Annexure 2.9).

Further distribution to transitional areas would be based on the share of each identified local government's population in the total population of eligible local governments, including transitional areas in the state and ULGs constituted after the 2011 Census.

⁴² Pradhan, Kanhu & Roy, Shamindra. (2018). Census towns in India - Current patterns and Future Discourses.

2.6.14 Operationalisation of the Premium

The Urbanisation Premium will be implemented in a phased manner over the Finance Commission's award period, with clearly defined responsibilities and timelines for states.

In Year 1, each state government will be required to formally notify a Rural–Urban Transition Policy (RUTP) by 30 September 2026. The policy must outline the state's approach to managing rural-to-urban transitions in a systematic, capacity-ready manner. Simultaneously, states must initiate the process of identifying transitional areas eligible for the grant, based on a field investigation using principles outlined in the policy. A transitional area may include (i) a complete or partial GP transitioning into a new ULG or (ii) a complete or partial GP merging into an existing ULG. A complete list of transitional settlements to be covered under the RUTP should be prepared and submitted to MoHUA on or before 31 March 2027 for the GPs to be eligible for the premium. **The allocation for Year 1 would be 10% of the total premium and would be released to states upon notification of a RUTP (refer to Box 3). States can distribute it further to ULGs that are constituted between the 2011 Census and 30 September 2026.**

Box 3: Guidelines for Developing a Rural–Urban Transition Policy

The principal objective of a rural–urban transition policy is to ensure planned and sustainable urbanisation while preventing unplanned and haphazard growth. Such a policy seeks to address the challenges posed by the current ad-hoc process of identifying settlements for rural-to-urban transition, as well as the transition itself. This process must be systematic and grounded in specific foundational principles, ensuring that the transition of a GP (or part of a GP) into a ULG (or part of a ULG) follows a clear, structured approach.

Core Components of the Policy

1. Identification of transitional settlements:

States must identify settlements eligible for transition within one year of a Census (or, for the purposes of the XVI FC, within one year of its report). This requires a comparison of Census-designated urban areas with the statutory status of settlements under state law. While such reviews may also occur between Census periods, it is mandatory that this exercise is undertaken after every Census.

2. Notification process and legal basis:

The policy must define the detailed procedure for the identification, assessment, and notification of transitional areas, both post-Census and during the interim period. Where required, state municipal laws must be amended to enable seamless transitions.

3. Transition plans (minimum 3-year horizon):

Each identified transitional settlement must be supported with a three-year Transition Plan, developed by the state government in consultation with the ULG or GP. The Transition Plan should be prepared for (i) newly constituted ULGs between 1 March 2026 and 30 September 2026 and (ii) transitioning GPs identified after 30 September 2026. The policy should clearly specify the structure, content, and completion criteria for these plans.

4. Institutional mechanism:

The policy must define clear roles and responsibilities across state government departments, the Directorate of Municipal Administration, district administrations, ULGs, and other relevant agencies. It should also include a grievance redressal mechanism for affected RLGs and ULGs.

Transition Plan

The transition plan will be crucial in determining the success of the transition. It must address, at a minimum, the following matters:

a. Impact assessment of finances and mitigation plan for any losses

The transition plan must include a detailed impact assessment of the financial effects of the transition on the new or receiving ULG, specifically in relation to union and state grants, as well as Finance Commission grants from both the union and the state commissions. It should identify any financial losses and the compensation required from the state government to mitigate these losses.

b. Impact assessment of citizen services and infrastructure and service delivery

The plan will thoroughly assess the impact of the transition on citizen services, infrastructure, and service delivery, and outline a roadmap for integrating existing schemes into equivalent new ones.

c. Phased levy of property tax and user charges

The transition plan should provide for the phased implementation of property tax and user charges to ensure a gradual impact on citizens and businesses, while also ensuring full benefit of the levies under state laws at the point of transition.

d. Implications on master plan and land use conversion regulations

The plan must account for the implications of the transition on the master plan and land use conversion regulations.

e. Phased application of guideline values, stamp duty, and registration charges

The transition plan should address the impact of changes in guideline values, stamp duties, and registration charges. The principle of phased implementation, with no delay in the full application at the point of transition, should also be followed here.

f. Institutional continuity with respect to office, assets, records, and staff

The transition plan must provide a detailed outline regarding staff, municipal, and ward offices, the division or transfer of assets, and office records and documents.

g. Public consultations and citizen communications

In addition to being published on the website and on physical notice boards in ULG/GP offices, the plan must be published in both an English and a vernacular newspaper. Public consultations must be invited, with the public feedback period lasting a minimum of 60 days and accompanied by no fewer than four public meetings.

In Year 2, the state government shall prepare 3-year 'transition plans' for each transitional area, in consultation with the concerned GP or ULG. The transition plan should be prepared for (i) ULGs that are newly constituted between 1 March 2026 to 30 September 2026 and (ii) transitioning GPs identified post 30 September 2026, as shared in the list to MoHUA. For GPs identified as transitional areas with a residual term of less than three years as of 1 April 2027, grants will be provided to the GP until the expiry of the elected body's term, after which they will be allocated to the new or receiving ULG. This approach ensures that no elected government is dissolved prematurely under the pretext of transition.

The allocation for Year 2 would be 15% of the total premium and its release would be contingent on the submission of transition plans to MoHUA. States may distribute the premium to ULGs constituted after 2011 and to transitioning GPs based on the share of each ULG/GP's population in the total population of eligible local governments including ULGs constituted after the 2011 Census and transitional areas in the state. In cases where only part of a GP is merged with an existing ULG, the recipient ULG will receive funds based on the population of that portion of the GP, with the funding allocated for development works within the GP boundary.

From Year 3 onwards, funds will be disbursed to newly constituted ULGs and transitioning GPs for the implementation of transition plans. The allocations for Years 3, 4, and 5 will be 25% of the total premium for each year.

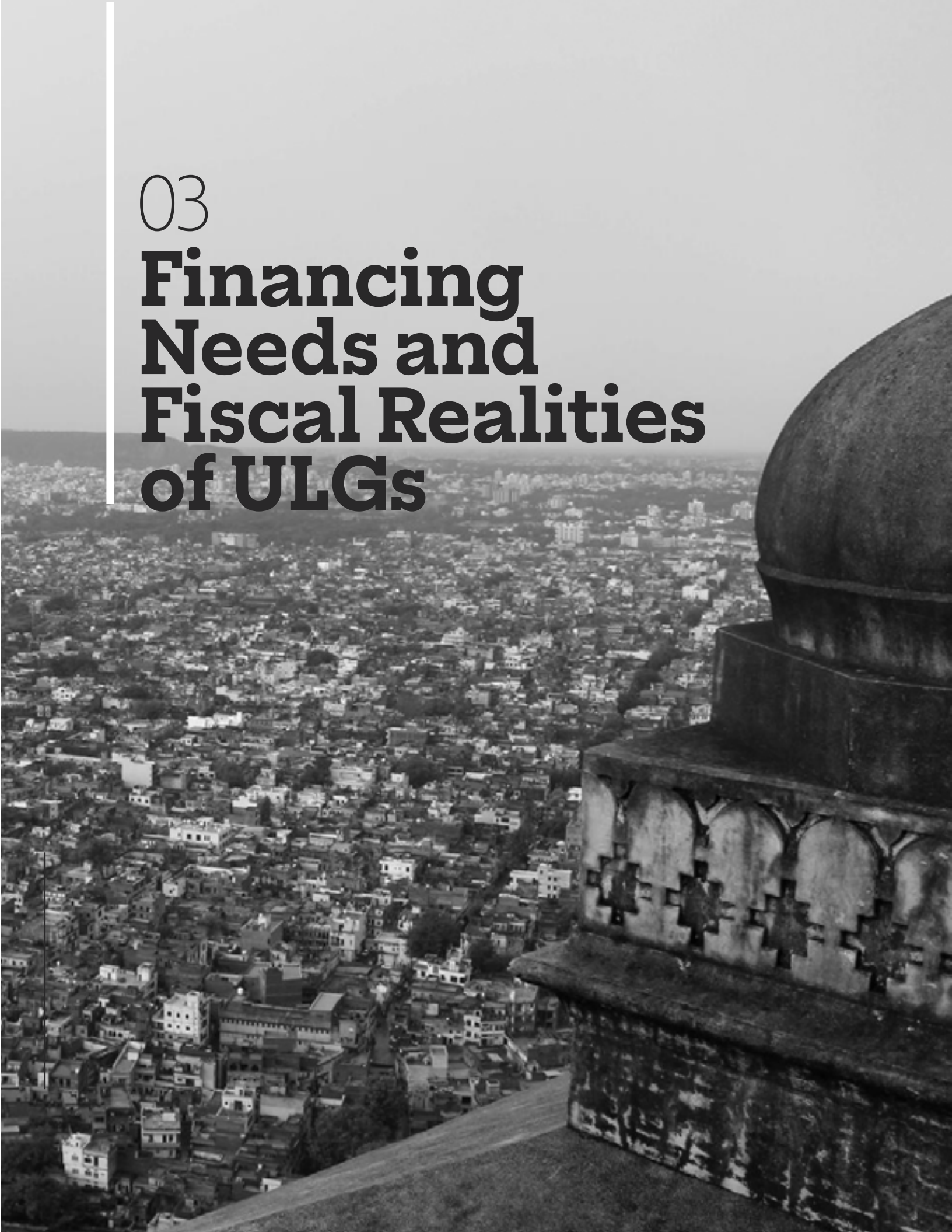
Table 3: Year-wise Allocation of Urbanisation Premium

	Year 1	Year 2	Year 3 Onwards
Milestones for Fund Release	Notify Rural–Urban Transition Policy (RUTP) by 30 September 2026	Submit 3-year transition plans for newly constituted ULGs (constituted March–September 2026) and transitional areas to MoHUA by 31 March 2027	Implement transition plans
Fund Allocation	10%	15%	25% per year
Eligible Local Governments			
ULGs Constituted Post-2011	✓	✓	✓
Transitional Areas Identified by State		✓	✓

These funds are earmarked exclusively for use in the identified transitional areas only, based on the projects approved in the transition plans. MoHUA may serve as the nodal union ministry responsible for overall monitoring, compliance, and evaluation. At the state level, the Urban Development Department (UDD), along with the concerned district administration, should lead grant administration, given its critical role in the transition process, (as discussed in Figure 4). Funds can be allocated from the state to the relevant GP/ULG. Additionally, an institutional mechanism should be established for coordination between the UDD and Department of Panchayati Raj and Rural Development, under the leadership of the development commissioner or chief secretary of the state.

03

Financing Needs and Fiscal Realities of ULGs



This chapter highlights three critical structural challenges facing municipal finance in India: the absence of updated and disaggregated estimates of investment requirements, the fragmented and opaque institutional landscape of urban expenditure, and the critical dependence on intergovernmental grants. Together, these challenges affect the accountability, transparency, and long-term sustainability of urban public finance. The analysis sets the stage for a reimagined grant architecture under the XVI Finance Commission (FC) that incentivises reform and strengthens the financial capacity of Urban Local Governments (ULGs).

3.1 The Urban Financing Requirement: The Data Vacuum

India's cities and towns require sustained investment in infrastructure and service delivery. However, there are no reliable, up-to-date estimates of urban investment needs. This critical knowledge gap persists across all levels of government, as foundational data on municipal investment requirements is either missing, outdated, or fragmented.

In the past, there have been sporadic attempts to estimate these gaps. The most prominent was a study by the McKinsey Global Institute (2010), which projected that India would require US \$1.2 trillion (₹53 trillion) in urban capital expenditure over 20 years, up to 2030. This implies an increase from actual investment of ₹765 per capita (\$17 at 2008 prices) in 2010 to ₹6,030 per capita (\$134 at 2008 prices) annually over 2010–2030.

In a similar effort, a comprehensive study by the High-Powered Expert Committee (HPEC)⁴³ in 2011 projected urban investment needs at ₹39 lakh crore (2009-10 prices) over a 20-year timeframe, with a significant role envisaged for ULGs. It recommended that by 2021-22, annual investment should reach 1.14% of GDP (equivalent to ₹1.79 lakh crore), and must remain at 1.14% (₹3.86 lakh crore) by 2031-32, a substantial increase from 0.7% in 2011-12. The Committee further advised achieving a municipal revenue base of 2.01% of GDP by 2032, with municipal own source revenue rising from 0.5% to 1.47% of GDP by 2031 — more than three times its previous level.

More recently, a World Bank (2022)⁴⁴ study estimated that India will require US \$840 billion (₹61.4 lakh crore) in capital investment for urban infrastructure and municipal services over 15 years, up to 2036 (at 2020 prices). This amounts to ₹7,884 per capita and represents approximately 1.18% of the estimated GDP or US \$108 per capita annually. This investment is intended to bridge service delivery and infrastructure gaps in the context of rapid urbanisation. Basic municipal services —

⁴³ High Powered Expert Committee for Estimating the Investment Requirements for Urban Infrastructure Services. (2011, March). Report on Indian urban infrastructure and services. Ministry of Urban Development, Government of India.

⁴⁴ Athar, S., White, R., & Goyal, H. (2022). Financing India's urban infrastructure needs: Constraints to commercial financing and prospects for policy action. The World Bank.

including water supply, sewerage, municipal solid waste management (SWM), stormwater drainage, urban roads, and street lighting — account for over half of these investment needs, totalling almost US \$450 billion.

Although each study contributed valuable insights, none provides a framework that is current, granular, or institutionally embedded for ongoing planning and fiscal devolution. The McKinsey study drew on outdated assumptions about population growth and economic trajectory. It did not adequately address sectoral and spatial specificity and was not designed to be integrated or updated into formal government planning. The HPEC report (2011), commissioned by the Government of India, was methodologically rigorous and grounded in national service benchmarks. It provided investment estimates by sector and ULG size, and included O&M costs. However, the study relied on 2011 Census data, early data from the Jawaharlal Nehru National Urban Renewal Mission (JnNURM), and decade old cost norms, limiting its relevance today. The World Bank report (2022) extended the horizon to FY2036 and incorporated more recent transport cost benchmarks. However, its methodology was built on HPEC's per capita norms, adjusting only for inflation and population changes. The population projections, GDP growth assumptions, and per capita benchmarks used across these studies no longer reflect present demographic trends, economic growth patterns, or sectoral investment needs.

Effective fiscal devolution and planning frameworks require credible estimates of urban infrastructure investment needs. Yet the McKinsey study, the HPEC report, and the World Bank report were standalone efforts, not part of a systematic or regularly updated initiative. More importantly, each was constrained by a common limitation: the absence of standardised, granular, and comparable data across ULGs, a challenge acknowledged by both HPEC and the World Bank, and one that remains unresolved today.

Beyond the lack of reliable data, ULGs also face systemic constraints, many identified by the HPEC more than a decade ago and reaffirmed by the World Bank in 2022:

- 1. Lack of comprehensive service delivery baselines:** Service gaps are not mapped in terms of coverage, quality, or equity. Available data often excludes informal settlements or understates backlogs. ULGs typically lack the personnel and systems to regularly collect, verify, and publish service-level data. Where data exists, it is inconsistent across time periods and formats. Reluctance to disclose performance information publicly, given reputational concerns and weak accountability frameworks, further undermines transparency.
- 2. Outdated and narrow benchmarking frameworks:** The 2008 Service Level Benchmarks (SLBs) issued by the Ministry of Housing and Urban Affairs (MoHUA) cover only four core services,

excluding critical areas such as road connectivity, housing, etc. They also fail to account for regional context and variations in ULG-size.

- 3. Absence of statutory planning instruments:** Investment decisions are often ad hoc and scheme-driven, as only a few ULGs prepare Capital Investment Plans (CIPs) or City Action Plans (CAPs) that link infrastructure investments to service targets, limiting alignment with local service needs.
- 4. No standardised cost norms:** ULGs have no reliable systems to estimate unit costs (e.g., per kilometre of road, per water connection, or per public toilet), and there is no national repository of per-unit cost benchmarks. As a result, ULGs struggle to prepare realistic investment plans or compare costs across projects and cities.
- 5. Fragmented institutional roles and limited information on parastatal agencies:** The World Bank (2022) report acknowledged that analyses were constrained by limited financial and investment information on parastatal agencies. The multiplicity of agencies, particularly in water, results in siloed data collection and weak integration at the ULG level, obscuring the true scale of investments and weakening local accountability.

These structural weaknesses mean that even as India's urban footprint expands, governments across tiers lack the capacities and institutional frameworks to accurately assess how much to invest, in which sectors, over what timeline, and through what financing strategy. This, in turn, affects the quality of grant design, devolution formulae, and policy targeting both state and national levels. To address this, we must institutionalise a bottom-up, standardised approach for estimating municipal investment requirements across India's diverse urban landscape. The Ministry of Housing and Urban Affairs (MoHUA) should take the lead, with a mandate to develop and promulgate a national framework for systematically assessing infrastructure and service delivery gaps.

The key characteristics of such a framework would include:

- 1. Implementation at the state level:** The framework would empower states to conduct assessments tailored to their contexts, ensuring local relevance and ownership.
- 2. Recurring and dynamic assessment:** The assessment should be conducted at least once every 10 years, complemented by interim updates that reflect changes in service demand, technology, and policy priorities. Such an approach would recognise the evolving nature of urbanisation and infrastructure needs.

3. **Differentiated approaches:** The framework must accommodate the diversity of ULGs in India by incorporating context-specific methodologies tailored to state conditions and ULG typologies, ranging from megacities to smaller towns.
4. **Comprehensive sectoral coverage:** The framework must expand beyond the current limited focus on a few sectors to cover all 18 functions devolved to ULGs under the Twelfth Schedule of the Constitution. This includes urban transport, housing, roads, water supply, sanitation, and other critical services.

3.2 Estimating Urban Investment Needs And Expenditures: The Fragmented Institutional Landscape

Estimating current and future investment needs in urban infrastructure and services is not only a challenge of scale but also one of structure. While the 74th Constitutional Amendment Act (CAA), 1992 sought to empower ULGs as the third tier of government and outlined their roles and responsibilities in the Twelfth Schedule, urban governance remains a state subject. At present, state governments decide the degree of devolution, the prioritisation of urban functions, and the role of ULGs in their broader development strategy.

Despite a constitutional mandate, most ULGs lack complete control over essential functions such as water supply, sewerage, urban transport, and housing. These often remain under the purview of parastatal agencies or departments that report directly to state governments. As a result, urban functions are not only fragmented but also frequently overlap, creating institutional ambiguity and weakening local accountability. For example, the Hyderabad Metropolitan Water Supply and Sewerage Board (HMWSSB) manages water services independently of the Greater Hyderabad Municipal Corporation (GHMC), which plays only a minor role. Similarly, urban planning functions in ULGs such as Delhi and Bengaluru are handled by state-controlled urban development authorities, which operate with little to no municipal oversight and are primarily accountable to their parent state departments.

This issue is not limited to a few large ULGs alone; it is systematically embedded in the way states have structured urban governance. We illustrate the scale and implications of this institutional fragmentation with the cases of Karnataka and Odisha.

State-Level Examples: Karnataka and Odisha

In Karnataka, the institutional landscape for urban service delivery is notably complex. At least 13 parastatal agencies are involved in various urban sectors, including 7 state-level parastatals and 5 Bengaluru-specific entities. Additionally, there are 31 Urban Development Authorities (UDAs), 52 Town Planning Authorities (TPAs), and 7 Special Purpose Vehicles (SPVs) established for the Smart Cities Mission. These agencies span multiple departments, although the majority are supervised by the Urban Development Department (UDD) (refer to Annexure 3.1 for a list of parastatals in Karnataka).

Although Karnataka's state legislation has devolved 17 functions to ULGs⁴⁵, municipal governments have full jurisdiction over only 3⁴⁶. The remaining 14 functions overlap significantly with parastatal agencies and other state-level implementing bodies. Field studies confirm that ULGs depend on parastatals for large-scale infrastructure delivery, including water supply networks, underground drainage systems, and critical tasks such as slum improvement, land use regulation, and master planning. Furthermore, the governance structures of these parastatals do not include any elected municipal representatives, effectively excluding ULGs from key decision-making processes on city infrastructure.

The significance of parastatals is also reflected in budget allocations. In Karnataka, between FY 2020–21 and FY 2023–24, parastatals and ULGs each accounted for approximately 40% of the Urban Development Department (UDD) budget. However, allocations to parastatals increased at a faster rate, around 9%, compared to just 2% for ULGs. The share of parastatal allocations fluctuated between 38% and 43%, while allocations to ULGs remained around 40% consistently (refer to Annexure 3.2 for the detailed budget allocations).

Odisha presents a similar picture. Eleven parastatal agencies are directly involved in urban service delivery, including 4 at the state level and 7 that are city-specific (refer to Annexure 3.3). These agencies receive a substantial portion of public spending on urban services.

From FY 2018–19 to FY 2025–26, parastatals in Odisha received an average of 19% of the Housing and Urban Development Department (HUDD) budget. Parastatals play a key role in implementing state schemes and Centrally Sponsored Schemes (CSS). In some cases, grants to ULGs are diverted to parastatals for infrastructure development (refer to Annexure 3.4 for detailed budget allocations).

Parastatals are fundamental to service and infrastructure delivery. Yet, despite their critical role and sizeable financial footprint, they remain largely invisible in discussions on municipal finance. Parastatals are not subject to the same transparency and accountability frameworks as elected local governments. They are not typically required to disclose budgets, financial progress, or

⁴⁵ Karnataka Municipal Corporations Act, 1976 and Karnataka Municipalities Act, 1964.

⁴⁶ CAG. (2020). Performance audit of Implementation of 74th Constitutional Amendment Act. Report of the Comptroller and Auditor General of India. Report No.2 of the year 2020. Government of Karnataka.

project outcomes publicly. As a result, their fiscal operations remain opaque, further hindering a comprehensive understanding of urban investment flows. With limited public disclosure, it is difficult to assess the investment parastatals make in urban infrastructure⁴⁷.

Furthermore, even when ULG funds are transferred to parastatals for service provision, the latter are not institutionally accountable to ULGs. Their reporting lines, funding, and oversight remain with state-level departments. **As parastatals continue to perform civic functions, they should be held accountable to the ULGs they operate in through Service Level Agreements (SLAs).** Regular reporting and **public disclosure of parastatal activities and finances, including annual and performance audits**, should be mandated to ensure accountability and quality outcomes. Where ULGs transfer Finance Commission grants to parastatals, such entities should be encouraged to publish audited annual accounts and budgets, in line with the disclosure requirements for ULGs. While not a precondition for release of funds, this measure would serve as a foundation for extending the practice of publishing audited annual accounts and budgets to parastatals such as water boards and transport corporations, many of which manage expenditures greater than those of ULGs.

3.3 Infrastructure Financing: Availability and Gaps

An accurate assessment of how much investment reaches ULGs, and the sources of these investments, remains limited due to a fragmented urban governance structure and inconsistent financial record keeping. Urban development is constitutionally a state subject, and the 74th Constitutional Amendment envisioned a greater role for ULGs in shaping it. In practice, however, roles and responsibilities often overlap across union, state, and ULGs, as well as their associated parastatals, such as development authorities, infrastructure corporations, and increasingly, private sector entities. Even when information is available for some parastatals, it is usually at the state level and does not provide insights into ULG specific investments.

Given the substantial information available on ULG finances, we will focus our analysis on the revenues and expenditures of ULGs.

In 2021–22, **total municipal revenue across India was estimated at approximately ₹2.08 lakh crore, equivalent to just 0.77% of GDP⁴⁸**. This is well below the HPEC projection of 1.71% of GDP for the same year, and lesser than the HPEC target of 2.01% for 2031–32. The gap between current revenue levels and long-term needs is particularly stark in the case of Own Source Revenue (OSR).

⁴⁷ CAG. (2020). Performance audit of Implementation of 74th Constitutional Amendment Act. Report of the Comptroller and Auditor General of India. Report No.2 of the year 2020. Government of Karnataka.

⁴⁸ Pan-India municipal revenue is extrapolated from audited accounts of 3,803 ULGs for the financial year 2021–22. The percentage share of GDP has been calculated using the 2021–22 national GDP figure of ₹2,69,49,646 crore.

ULGs generated ₹1.032 lakh crore in OSR in 2021–22, amounting to just 0.38% of GDP⁴⁹. To meet the HPEC's 2031–32 projection, municipal OSR will need to grow at an estimated Compound Annual Growth Rate (CAGR) of 14.59%, a pace unlikely to be achieved without systemic reforms in municipal revenues.

At the national level, municipal finances are primarily composed of own revenue (57%) and revenue grants and subsidies (34%), with assigned revenues and other income forming a small fraction (refer to Figure 5). However, this aggregate picture reveals sharp disparities across ULG sizes. India's largest ULGs display a strong base in own revenue, which significantly skews the national average. In contrast, smaller and medium-sized ULGs remain heavily reliant on grants to meet even basic service obligations. This variation becomes particularly stark when disaggregated by population size. Data from 2021–22 reveals a clear size-based disparity: ULGs with a population above 4 million generated 71% of their revenues from own sources, while those with fewer than 500,000 people generated only 37% or less. Smaller ULGs are far more dependent on revenue grants and subsidies, which constituted 57% of their revenue share — double the share for ULGs with populations above 4 million (refer to Annexure 3.5 for population category-wise revenue share). This indicates that large ULGs have greater fiscal capacity and revenue autonomy, while smaller ULGs remain structurally dependent on grants from union and state governments.

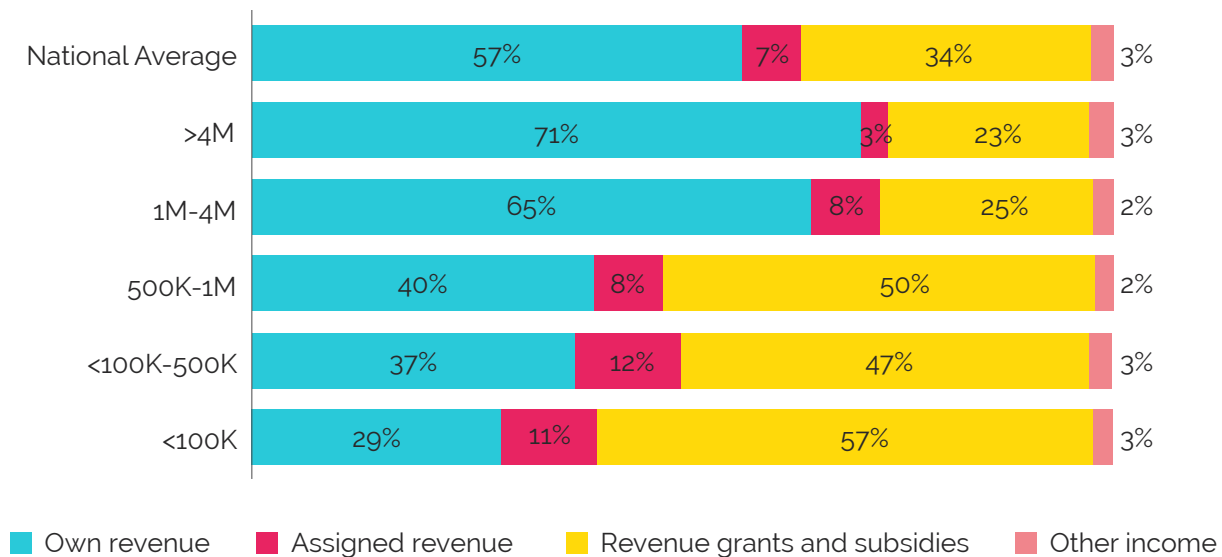


Figure 5: National and population category-wise revenue mix for 2021-22

⁴⁹ Pan-India municipal revenue is extrapolated from audited accounts of 3,803 ULGs for the financial year 2021–22. The percentage share of GDP has been calculated using the 2021–22 national GDP figure of ₹2,69,49,646 crore.

Understanding revenue alone offers an incomplete picture unless considered along with expenditure needs. Municipal spending can broadly be classified into revenue and capital expenditure. Revenue expenditure refers to spending on day-to-day operations such as salaries, subsidies, operations and maintenance (O&M), and interest payments; costs that sustain services but do not create long-term physical assets. In contrast, capital expenditure focuses on building or upgrading physical infrastructure such as roads, water supply systems, sewage treatment plants, housing, and public transport. For India's fast-growing cities, an increased share of capital expenditure is essential to develop sustainable urban infrastructure, improve service delivery, attract investment, and ensure long-term economic resilience. While revenue expenditure is necessary for maintaining basic services, capital expenditure determines the long-term health and productivity of urban centres.

At the ULG level, capital expenditure is primarily financed through transfers from higher tiers of government. In FY 2021–22, ULGs generated OSR of ₹1.03 lakh crore, while their revenue expenditure stood at ₹1.13 lakh crore, and capital expenditure was ₹0.55 lakh crore (refer to Annexure 3.6). This means that **OSR could finance only about 91% of revenue expenditure, leaving little room for capital investment from internal sources.** This fiscal strain is particularly pronounced in smaller ULGs: data shows that **ULGs with populations under 100,000 were able to finance only 41% of their revenue expenditure through OSR**, whereas ULGs with **populations over 4 million generated revenues equal to 140% of their revenue expenditure**, with surplus capacity to invest in capital projects.

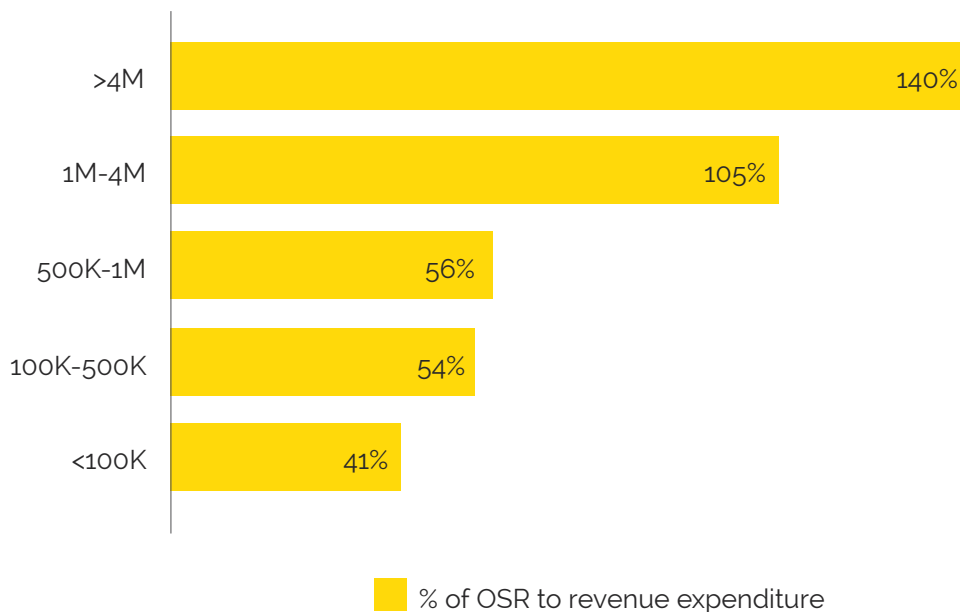


Figure 6: Percentage of own revenue to revenue expenditure

This twofold challenge, that small ULGs not only generate less OSR but also fall short of meeting even basic expenditure needs, has clear implications. While larger ULGs may benefit more from reforms that expand borrowing or market financing, smaller and medium-sized ULGs require predictable, untied grants just to meet their foundational service and infrastructure obligations. For these ULGs, FC grants are not merely supplementary; they are essential.

In this context, the union and state governments play a pivotal role in financing urban infrastructure through three primary channels: (i) Union and State Finance Commission grants, which are devolved to ULGs; (ii) Centrally Sponsored Schemes (CSS), which are implemented in partnership with states and ULGs; and (iii) State Schemes/ Grant-in-aid. These instruments form the core of budgetary support for urban infrastructure.

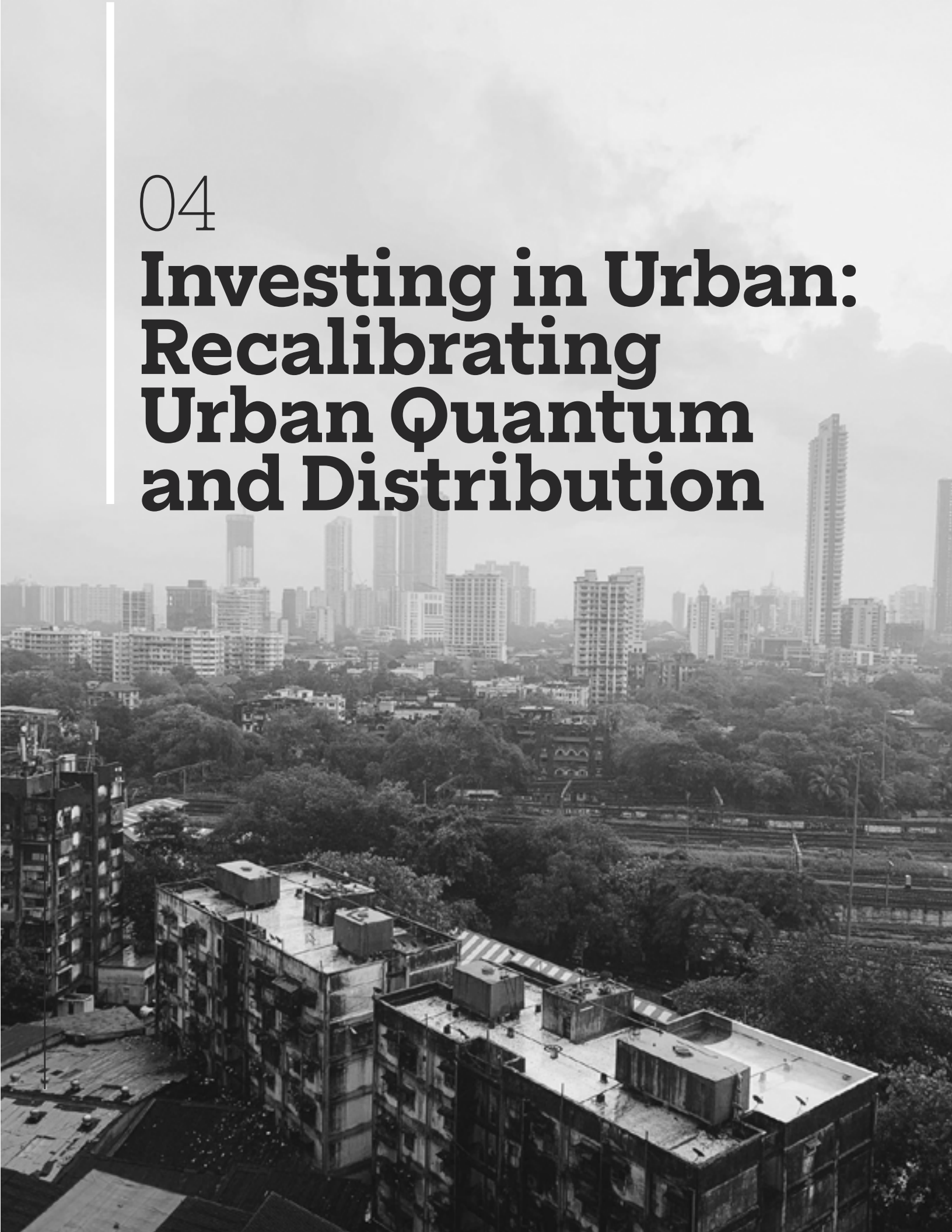
Field experiences show that in many states, UFC and CSS grants are key sources for funding urban infrastructure projects. While CSS remains an important avenue for capital financing, these funds are typically tied to scheme-specific objectives and stringent national level guidelines that apply similarly across all states and ULG types. This limits the discretion of ULGs to allocate resources based on local needs and planning priorities. The design of many CSS also requires matching contributions or adherence to central norms, further curtailing fiscal autonomy. Finance Commission grants, therefore, take on added importance. As formula-based, largely untied transfers, they provide predictable and flexible funding that enables ULGs to invest in city-specific priorities, bridge resource gaps, and strengthen institutional capacity.

Importantly, FC grants also reaffirm the constitutional mandate to recognise ULGs as the third tier of government within India's federal structure. Beyond their fiscal contribution, they signal a structural commitment to empowering local governments.

The XVI FC has an opportunity to build further on the formula-based transfers and reimagine urban grants as strategic levers of reform. The subsequent chapters outline a framework for grant design that responds to the diverse capacities and needs of India's cities. Additionally, the proposed grant structure is designed to incentivise performance and strengthen the financial and institutional foundations of urban governance in India.

04

Investing in Urban: Recalibrating Urban Quantum and Distribution



This chapter traces the evolution of allocations to Urban Local Governments (ULGs) by successive Finance Commissions (FCs), examining how they have responded to the fiscal needs of ULGs. It analyses the quantum of grants, rural–urban distribution patterns, and horizontal allocation criteria, capturing both the successes and the limitations of past approaches. It also reviews the grant architecture adopted by previous Commissions, assessing their effectiveness through analysis of formulae, grant types, conditionalities, and end use. Drawing from this analysis, the chapter provides recommendations for the XVI FC on the total quantum of local government (LG) grants for the 2026–31, the urban share these grants, formulas for horizontal distribution among states, and the guiding principles for grant architecture.

Overview and Approach

A structured way to approach the design of grant architecture for devolution to ULGs is through seven key questions, which span the two essential dimensions of devolution: the quantum of funds and their distribution, and the grant architecture. This framework also details the crucial factors the Union Finance Commission must consider in formulating its recommendations to the union government.

- 1. What should be the quantum of grants allocated to LGs?**
- 2. What should be the ratio of inter se distribution of grants for rural and urban local governments?**
- 3. What should determine the inter se distribution of grants amongst the States?**
- 4. What eligibility conditions or municipal reforms should be mandated for claiming grants?**
- 5. How should grants be distributed to ULGs within a state, basis different typologies?**
- 6. How should the grants be administered?**
- 7. What special grants are we recommending?**

Of these seven questions, the focus of this chapter is the first three. In particular:

1. The quantum of local government grants
2. The percentage share of rural and urban grants in the total local government grants
3. The distribution of local government grants among states.

Questions 4–7, which address second order aspects of grant design, will be taken up in subsequent chapters. However, the foundational principles for those discussions are introduced here. Our recommendations in Chapters 5 and 6 are anchored in a set of guiding principles derived from an analysis of the grant architecture adopted by previous Finance Commissions.

While we acknowledge that the first question is determined by macro-economic factors and lies beyond the scope of our study, we have estimated an indicative quantum of local government grants, including those allocated for ULGs. These estimates provide a practical framework for our recommendations. The analysis draws on straightforward projections of publicly available information on economic indicators, such as Gross Domestic Product (GDP) and Gross Tax Revenue (GTR).

Each recommendation will be supported by a detailed analysis of how grants evolved from the X to the XV Finance Commissions. By studying past trends and the approaches adopted by earlier Commissions, we aim to understand the rationale behind their decisions and build on insights into what worked and what did not to inform our own recommendations. This analysis serves as institutional memory for the Commission, providing a reference point for understanding the evolution of grant allocation and methodology.

Evolution of Finance Commission Grants to Local Governments (1995–2026)

Following the 74th Constitutional Amendment, successive Finance Commissions began addressing the fiscal needs of ULGs. The evolution of grants from the X to the XV FCs reflects a growing recognition of the responsibilities of local governments as well as evolving approaches to grant distribution. These included the quantum of grants-in-aid, inter-state rural–urban allocations, the formula for horizontal distribution across states, and the design and implementation of the grants. These trends provide critical direction for how the XVI FC can frame its approach to strengthening urban devolution.

4.1 Share of Local Government Grants

The allocation of grants to local governments has steadily increased across successive Finance Commissions, both in absolute terms and as a share of the divisible pool. Local government grants rose from ₹5,381 crore under the X FC (1995–2000) to ₹4.36 lakh crore under the XV FC (2021–2026), increasing from 1.38% to 4.23%⁵⁰ of the Divisible Pool (DP).

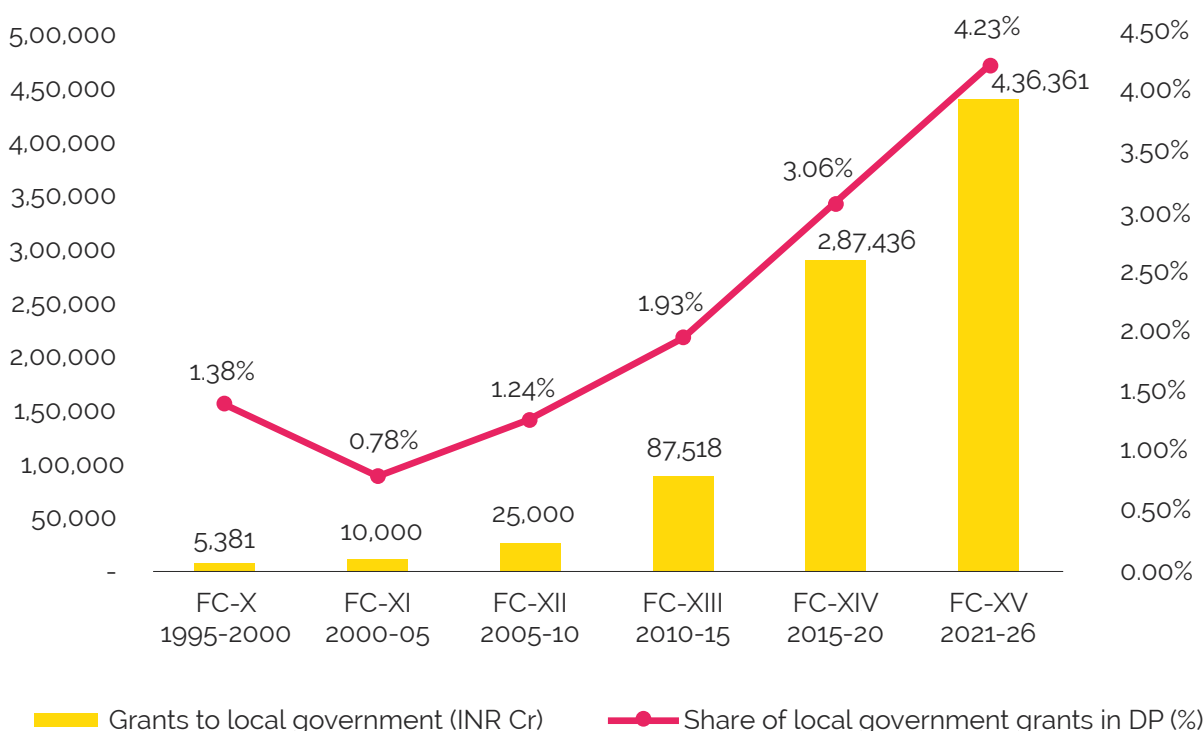


Figure 7: Growth in local government grants and share of divisible pool (X FC to XV FC)

The X FC (1995–2000), constituted at the time of the introduction of the 73rd and 74th Constitutional Amendment, was the first Finance Commission to recommend grants for local governments. Although the Terms of Reference (ToR) for local governments did not exist at the time, the FC allocated a lump-sum ₹5,381 crore to state governments for devolution to local governments.

The ToR for the XI FC (2000–2005) explicitly recognised local governments. The Commission subsequently recommended ₹10,000 crore⁵¹ in grants to them. Despite the absolute increase, the share of grants relative to the divisible pool decreased from 1.38% to 0.78%.

⁵⁰ This excludes the local government grant recommended during the period 2020–21.

⁵¹ Eleventh Finance Commission. (2000). Report of the Eleventh Finance Commission. Government of India.

The XII FC (2005–2010) acknowledged the expanding responsibilities of ULGs under the Twelfth Schedule and significantly raised local government allocations to ₹25,000 crore⁵². At 1.24% of the divisible pool, this move reversed the trend of declining local government share in the divisible pool.

The XIII FC (2010–2015) considered allocating local government grants as a percentage of the divisible pool, similar to devolution to state governments. However, as per legal advice, doing so would elevate such transfers to the level of tax devolution, conflicting with Articles 275 and 280, which limit tax devolutions to union and state governments and stipulate that local governments receive grants-in-aid only.

The XIII FC aimed to adhere to this constitutional framework, while acknowledging the demand of LGs to benefit from the buoyancy of union taxes. It recommended that the quantum of grants-in-aid for each year of its award period (year 't') be set as a fixed percentage of the divisible pool from the previous year ('t-1'). The recommended grant-in-aid to local governments was ₹87,519 crore⁵³, or 1.93% of the estimated divisible pool for the 2010–2015 period.

The XIV FC (2015–2020) marked a paradigm shift in fiscal decentralisation to local governments. Prioritising stability and predictability through assured transfers, it recommended a fixed grant-in-aid for its award period rather than linking it to a percentage of the previous year's divisible pool, and allocated ₹2.87 lakh crore⁵⁴ to local governments, equivalent to 3.06% of the estimated divisible pool.

Building on the XIV FC's approach, the XV FC (2021–2026) continued providing predictable and stable transfers, expanding the grants by recommending a grant-in-aid of ₹4.36 lakh crore equivalent to 4.23% of the estimated divisible pool⁵⁵. In its interim report, it recommended ₹90,000 crore for 2020–21 alone, equivalent to 4.31% of the estimated divisible pool⁵⁶.

While the XV FC recommended the highest-ever absolute amount of ₹4.36 lakh crore, the growth rate dropped steeply to just 52%, the lowest since X FC (refer to Figure 8).

⁵² Twelfth Finance Commission. (2004). Report of the Twelfth Finance Commission. Government of India.

⁵³ Thirteenth Finance Commission. (2009). Report of the Thirteenth Finance Commission. Government of India.

⁵⁴ Fourteenth Finance Commission. (2015). Report of the Fourteenth Finance Commission. Government of India.

⁵⁵ Fifteenth Finance Commission. (2020). Report of the Fifteenth Finance Commission. Government of India.

⁵⁶ Ibid.

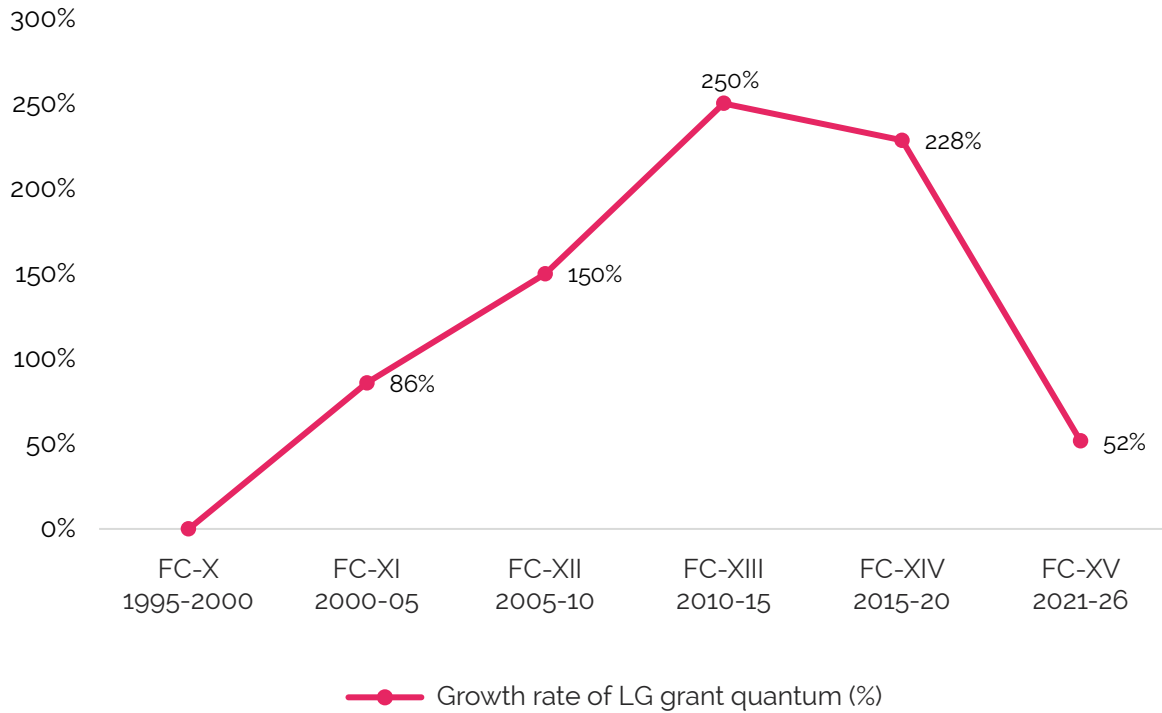


Figure 8: Growth rate trend of LG grant quantum

Despite the increase in the overall quantum of grants, per capita allocations remained static across the XV FC period. For instance, the per capita local government grant for 2025–26 is ₹672 — slightly lower than the ₹674 in the final year of the XIV FC (2019–20), despite a six-year gap (refer Figure g). This stagnation suggests that local governments did not benefit from the growth in union tax collections during this period. It is also concerning that per capita FC grants have not kept pace with the rising cost of delivering essential services.

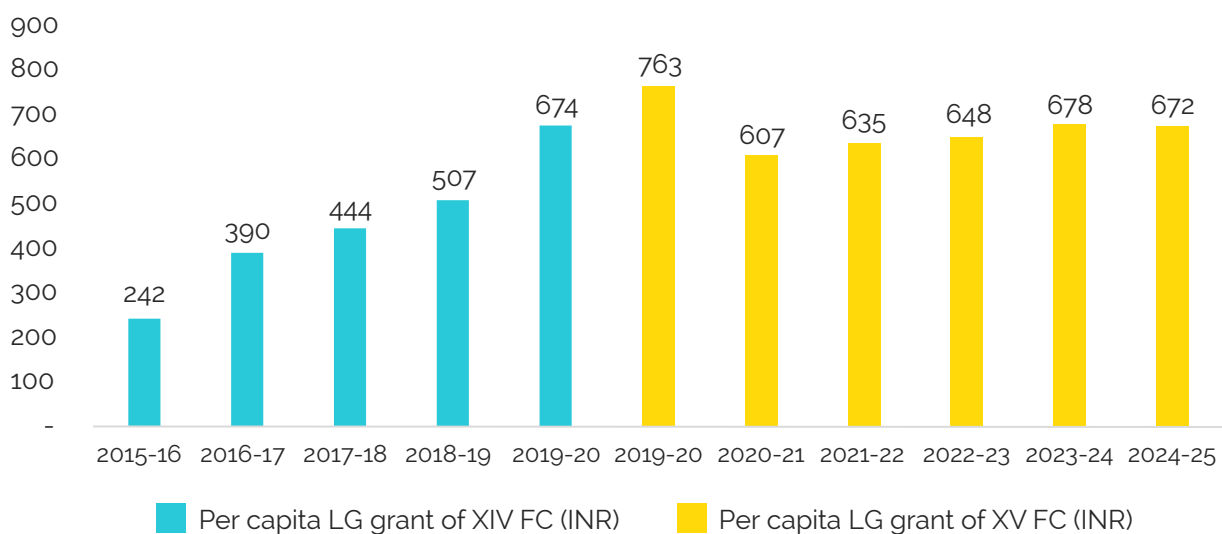


Figure 9: Per capita LG grant trend for XIV and XV FC, year on year

The XIV FC estimated an increase in yearly allocations of LG grants as a percentage of the divisible pool, rising from 2.17% to 3.55% during 2015–2020. In contrast, the XV FC reversed this trend (refer to Figure 10), with the share decreasing each year from 5.00% to 3.52% during 2021–2026, averaging 4.23% over the award period (refer to Annexure 4.1).

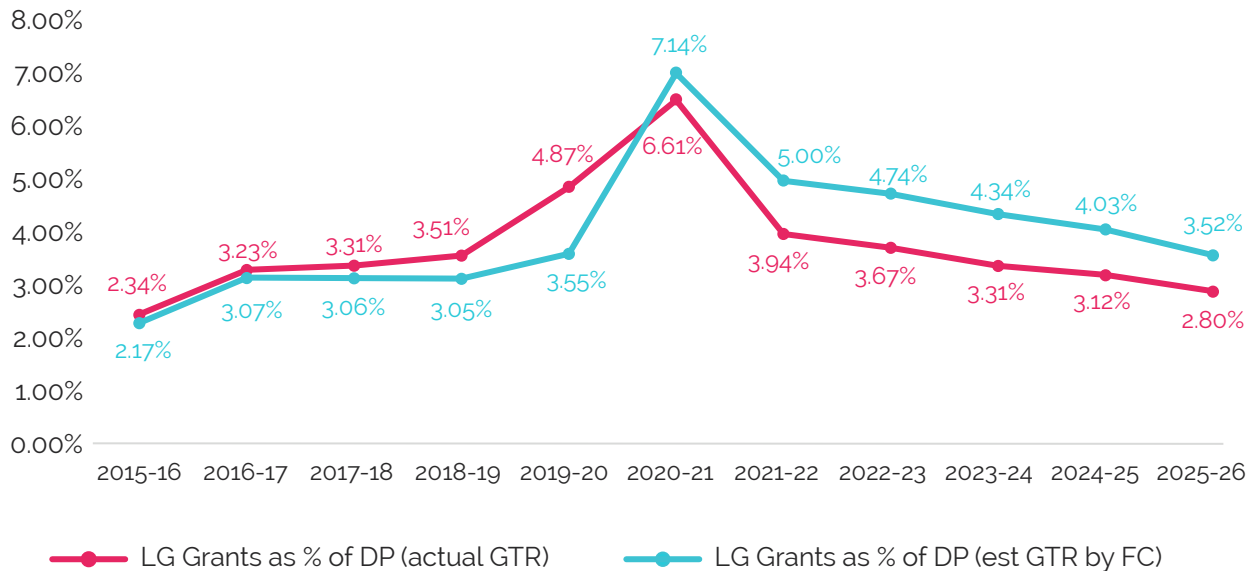


Figure 10: LG grants as percentage of divisible pool on actual GTR and estimated GTR by XIV and XV FC

Note: In this graph, the blue line represents the percentage of the divisible pool, as estimated by the respective FC in their report. It is compared with the pink line which represents LG grants as a percentage of the divisible pool, calculated using actual GTR data. Since the exact figures for the divisible pool are not publicly available, we estimate them by applying the same percentage share of GTR used by the respective Finance Commissions. This ensures consistency with the FC methodology. We then compute LG grants as a percentage of this estimated divisible pool, using the share recommended by the respective FCs. This approach tracks how the share of LG grants relative to the divisible pool has evolved over time, based on actual fiscal outcomes

We also assessed the trajectory of **LG grants as a share of GDP**; a benchmark commonly used in several countries to indicate the extent of fiscal devolution to local governments. During the XIV FC period, this share **increased from 0.21% to 0.36%** (refer to Annexure 4.2). In contrast, under the XV FC, **it declined steadily from 0.34% in 2020–21 to 0.30% in 2023–24**, reflecting the decline in allocations as a percentage of the divisible pool. This decline of LG grants relative to both GDP and the divisible pool signals a narrowing fiscal space for local governments.

Given the rising expectations and expanding mandates of local governments, both rural and urban, there is a compelling case for the XVI FC to recommend a constant grant-in-aid share of a minimum of 4.23% of the estimated divisible pool for local government each year of the award period. While this may increase the total quantum, it would help restore adequate per capita allocations that are more closely aligned with the realities of service delivery.

4.1.1 Indicative Estimations for XVI Finance Commission Grants to Local Governments

Successive Finance Commissions have determined grants to local governments as a fixed percentage of the divisible pool, which is based on the projected Gross Tax Revenue (GTR) of the union government for the award period. However, the methodology for determining the share of the divisible pool for local governments has not been clearly outlined.

Since the exact figures for the divisible pool are not publicly available, we relied on two complementary approaches, using available data, to estimate the quantum of grants for the XVI FC period (2026–31):

1. **Divisible pool-based approach:** This method, used by past Finance Commissions, calculates grants to local governments as a percentage of the estimated divisible pool.
2. **GDP-based approach:** This method proposes that local governments receive a fixed share of the country's economic output (nominal GDP). It is based on international benchmarks of fiscal devolution and ensures that funding grows in line with the broader economy.

These are the steps we followed to arrive at the estimates for the XVI FC period (2026–31):

4.1.1.1 Approach 1: Divisible Pool-based Approach

As noted above, the actual quantum of the divisible pool from past FCs is not publicly available. Therefore, we used the publicly available Gross Tax Revenue (GTR) data to estimate the divisible pool

Step 1: Methodology for determining the GTR growth rate

To estimate the GTR for the XVI FC period (2026–31), we sourced GTR data from union budgets (FY 2015–16 to FY 2023–24), revised estimates for FY 2024–25, and the budget estimate from union budget FY 2025–26. We calculated the annual growth rates from 2015. However, due to the lack of a clear and defined trend (refer to Annexure 4.1), we applied the growth rate between 2023–24 and 2025–26, during which GTR grew at 11% (refer to Annexure 4.1). **We therefore assume a constant 11% annual growth rate for GTR during the XVI FC's award period.**

Step 2: Calculating the projected GTR for 2026–31

Using the FY 2025–26 budgeted GTR of ₹43 lakh crore as the base, we project the GTR for each year of the award period, applying an 11% annual growth rate (refer to Table 4).

Step 3: Methodology for determining the share of the divisible pool in GTR

We sourced the estimated divisible pool and GTR for the XIV FC and XV FC from their respective reports (refer to Annexure 4.6, 4.7, and 4.8). Using this data, we calculated the average share of the divisible pool in GTR as 89% for XIV FC and 76% for XV FC. We assume the **share of the divisible pool in GTR for the XVI FC period will remain constant at 76%**.

Step 4: Calculating the divisible pool

Applying the 76% share to the projected GTR yields the divisible pool figures as listed in Table 4.

Step 5: Determining the LG grant share

We retain **4.23% as the benchmark share for LGs in our projections**, based on the average recommended share of local government grants as a percentage of the divisible pool during the XV FC period.

Table 4: Estimated LG Grants Under Approach 1 for Each Year During the XVI FC Period

Year	GTR (INR lakh crore)	DP = 76% of GTR (INR lakh crore)	LG Grants @ 4.23% (INR lakh crore)
2026–27	47	36	1.52
2027–28	53	40	1.72
2028–29	59	45	1.92
2029–30	65	50	2.10
2030–31	73	55	2.40
2026–31	297	226	9.73

4.1.1.2 Approach 2: GDP-based Approach

Step 1: Methodology for determining the GDP growth rate

To estimate the GDP for the XVI FC award period (2026–31), we analysed trends in nominal GDP. From FY 2021–22 to FY 2023–24, nominal GDP grew at a CAGR of 11.9% (refer to Annexure 4.3). The National Statistical Office (NSO) projected a 9.7% growth rate for 2024–25. **Adopting a conservative approach, we assumed a 9% annual growth rate for the period 2026–31.**

Step 2: Calculating the projected GDP for 2026–31

Using the 2024–25 base GDP estimate of ₹324 lakh crore (as per the First Advance Estimate⁵⁷), we projected nominal GDP for five years at 9% annual growth:

⁵⁷ Advance estimates of GDP are preliminary projections of economic performance, released before final, more detailed data becomes available. These estimates are based on available indicators and data, such as production of key crops and other economic indicators, and are subject to revision later on as more complete information becomes available.

Table 5: Projected GDP for the Period FY 2025–26 to FY 2030–31

Year	GTR (INR lakh crore)
2025–26	353
2026–27	385
2027–28	420
2028–29	458
2029–30	499
2030–31	544
Total Projected GDP for XVI FC Award Period	2,304

Step 3: Methodology for determining the local government grant share

During the XIV FC period, India's local government grants were 0.36% of the GDP. This is projected to decline to 0.28% by the end of the XV FC period in 2025–26. It is crucial for the XVI FC to build on the foundation laid by the XIV FC and raise LG grants to 0.4% of the GDP. This adjustment will align LG grants with GDP growth, creating the fiscal space necessary for local governments to support their expanding service delivery mandates. It will also bring India in line with global standards: countries with fiscal federalism frameworks typically allocate a far higher share of GDP to local governments. For example, Brazil transferred approximately 7.1% of its GDP in 2020⁵⁸, the Philippines mandates ~0.5%⁵⁹, and South Africa will transfer around 2.4% of GDP for 2025–26⁶⁰. We have therefore set a benchmark of 0.4% of GDP for LG grants.

Table 6: Estimated LG Grants for Each Year During the XVI FC Period

Year	LG Grants @ 0.4% of GDP (INR lakh crore)
2026–27	1.54
2027–28	1.68
2028–29	1.83
2029–30	1.99
2030–31	2.17
2026–31	9.22

⁵⁸ OECD & UCLG. (2019). Country profile: Brazil. In World Observatory on Subnational Government Finance and Investment. Retrieved June 13, 2025, from https://www.sng-wofi.org/country_profiles/brazil.html

⁵⁹ Senate Economic Planning Office. (2022, March 21). IRA in 2022 [PDF]. Senate of the Philippines. Retrieved June 13, 2025, from https://web.senate.gov.ph/publications/SEPO/AAG%20IRA%20in%202022__21March2022.pdf

⁶⁰ National Treasury. (2025, May). May 2025 Budget overview [PDF]. Government of South Africa. <https://www.treasury.gov.za/documents/National%20Budget/2025May/review/May%202025%20Budget%20Overview.pdf>

Final Proposal for Quantum of Local Government Grants

Based on the outlined steps and assumptions, the estimated LG grants amount to ₹9.73 lakh crore under the divisible pool-based approach and ₹9.22 lakh crore under the GDP-based approach. Taking the average of these two estimates, **we propose a total LG grant quantum of ₹9.50 lakh crore for the XVI FC period.** This figure serves as the reference point for subsequent recommendations in the report.

Table 7: Proposed LG Grants for the XVI FC Period

Year	Proposed LG Grants (INR lakh crore)
2026–27	1.50
2027–28	1.68
2028–29	1.88
2029–30	2.10
2030–31	2.34
Total	9.50

Note: These are indicative estimates based on available macroeconomic data and historical benchmarks. Actual allocations may vary depending on the fiscal position and methodology adopted by the XVI FC.

We propose that the XVI FC allocate at least ₹9.50 lakh crore to local governments for the 2026–31 period. This proposed quantum represents a necessary course correction and achieves three critical outcomes.

1. Reverses the deceleration in the growth rate of grants during the XV FC, restoring the growth rate to 118%, a level more consistent with the expansionary trends of earlier Commissions (refer Annexure 4.4).
2. Recovers momentum in per capita allocations, achieving a 109% increase over the previous cycle and addressing the stagnation observed between 2021 and 2026 (refer to Annexure 4.4), when per capita grants plateaued despite rising service delivery costs.
3. Ensures predictable, year-on-year growth in per capita support, providing local governments with buoyant grants in line with growth in union taxes.

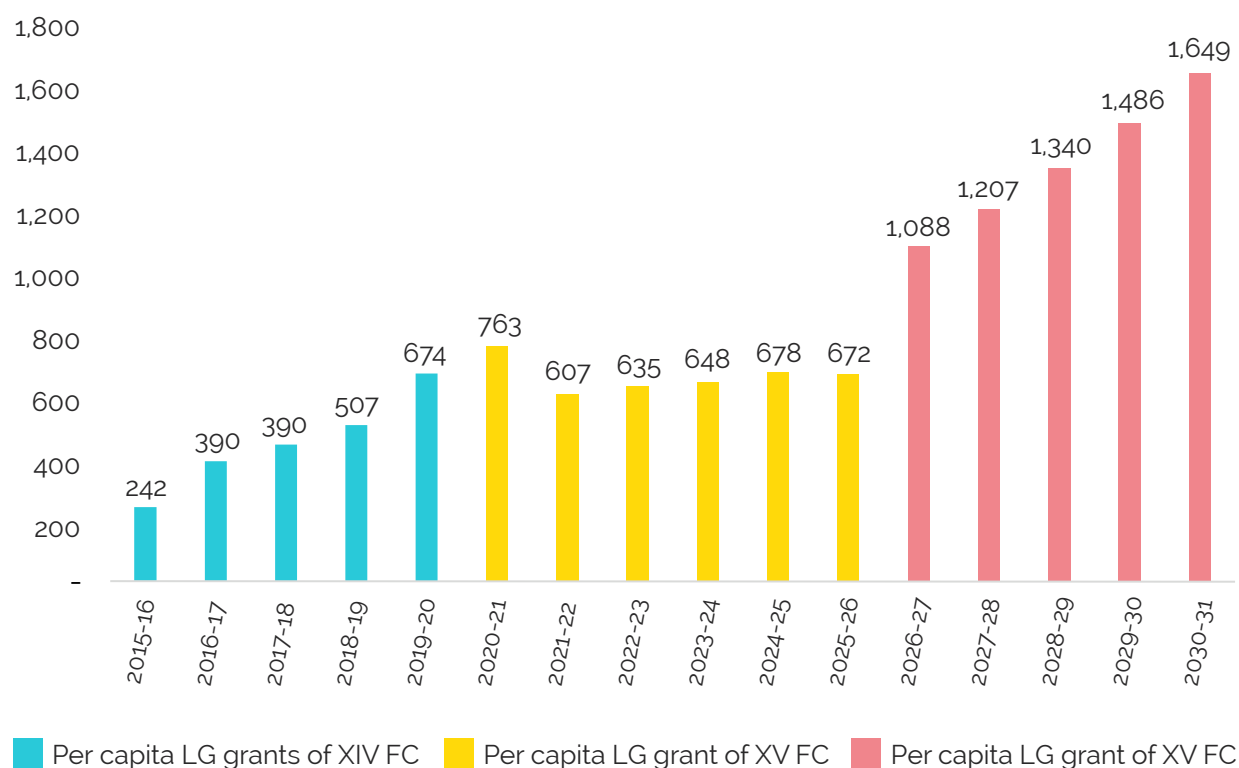


Figure 11: Year-on-year per capita (INR) LG grant trend for the XIV, XV and XVI FCs

While this allocation may seem significant in absolute terms, it remains modest by international standards, amounting to just 0.41% of the projected GDP (compared to 0.33% under the XV FC) and 4.21% of the divisible pool.

4.2 Inter se Distribution of Grants Between Rural and Urban Local Governments

ULGs' share of total grants-in-aid to local governments increased from approximately 19% under the X FC (1995–2000) to around 36%⁶¹ under the XV FC (2021–2026). However, it remains below the projected urban population share, which is expected to reach 38% by 2026, according to the World Urbanization Prospects, 2018.

Historically, Rural Local Governments (RLGs) have received a larger share of grants than ULGs. The X FC calculated local government grants on an ad-hoc basis, granting ₹100 per capita to RLGs, amounting to ₹4,380.93 crore over the period from 1996 to 2000. For ULGs, the X FC recommended grants of approximately ₹1,000 crore for the same period, while acknowledging a significant funding gap for the operation and maintenance of core municipal services in urban India. The National

⁶¹ The 36% share of local government grants allocated to urban areas includes special/additional grants.

Institute of Urban Affairs (NIUA) estimated this gap at ₹5,987 crore in 1995, with projections rising to ₹12,980 crore by 2000.

The XI FC recommended an 80:20 division of local government grants between RLGs and ULGs, allocating ₹8,000 crore to RLGs and ₹2,000 crore to ULGs. This was based on the rationale that ULGs had greater access to their own tax and non-tax revenue sources, while RLGs required more substantial fiscal support from higher levels of government.

The XII FC maintained the 20% allocation to ULGs, amounting to ₹5,000 crore, but emphasised the need to incentivise ULGs to strengthen their own revenue sources.

The XIII FC adopted a population-based approach, allocating 26.82% of local grants to ULGs (approximately ₹23,000 crore) and 73.18% to rural governments, reflecting the urban-rural population share based on the 2001 Census.

The XIV FC refined this approach by using 2011 Census data, allocating 30.31% of grants to ULGs (around ₹87,000 crore) and 69.69% to RLGs. This resulted in a significant increase in ULG funding, nearly quadrupling the amount allocated by the XIII FC, and aligning financial allocations more closely with the country's evolving demographic composition.

The XV FC acknowledged the accelerating pace of urbanisation and the growing economic significance of cities. Importantly, it recognised the phenomenon of 'hidden urbanisation,' where official statistics underestimate urban expansion, particularly in the peripheries of major cities. Drawing on the World Urbanization Prospects 2018, the XV FC noted that 2011 Census figures were outdated and that India's urban population was projected to reach between 37–38% by 2025, the XV FC proposed a gradual adjustment in grant distribution. It recommended moving from a rural-to-urban ratio of 67.5:32.5 in FY 2020–21 to 65:35 by FY 2025–26, allocating ₹1.22 lakh crore⁶² to ULGs over five years.

4.2.1 Recalibrating Rural–Urban Grant Distribution for the XVI FC

There is a compelling case for the XVI FC to build on the progressive steps taken by the XV FC and increase the share of urban grant allocations. Four critical factors underpin this recommendation:

1. India is rapidly urbanising and projected to achieve 41% urbanisation by 2031.

Given the lack of updated census data, the XVI FC is likely to face challenges in accurately

⁶² The ₹1.22 lakh crore figure excludes special/additional grants. Including these, the total allocation to ULGs during the XV FC period amounts to ₹1.55 lakh crore, or approximately 36% of total local government grants.

estimating the extent of urbanisation. Projections suggest India has urbanised rapidly since the 2011 Census. The Ministry of Health and Family Welfare (MoHFW)⁶³ estimates that India's urban population will reach 36% by 2026 and 38% by 2031. Similar projections from the UN⁶⁴ estimate 38% urbanisation by 2026 and 41% by 2031. Satellite data from the Global Human Settlements Layer (GHSL) by the Group on Earth Observations at the European Commission indicates that India's urbanisation level was 63% in 2015 — almost double the rate reported in the 2011 Census.

Additionally, the XV FC's interim report (2019) explicitly recommended increasing the share of ULGs in local government grants to 40% over the medium term:

"Given the projection of 38% urbanisation in India by 2025 and further acceleration of this trend with economic growth, the changing sectoral composition of the GDP, and rural-urban migration, we believe the share of urban local bodies in the Finance Commission grants to local bodies should be gradually increased to 40% over the medium term." – XV FC, 2019

2. Investing in urban yields higher return on investments.

Cities are India's economic engines. Urban areas, though home to less than one-third of the population, contribute over two-thirds of the country's GDP, a share projected to rise to 75% by 2030⁶⁵. This economic capacity is driven by the agglomeration advantages cities offer: higher wages, greater innovation, and stronger business dynamism.

However, the relationship between urbanisation and economic growth in India remains under-optimised. Globally, a 1% increase in urbanisation is associated with a 3.9% rise in per capita GDP⁶⁶, highlighting significant untapped potential. Targeted public investments are crucial to bridging this gap.

According to the McKinsey Global Institute (2020), infrastructure investments typically yield a 20% socioeconomic return, meaning every dollar spent can increase GDP by \$0.20 in the long term⁶⁷, making it one of the most productive uses of public capital. To sustain this momentum, India will need to invest an estimated \$840 billion in urban infrastructure by 2036 — approximately \$55 billion, or 1.2% of GDP annually⁶⁸. This scale of investment is not only necessary to meet service delivery needs but also critical to unlocking the full economic potential of India's cities.

⁶³ MoHFW, Gol. (2019). Report of the Technical Group on Population Projection.

⁶⁴ UN. Department of Economic and Social Affairs, Population Division. (2024). World Population Prospects 2024.

⁶⁵ Subudhi, S., Bakliwal, S., & Bilgrami, S. (2023, March 10). Cities of the future: Reimagining and rejuvenating India's top 50 urban ecosystems. Boston Consulting Group. <https://www.bcg.com/publications/2023/india-cities-of-the-future>

⁶⁶ World Resources Institute India. (2021). The State of the Cities Report.

⁶⁷ McKinsey Global Institute. (2020, January 6). Four ways governments can get the most out of their infrastructure projects. McKinsey & Company.

⁶⁸ World Bank. (2022). Financing India's Urban Infrastructure Needs: Constraints to Commercial Financing and Prospects for Policy Action.

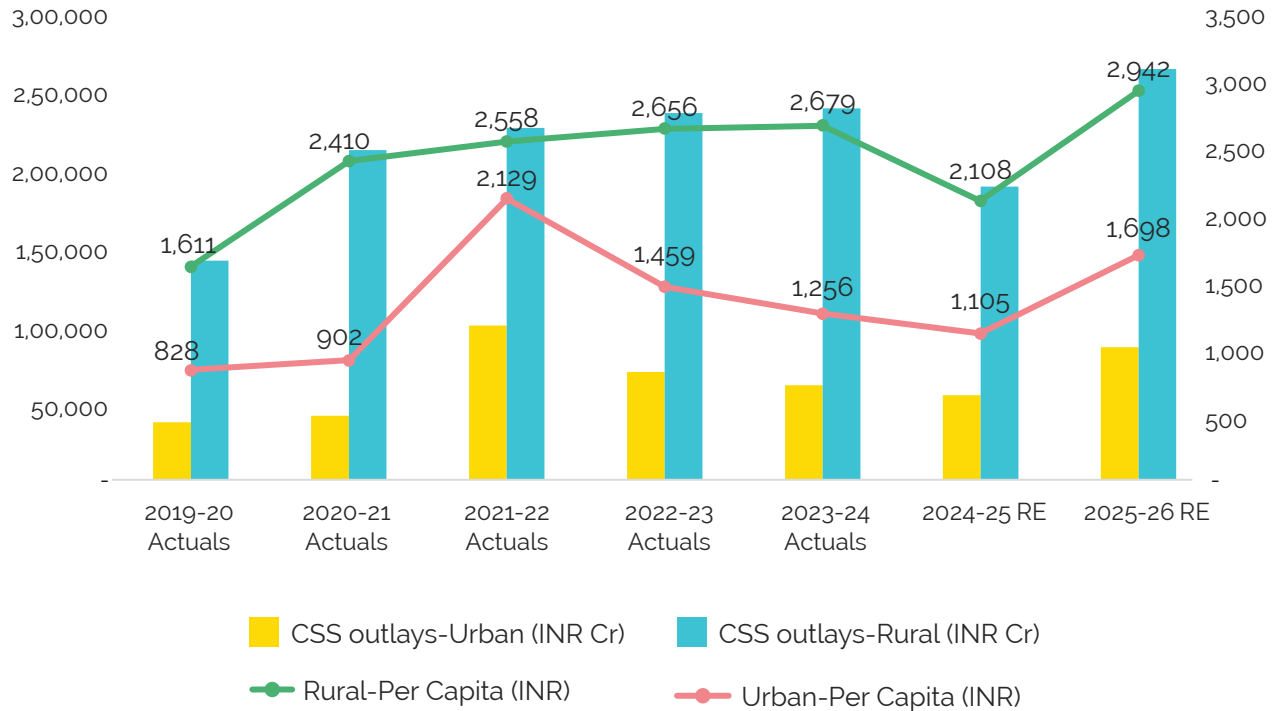


Figure 12: Trends in CSS outlays to urban and rural areas, and per capita allocations to urban areas

3. Historically, rural areas have been favoured over urban in central outlays.

Allocations under Centrally Sponsored Schemes (CSS) have disproportionately favoured rural areas, both in absolute terms and on a per capita basis. Between FY 2019–20 and FY 2023–24, rural areas consistently received five to six times the total CSS allocations of their urban counterparts. In 2021–22, for instance, while urban allocations peaked at ₹1.00 lakh crore⁶⁹, rural allocations totalled ₹2.28 lakh crore — more than two times higher. This disparity is even more pronounced on a per capita basis. Per capita CSS allocations to rural areas have remained substantially higher, widening over time from ₹1,611 in 2019–20 to ₹2,942 in the 2025–26 Budget Estimates (refer to Annexure 4.9). In contrast, urban per capita allocations increased only moderately from ₹828 in 2019–20 to ₹1,698 in 2025–26 (refer to Annexure 4.10), still only about a third of rural allocations in that year.

4. Several State Finance Commissions (SFCs) have increased the share of grants to ULGs.

Evidence shows that State Finance Commissions (SFCs) have been favouring urban areas and increasing the share of local government grants from states to ULGs.

An analysis of recent SFC reports from fifteen⁷⁰ reveals that in nine, urban allocations exceed state urbanisation rates. In six⁷¹ states with urbanisation rates ranging from 22% to 48%, 40% or more of local government grants are devolved to ULGs (refer Annexure 4.11). The XV FC also recommended increasing the share of grants to ULGs to 40% over the medium term.

Based on these trends, we recommend raising the allocation to ULGs from approximately 36% (₹1,55,628 crore) to 40% (approximately ₹3,80,000 crore) of total local government grants under the XVI FC. This would result in a per capita urban grant of ₹7,642 during the XVI FC award period.

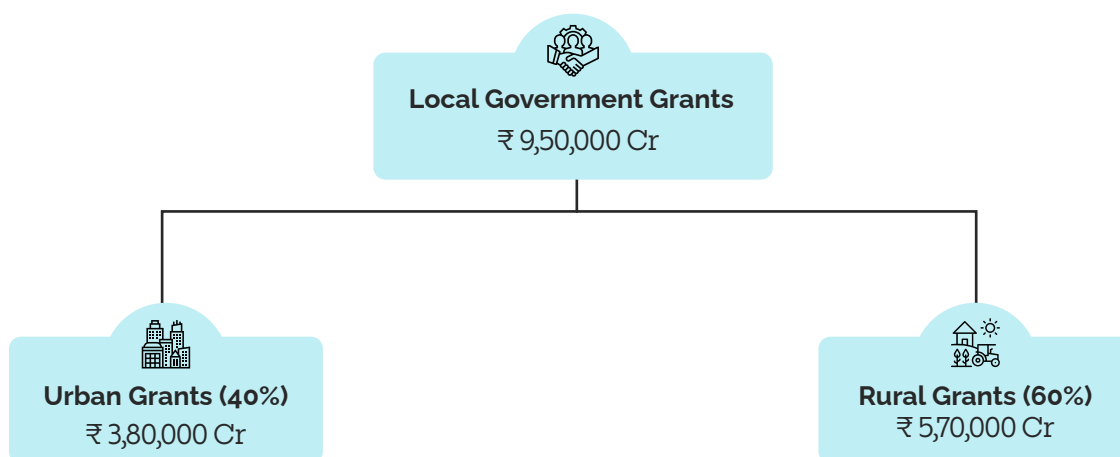


Figure 13: Inter se urban grants and rural grants under XVI FC

4.3 Inter se Distribution of Grants Among States (Horizontal Distribution)

Over successive Commissions, the approach to distributing grants to LGs has evolved from targeting poverty and service deficits to balancing equity, efficiency, and decentralisation.

Table 8 below summarises the criteria used by successive Finance Commissions (X to XV) to distribute grants to states for local governments.

⁶⁹ Urban allocations include outlays for Metro Rail projects and MRTS (Mass Rapid Transit System).

⁷⁰ For 13 states — Arunachal Pradesh, Chhattisgarh, Goa, Gujarat, Jharkhand, Madhya Pradesh, Maharashtra, Manipur, Meghalaya, Mizoram, Nagaland, Tripura, and Telangana — SFC inter se ratios between the latest urban-rural allocations are unavailable.

⁷¹ Assam, Haryana, Punjab, Tamil Nadu, Uttar Pradesh, and Uttarakhand devolved 40% or more to urban areas.

The X FC recommended that urban allocations to states be based solely on the share of their slum population, as per the 1971 Census. This approach reflected an early attempt to direct urban grants towards specific issues, such as urban poverty and service deficits. These grants were incorporated into state plans, with the expectation that states would allocate them to local governments. The XI, XII, and XIII FCs broadened the criteria by introducing factors related to equity (e.g., distance from the highest per capita income) and efficiency (e.g., revenue effort)⁷².

Table 8: Criteria and their Assigned Weights for Distribution of Grants to States for Local Governments by FCs

Year	X FC		XI FC	XII FC	XIII FC		XIV FC	XV FC
	RLG	ULG			RLG	ULG		
Census	1971		1971	2001	2001		2011	2011
Population	100		40	40	50		90	90
Ratio of urban slum population		100						
Geographical area			10	10	10		10	10
Distance from highest per capita income			20	20	10	20		
Index of devolution					15			
Index of decentralisation			20					
Index of deprivation				10				
Revenue effort			10	20				
Proportion of SCST in population					10			
FC local body grants utilisation index					5			

⁷² Fiscal transfer systems are typically guided by two foundational principles: equity and efficiency. Equity is addressed along both vertical and horizontal dimensions. Vertical equity concerns the appropriate distribution of resources between different levels of government, while horizontal equity focuses on ensuring fairness across similar levels of government by accounting for variations in fiscal capacity, expenditure needs, and structural cost disabilities. Efficiency, on the other hand, requires that transfers be structured to minimise distortions in economic decision-making and promote the optimal use of public resources, while still addressing regional disparities and service delivery obligations.

Following the constitutional amendments incentivising decentralisation, the XI FC introduced the Index of Decentralisation to assess the extent to which powers and responsibilities were devolved to local governments. It also factored in the revenue efforts of local governments to augment their own resources. The XII FC retained most of these criteria but replaced the Index of Decentralisation with the Index of Deprivation to better capture inter-state disparities, using data on minimum needs indicators⁷³. Additionally, to ensure greater equity for states with lower Gross State Domestic Products (GSDP), the XII FC extended the 'distance from highest per capita income' criterion to both rural and urban areas, whereas the XI FC had applied it only to rural areas.

The XIII FC retained the use of the distance from per capita income criterion but discontinued the use of the Index of Deprivation and revenue effort, citing a lack of reliable data. For urban areas, it introduced the utilisation of grants awarded by the XII FC as a performance metric. Further, to promote decentralisation, it introduced the Index of Devolution, as accurately assessing the Index of Decentralisation⁷⁴ remained challenging.

While previous Finance Commissions emphasised a combination of equity and efficiency, the XIV and XV FCs shifted to a simpler, need-based approach. These Commissions primarily used population and area in a 90:10 ratio as the key determinants for the distribution of LG grants across states.

The XV FC introduced a gradually adjusting national rural–urban ratio, applied uniformly across all states to determine the allocation of funds between rural and urban areas. This ratio evolved from 67.5:32.5 in FY 2020–21 to 65:35 in FY 2025–26.

However, this approach did not account for significant variations in levels of urbanisation across states. By applying a uniform rural–urban ratio, the XV FC inadvertently skewed the distribution of grants within states. States with higher urban populations were disadvantaged in per capita allocations to ULGs, while less urbanised states received relatively more, and vice versa for RLGs. For example, Tamil Nadu, with an urban population of 48%, received ₹2,058 per capita for ULGs, while Uttar Pradesh, with an urban population of only 22%, received ₹4,367 per capita⁷⁵ (refer to Annexure 4.12 for state-wise implications).

⁷³ Minimum needs indicators refer to basic service benchmarks used to assess levels of deprivation in essential public services. In the context of the XII Finance Commission's Index of Deprivation, these included:

- i. percentage of households fetching drinking water from a distance of over 100 metres,
- ii. percentage of households without latrines within their premises, and
- iii. percentage of households without drainage for wastewater.

These indicators were used to identify states where local governments faced greater challenges in delivering core municipal services.

⁷⁴ The Index of Decentralisation, aimed to assess the extent to which states had empowered local governments. It considered legislative, functional, fiscal, and electoral dimensions of decentralisation—such as the assignment of functions, taxation powers, conduct of local elections, and establishment of District Planning Committees. The Index of Deprivation, shifted focus to inter-state disparities in access to basic services. It used minimum needs indicators—such as access to drinking water, sanitation, and drainage—to identify states where local government faced greater service delivery deficits. The Index of Devolution, sought to quantify actual fiscal transfers to local government based on state finance accounts. It measured the share of non-plan revenue expenditure devolved to local governments over a three-year period, adjusted for inconsistencies in data reporting.

⁷⁵ The urbanisation rate includes census towns and outgrowths.

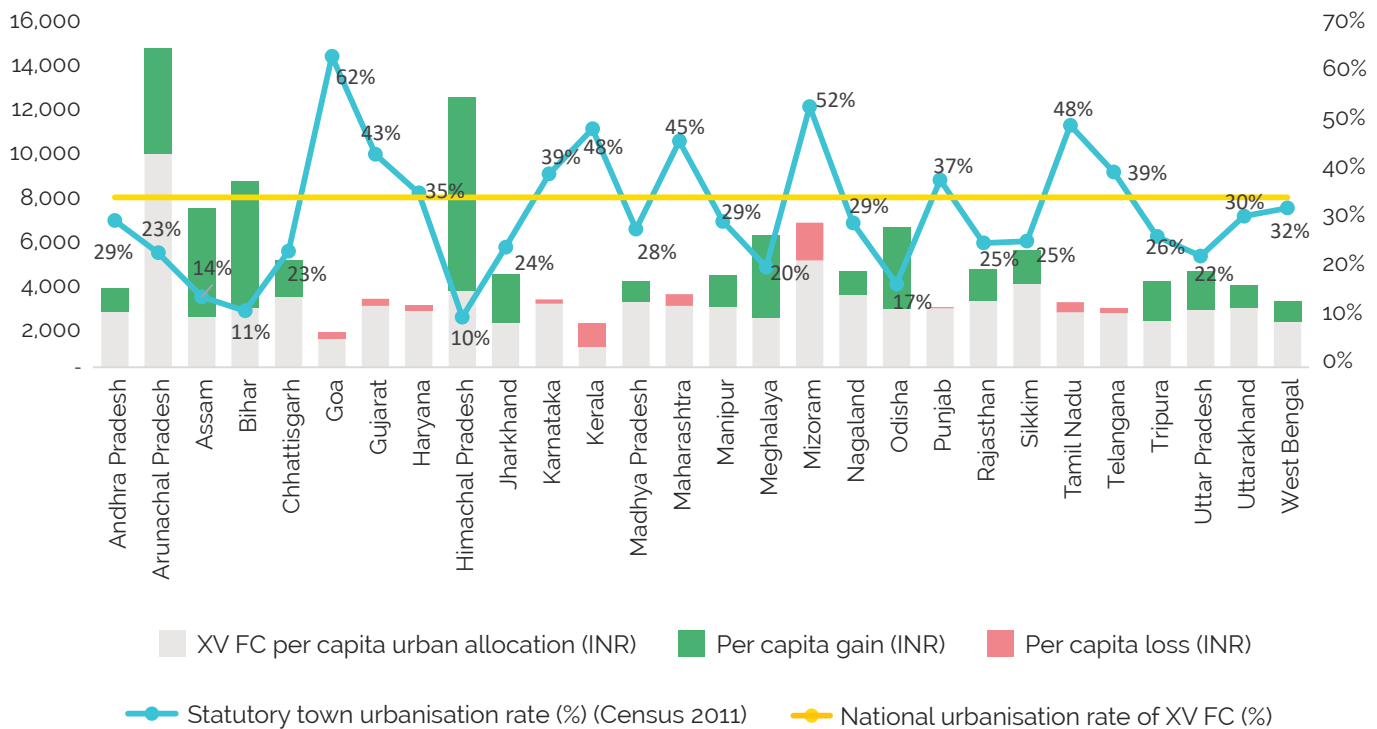


Figure 14: State which have lost/gained under the distribution method to state under XV FC

4.3.1 Correcting Horizontal Distribution Imbalances: Recommendations for the XVI FC

To address the skewed allocations under the XV FC and ensure a more equitable distribution of grants between RLGs and ULGs, we have evaluated two methods based on their simplicity and effectiveness.

Method 1: Bottom-up approach

Similar to the approach used by the XIV FC, this method uses each state's rural and urban population data from the 2011 Census to determine inter-state allocations, building the rural and urban grants quantum from the bottom-up. This approach would result in rural grants comprising approximately 70% of total LG grants, with urban grants accounting for about 30% (refer to Annexure 4.13). While this ensures that rural and urban LGs receive allocations aligned with population, it relies on outdated data that no longer reflects current ground realities. Moreover, equal per capita allocations across rural and urban areas do not account for the differentiated nature of service delivery needs.

We also used the Ministry of Health and Family Welfare's latest population projections from 2019 to update rural-urban ratios. While more current, these projections produce anomalies. For example, states like Goa and Kerala, with high projected urbanisation, would receive over 80% of their total LG grants as urban allocations, which does not reflect on-ground realities.

Method 2: Dual-track approach

According to this method, local government grants are distributed in a 60:40 ratio and calculated as follows:

- 1. Urban grants based on each state's proportion of the country's total urban population, as per the 2011 Census.**
- 2. Rural grants based on the rural population and area in a 90:10 ratio.**

This would result in an allocation of ₹5,70,000 crore for rural areas and ₹3,80,000 crore for urban areas based on the proposed local government grants for the XVI FC Period.

This method builds on the longstanding practice of Finance Commissions using population as the core parameter, while eliminating geographical area as criterion for urban grants, given that urban areas account for only 3% of India's landmass.

This dual-track method, calculating rural and urban shares independently captures the differing expenditure patterns across jurisdictions. For urban areas, where population density is typically high and land area is limited, geographical area plays a minimal role. In contrast, rural areas contend with sparse populations and large geographies, making area a more relevant factor for rural allocations.

We recommend that the XVI FC apply Method 2 to correct the imbalances caused by applying a uniform rural-urban ratio across states. This method will ensure that both rural and urban local governments in every state receive an equitable share of grants. Furthermore, this approach results in minimal deviation from the X FC's overall share of LG grants to each state, and is likely to result in greater acceptability (refer to Annexures 4.13 and 4.14)

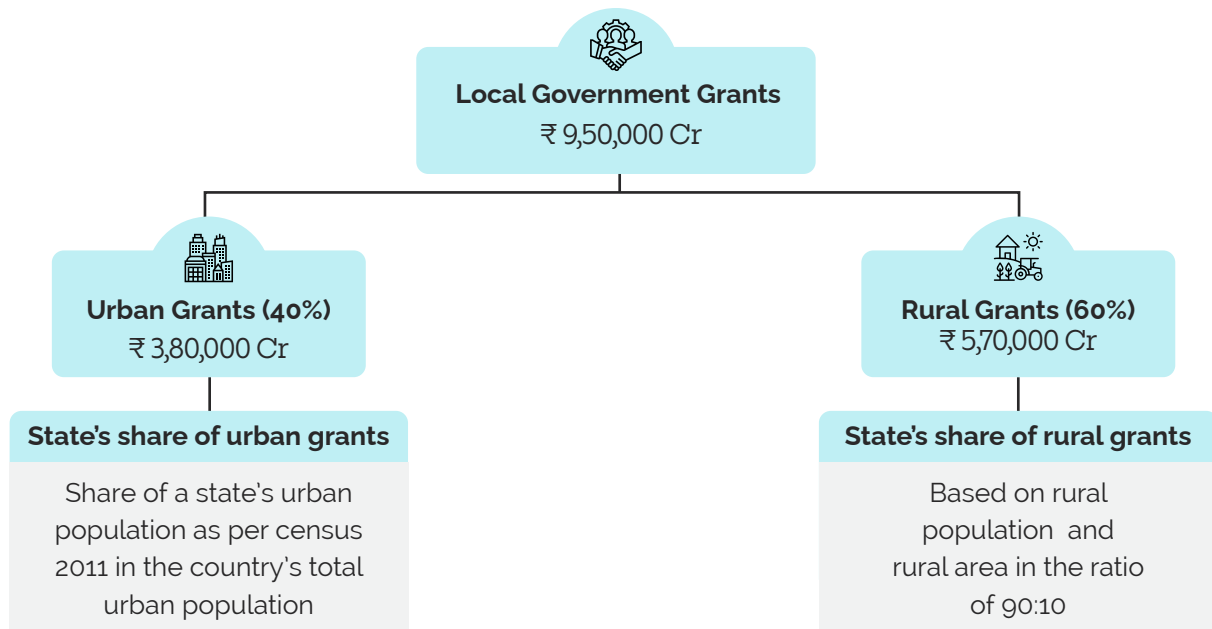


Figure 15: Methodology for distribution of urban grants to states

4.4 Grant Architecture Recommended by Previous FCs

In this report, 'grant architecture' refers to the combination of:

1. Types of grants
2. Intended end-use of those grants
3. Conditionalities for claiming the grants

This section analyses the grant architecture of Finance Commissions (X to XV), examining their design, intent, and implementation where possible. The goal is to distil key lessons and principles that will inform the XVI FC's approach to urban grant architecture.

Over time, grant architecture has evolved from largely unconditional, untied allocations to more targeted, conditional, and outcome-based frameworks. Three primary types of urban grants have emerged over successive FCs: basic grants (both untied and tied), performance-based grants, and additional/special grants.

Basic grants are classified into untied and tied grants. Untied grants offer ULGs the flexibility to address local priorities and operational needs. Tied grants, on the other hand, are defined by the Finance Commission and are typically earmarked for specific sectors, such as sanitation or drinking water.

Performance-based grants are allocated to ULGs based on their performance against pre-defined benchmarks in key areas such as sanitation, education, and fiscal management. These grants incentivise improved governance, efficiency, and service delivery by rewarding measurable progress.

Additional/Special grants are purpose-specific allocations aimed at addressing critical gaps in sectors such as health, education, and urban infrastructure, or governance areas like shared services, capacity building, and decentralisation. These grants are designed to strengthen underperforming or strategically important areas through targeted financial support.

Table 9: Evolution of Grant Types from X FC to XV FC

FC	Basic Grants		Performance-based Grants		Additional/ Special Grants
	Untied	Tied	Untied	Tied	
X FC	✓				
XI FC	✓				✓
XII FC	✓				
XIII FC	✓ (65%)		✓ (35%)		
XIV FC	✓ (80%)		✓ (20%)		
XV FC (all conditional grants)	✓	✓		✓	✓

Finance Commission grants to ULGs initially began as largely unconditional, allowing ULGs to use funds based on local needs, barring a few stipulations. The X FC provided 100% untied grants, intended for the development of essential local services. States were required to develop schemes for their utilisation and were prohibited from using the funds for salaries or wages.

A subtle shift occurred with the XI FC, which introduced additional/special grants to address the lack of reliable financial and budgetary data for local governments. It recommended that states develop comprehensive databases on the finances of RLGs and ULGs, estimating a total cost of

₹200 crore for this effort, with approximately ₹2.94 crore earmarked specifically for ULGs. This ₹200 crore was tied and treated as the first charge on the overall local government grant. However, utilisation data from the Ministry of Finance reveals that only ₹93 crore was spent on database creation, resulting in a utilisation rate of just 47%. The remaining ₹9,200 crore local government grants was untied in principle, with restrictions in place for utilisation on salaries.

The XII FC recommended 100% untied to ULGs. While the FC refrained from specifying sectoral allocations due to a lack of credible cost data, it recommended prioritising water supply and sanitation. Additionally, towns with populations over 1,00,000 were encouraged to earmark 50% of funds for solid waste management projects, preferably through public-private partnerships, though this was not mandatory.

A key shift occurred with the XIII FC, which introduced a two-tier grant structure for ULGs:

1. Basic grants (65%), continuing the practice of untied grants, and
2. Performance-based grants (35%), linked to compliance with nine reform criteria.

These performance grants, while untied in usage, were conditional on states and ULGs meeting procedural and institutional reform requirements. However, the uniform application of conditions, regardless of ULG size, maturity, or institutional capacity, impacted performance and limited access to funds. The Ministry of Housing and Urban Affairs (MoHUA) also observed that these rigid conditions led to poor absorption, as most states failed to consistently meet all nine criteria. For example, Assam was allocated ₹87.68 crore in general performance grants between 2011–12 and 2014–15, but received only ₹10.18 crore in the first year. No further releases occurred due to non-fulfilment of conditions, resulting in a forfeiture of ₹77.50 crore⁷⁶. The Ministry recommended a shift toward outcome-based performance measures focused on revenue, productivity, and service delivery rather than complex procedural compliance⁷⁷.

In addition, oversight bodies, such as High-Level Monitoring Committees (HLMCs) chaired by state chief secretaries, were intended to monitor compliance. However, being embedded within the same administrative hierarchy limited their independence, undermining their effectiveness in ensuring accountability⁷⁸.

The XIV FC retained the two-tiered grant structure (80% untied basic grants and 20% performance-based grants) but significantly simplified the requirements to:

1. Submission of audited accounts
2. Increase in own revenues, and
3. Disclosure of service-level benchmarks.

⁷⁶ Comptroller and Auditor General of India. (2018). Performance audit of utilisation of 13th and 14th Finance Commission grants by urban local bodies of the Republic of India (Chapter 5).

⁷⁷ Fourteenth Finance Commission. (2015). Report of the Fourteenth Finance Commission. Government of India.

⁷⁸ Department of Expenditure, Ministry of Finance, Government of India. (2016, March 17). Guidelines of local bodies with utilisation certificate.

While this simplification improved performance, it did not meaningfully drive reform momentum, particularly in larger ULGs. Of the ₹17,489 crore allocated as performance grants, only ₹5,890 crore (approximately 34%) was disbursed. Despite the easing of conditions in the final two years, no further performance grants were released. In contrast, 97% of basic grants (₹67,531 crore out of ₹69,715 crore) were successfully disbursed⁷⁹. The relatively low annual performance grant allocated to each state likely failed to provide enough incentive for states to take effective action, resulting in poor performance grant absorption.

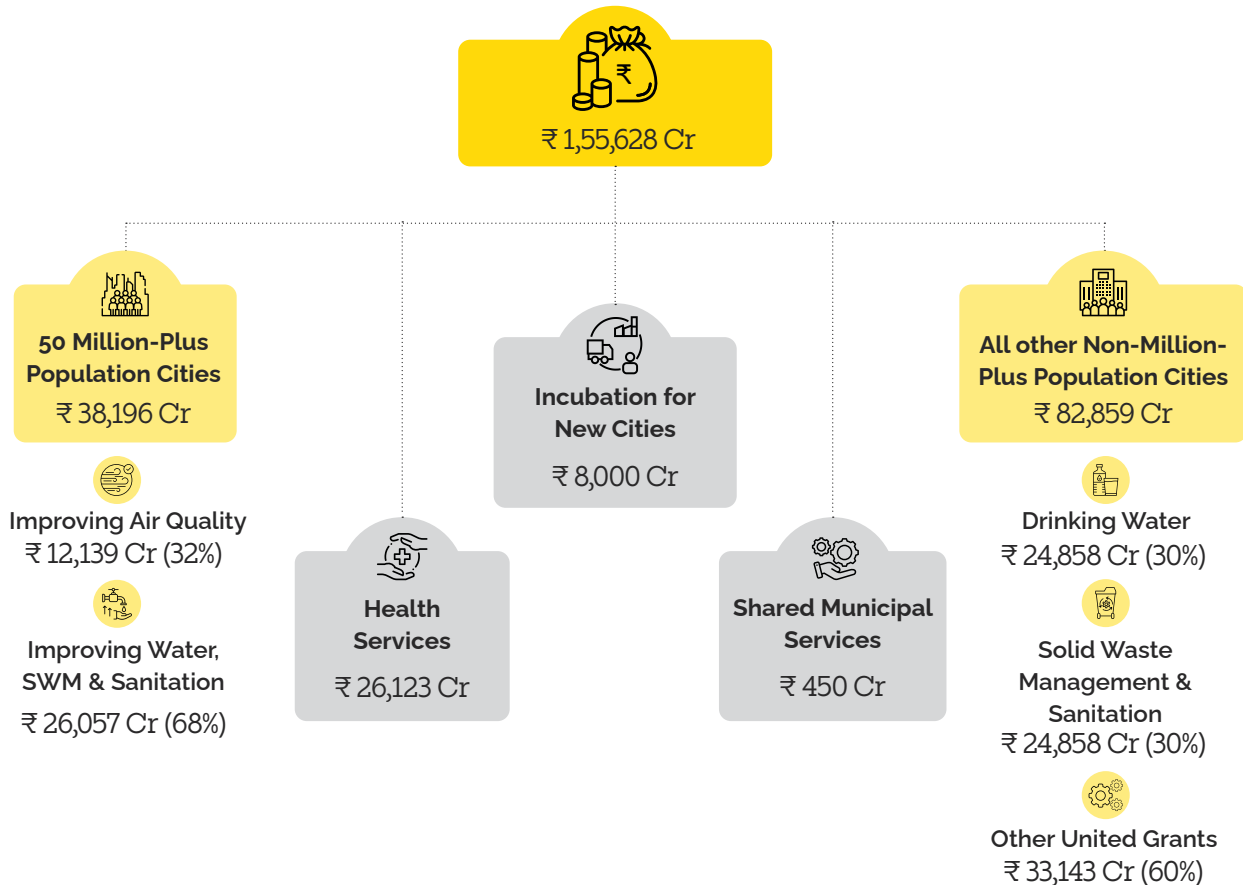


Figure 16: Urban grant architecture under XV FC

The XV FC introduced a differentiated grant architecture based on ULG size and typology. This approach recognised India's urban diversity, acknowledging that metropolitan cities face distinct challenges and opportunities compared to smaller towns. ULGs were subsequently classified into two categories:

- Category I:** Urban Agglomerations or cities with populations exceeding one million (Million-Plus Cities or MPCs)

⁷⁹ MoHUA. The data was given to XVI FC by MoHUA in their urban memorandum.

2. Category II: Cities and towns with populations below one million (Non-Million-Plus Cities or NMPCs).

Although a marked departure from the one-size-fits-all approach of previous Finance Commissions, this differentiated grant architecture aligned with the vision for metropolitan areas under Article 243P of the Constitution (74th Amendment Act, 1992).

The following sections examine this architecture: how it was designed, its implementation on the ground, and the lessons it holds for the XVI FC.

Unlike earlier Commissions, all ULG grants by the XV FC — whether tied, untied, or performance-based — were subject to four eligibility conditions introduced by the FC, along with two conditions set by the Department of Expenditure (DoE). These are discussed further in Chapter 5.

Table 10: Eligibility Conditions for XV FC Grants

Sl. No.	Basic Grants	2021-22	2022-23	2023-24	2024-25	2025-26
1	Publish provisional and audited annual accounts	✓ (25%) ULGs	✓ (25%) ULGs	✓	✓	✓
2	Notify property tax floor rates		✓			
3	Consistent improvement in collection of property taxes in tandem with growth rate of state's own GSDP			✓	✓	✓
4	Constitution of SFC and laying of ATR in the state legislature on or before March 2024				✓	✓
5	Certificate for unspent balance of XIV FC grants		✓	✓	✓	✓
6	Duly elected local governments in the state			✓	✓	✓

FC DoE To be fulfilled by state

The XV FC allocated ₹1,55,628 crore as total urban grants during 2021–26. Of this, ₹34,213 crore was allocated as special grants/additional grants, including ₹26,123 crore for health services, ₹8,000 crore for the incubation of new cities, and ₹450 crore for shared municipal services. The remaining ₹1,21,055 crore was assigned to MPCs and NMPCs under tied and untied structure.

MPCs received 100% performance grants tied to outcome improvements in air quality, water, and sanitation.

NMPCs received a mix:

1. 60% tied to sectoral priorities, of which 50% is tied to sanitation (including solid waste management) and 50% is tied to drinking water, rainwater harvesting and water recycling.
2. 40% untied and can be used by the ULGs for felt needs under the eighteen functions enshrined in the Twelfth Schedule, except for salaries and other establishment costs.

However, two key concerns were observed with this grant architecture:

1. The urban grants were fragmented into three special grants, marking a departure from past practices. Approximately 22% of the total grants were allocated as special grants to areas outside ULG jurisdiction. This resulted in diluted accountability and very poor uptake.
2. Of the remaining allocation, 73%⁸⁰ was tied to specific sectors, such as air quality, sanitation, and drinking water. While this alignment with national priorities was intentional, it sharply reduced ULG discretion in addressing local needs.

This shift raises important questions about local autonomy, and whether stringent funding structures sufficiently accommodate city-specific development needs. Critics argue that such a high proportion of tied funding could undermine the ability of ULGs to set their own spending priorities, effectively reducing them to implementing agencies for centrally determined priorities⁸¹.

The following sections examine the XV Commission's implementation experience in detail, focusing on performance-based grants to MPCs and sectoral allocations to NMPCs. Due to limited data availability, special/additional grants have not been assessed in detail. This examination provides crucial insights into designing a more effective urban grant architecture for the XVI FC.

4.4.1 The Million-Plus Cities Challenge Fund (MCF): Design, Implementation, and Lessons

The XV FC's most ambitious intervention was the recommendation of a performance-linked, outcome-based grant mechanism exclusively for million-plus Urban Agglomerations (UAs). As part of the Million-Plus Cities Challenge Fund, a total of ₹38,196 crore was allocated to 50 UAs, with grants divided into two components:

1. ₹12,139 crore was linked to improvements in air quality.

⁸⁰ The figure of 73% refers to the share of tied grants (₹87,880 crore) allocated for specific sectors—such as air quality, sanitation, and drinking water—out of the total ₹1,21,055 crore granted to Million-Plus Cities (MPCs) and Non-Million-Plus Cities (NMPCs) under the XV FC, excluding the 3 special grants.

⁸¹ Centre for Water and Sanitation. (2020, October). Strengthening finances of municipal governments (White Paper). CRDF, CEPT University. Retrieved from https://cwas.org.in/resources/file_manager/Strengthening_Municipal_Finances%20_White_paper.pdf

2. ₹26,057 crore linked to performance against Service Level Benchmarks (SLBs) in drinking water supply, sanitation, and solid waste management.

The air quality grant was designed to support the National Clean Air Action Plan (NCAP) launched by the Ministry of Environment, Forest, and Climate Change (MoEFCC) in January 2019. While the annual allocation was based on population, the grant introduced performance-based disbursement mechanisms to incentivise outcomes⁸². The plan initially targeted a 20-30% reduction in particulate matter concentrations in 102 ULGs by 2024, later revised to a 40% reduction in 131 ULGs by 2026⁸³.

As of July 2025, ₹12,645 crore⁸⁴ has been released to 130 ULGs⁸⁵ under NCAP for implementing City Action Plans (CAPs). Of this, XV FC grants account for ₹11,030 crore — 79.25% of the ₹13,918 crore allocated to Million-Plus Cities (MPCs) between 2020–21 and 2024–25. Of the transferred funds, 69% have been utilised, representing 55% of the total allocation⁸⁶. These figures underscore both the significant role of XV FC grants in financing NCAP implementation and the persistent gaps in fund utilisation. Annexures 4.16 and 4.17 present a detailed analysis of the challenges driving these gaps and propose recommendations to improve future performance.

The larger SLB-linked component of the MCF was designed around a structured performance framework aimed at tracking measurable service delivery improvements. To access these grants, MPCs were required to fulfil three conditions, in addition to the basic eligibility conditions outlined in Table 11.

Table 11: Performance Conditions for SLB-linked Grants to Million-Plus Cities under XV FC

Sl. No.	Performance Grant Conditions	2021-22	2022-23	2023-24	2024-25	2025-26
1	Sign tripartite MoU between state, ULG, and MoHUA establishing SLBs and annual targets for the award period	✓				
2	Publish all 28 SLBs online, along with ODF and GFC certificates and performance scores on 4 priority indicators against defined targets		✓	✓	✓	✓
3	Publish Detailed Utilisation Report (DUR)	✓	✓	✓	✓	✓

⁸² Disbursement was linked to two performance indicators: (i) reduction in PM₁₀ concentration, and (ii) increase in the number of good air quality days. For ULGs falling short of top performance thresholds, 50% of their undisbursed funds were redistributed to better-performing cities.

⁸³ The plan initially targeted a 20-30% reduction in particulate matter concentrations (PM_{2.5} and PM₁₀) in 102 ULGs by 2024. It was later revised to a 40% reduction in PM₁₀ in 131 ULGs by 2026, along with an increase in improved air quality days.

⁸⁴ Rajya Sabha Unstarred Question no. 2775, 2024. Retrieved from https://sansad.in/getFile/annex/266/AU2775_iH6kU8.pdf?source=pqars

⁸⁵ Hyderabad and Patancheru UA is considered as a single entity, so the number of cities have reduced from 131 to 130.

⁸⁶ Central Pollution Control Board. (n.d.). PRANA: Portal for regulation of air-pollution in non-attainment cities. <https://prana.cpcb.gov.in/>

Performance grants were disbursed based on achievements against four core indicators: (i) households covered with piped water supply, (ii) water supplied in litres per capita per day, (iii) reduction in non-revenue water, and (iv) households covered with sewerage and septage services. Additionally, ULGs had to meet prescribed targets for Garbage Free Star Rating and Open Defecation Free certification.

By FY 2023–24, ₹11,998 crore of the ₹26,057 crore SLB-linked grants had been released—an 81% annual disbursement rate that exceeded the XIV FC period⁸⁷. However, several challenges were observed owing to design limitations and capacity constraints:

1. **Absence of governance mechanisms in Urban Agglomerations:** Article 243ZE of the Constitution mandates Metropolitan Planning Committees (MPCs) in every metropolitan area to prepare regional development plans. However, CAG audits⁸⁸ reveal that only 3 out of 18 states with metropolitan areas (as defined by the 2011 Census) had operationalised MPCs. In the absence of these metropolitan-level planning and coordination bodies, the XV FC's agglomeration-based grant could not be effectively implemented. While state urban development departments could have filled this coordination role, ground evidence suggests most states failed to do so effectively.
2. **Ineffective coordination by nodal entities:** For Urban Agglomerations containing multiple MPCs, state governments in consultation with the MPCs were required to designate one ULG as the nodal entity to receive grants and achieve performance indicators for the entire agglomeration. In most cases, the largest ULG within the agglomeration was designated the nodal entity. However, these larger ULGs often lacked both incentives and formal mechanisms to coordinate with surrounding smaller ULGs, resulting in fragmented planning and execution. Many smaller ULGs remained unaware of their eligibility for performance-based grants and had no incentive to invest in improving service levels.
3. **Involvement of parastatals in service delivery:** In many of ULGs, state parastatals are responsible for water supply and related services. Holding ULGs accountable for performance in areas outside their jurisdiction created misplaced accountability.
4. **Project-specific performance linkages create delays:** State governments and urban agglomerations signed MoUs with MoHUA specifying year-wise action plans, target outcomes, fund releases, and specific projects. ULGs were required to demonstrate yearly progress on land acquisition, Detailed Project Report (DPR) preparation, statutory approvals, and project completion. However, linking performance to specific projects proved problematic when projects faced implementation delays, often unavoidable or outside the purview of the ULG. Data from

⁸⁷ Sourced from CityFinance as on 31.03.2025.

⁸⁸ Comptroller and Auditor General of India. (2023). Compendium of performance audits on the implementation of central schemes.

MoHUA indicates that 30 out of 50 million-plus Urban Agglomerations sought amendments to their initial project proposals due to delays in meeting milestones.

- 5. Weak monitoring and verification systems:** Although SLB frameworks have been in place since the XIII FC, service level reporting remains poor in ULGs. Moreover, MoHUA lacked systems to verify the accuracy of ULG-reported SLB data. The lack of third-party verification further undermined the credibility of performance claims.

Performance grants remain a valuable instrument for incentivising improvements, particularly given the role of ULGs as frontline service providers. However, their success depends critically on design. The XV FC experience offers important lessons for the XVI FC's approach to performance-based grants.

Table 12: Principles for Performance-linked, Outcome-based Grants

Coverage
1. Prioritise a limited number of large and high-impact ULGs for concentrated interventions, rather than spreading resources thinly across all ULGs. 2. Establish shared accountability between state governments and MoHUA for management and progress tracking, and between NITI Aayog and the Ministry of Finance in overseeing the urban economy. 3. Ensure that grant amounts are substantial enough to incentivise genuine reform and encourage long-term commitment from ULGs.
Indicators
1. Design performance indicators that are simple, measurable, and easy to administer and monitor. 2. Indicators should be within the functional jurisdiction of ULGs, and should be achievable within the grant period.
Monitoring and Verification
1. Invest in outcome tracking and third-party verification to maintain credibility and ensure transparency. 2. Reporting on indicators should not pose undue administrative burden on ULGs. 3. Data to measure performance should be readily available or easy to collect.
End Use
1. Broaden the grant agenda to include not only service delivery improvements but also the facilitation of urban economic growth, competitiveness, and sustainability.

4.4.2 Grants to Non-Million-Plus Cities (NMPCs): Design, Implementation, and Lessons

The XV FC allocated ₹82,859 crore over five years to Non-Million-Plus Cities, distributing these basic grants according to population to address diverse service delivery challenges.

The grants were structured as follows:

1. 40% untied grants: ₹33,143 crore for any of the 18 functions under the Twelfth Schedule, excluding salaries and establishment costs.
2. 60% tied grants: ₹49,716 crore allocated for strengthening service delivery in two core sectors:
 - i. 50% for solid waste management (SWM) and sanitation
 - ii. 50% for drinking water, rainwater harvesting, and water recycling.

ULGs could transfer tied funds between the two sectors if they had fully addressed the infrastructure needs of one category and required no further investment in that area. This required certification by the ULG, confirmation by the state's supervising authority for ULGs, and final submission to MoHUA.

NMPCs within Urban Agglomerations received these basic grants alongside their Metropolitan Challenge Fund allocations.

In addition to meeting the mandatory eligibility conditions outlined earlier, NMPCs were required to fulfill two performance criteria, as detailed in MoHUA's operational guidelines, specifically for tied grant release.

Table 13: Grant Conditions for NMPC Grants under the XV FC

Sl. No.	Grant Conditions	2021-22	2022-23	2023-24	2024-25	2025-26
1	Publish baseline data, set annual targets till 2025-26, report yearly achievements, and track service level benchmark progress	✓	✓	✓	✓	✓
2	Publish Detailed Utilisation Report		✓	✓	✓	✓

First, NMPCs must publish baseline service data, annual targets till 2025-26, yearly achievements, and tied grant utilisation details on the CityFinance. While meeting these targets is not mandatory

for grant release, NMPCs that achieve their targets become eligible for any undistributed MPC grant funds, allocated proportionally based on Census 2011 population data.

Second, NMPCs must submit a Detailed Utilisation Report⁸⁹ (DUR) on CityFinance before receiving their first tied grant instalment, as required by Department of Expenditure (DoE) guidelines. These reports are entirely self-reported by ULGs, with no independent monitoring or verification mechanism currently in place.

By contrast, untied grants have no such reporting requirements, resulting in significant transparency and accountability gaps. Utilisation data for these grants is not published on CityFinance and remains accessible, if at all, only through state monitoring systems. Even where such data exists⁹⁰, utilisation rates and expenditure patterns are not consistently tracked or reported either at the ULG or at the state levels. This absence of reliable and standardised data significantly hampers the ability to assess how untied grants are being used and what outcomes they are achieving.

4.4.2.1 Utilisation of Tied and Untied Grants

Analysis of DURs from 2,056 NMPCs on CityFinance shows that tied grant utilisation remained modest at 49%⁹¹ between 2020–21 and 2023–24. Spending patterns reveal an imbalance: 54% of tied grants went to solid waste management and sanitation, while 46% supported drinking water-related services. This deviates from the XV FC's intended 50–50 split between these sectors. Refer to Annexures 4.19.1 and 4.19.2 for a detailed analysis of tied grant utilisation.

Untied grants demonstrate significantly higher utilisation rates than tied grants. In Telangana⁹², untied grants achieved 77% utilisation compared to 53% for tied grants. Maharashtra⁹³ showed a similar pattern, with untied grants reaching 60% utilisation versus 41% for tied grants.

Expenditure patterns in Maharashtra mirror the national trend: 66% of tied grant spending focused on sanitation and solid waste management, with only 25% allocated to drinking water services. Untied grants in the state showed greater diversity, with 58% directed toward electricity

⁸⁹ The information submitted is entirely self-reported by ULGs, and there is currently no mechanism in place for independent monitoring or verification of these reports.

⁹⁰ Few states, like Karnataka, Telangana, Maharashtra and Tamil Nadu have project tracking systems that allow tracking of grant utilisation for both tied and untied grants. While data from Karnataka could not be accessed for this analysis, other 3 states shared data about grant utilisation. Data from Tamil Nadu was excluded due to its low coverage of ULGs (47–155 ULGs across years, out of 651 total) and absence of ULG-wise, year-wise fund utilisation details, but the utilisation patterns in Telangana and Maharashtra provide insights into the challenges and opportunities associated with XV FC grants to NMPCs.

⁹¹ ULGs are required to report utilisation of tied grants alone on Cityfinance on an annual basis for claim of XV FC grants. The following findings are based on an analysis of utilisation reports (self-reported) of 2,056 ULGs from 2020–21 to 2023–24, available from cityfinance.in.

⁹² Data collected for 141 ULGs (excluding Greater Hyderabad Municipal Corporation and Secumdarabad (Cantt) from CDMA office during our field visit on 26-09-2024. This includes ULG-wise release and utilisation data only and does not provide project-wise expenditure report. A total of ₹781 crore was released to 141 ULGs during the period 2021–22 to 2023–24 and of this, ₹495 crore or 63% was utilised.

⁹³ Data collected from UDD Maharashtra, as on date 27-01-2025.

infrastructure, 23% to general municipal expenses, and 10% to sewerage and solid waste management (refer to Annexures 4.20 and 4.21 for detailed analysis of utilisation of tied and untied grants in Telangana and Maharashtra).

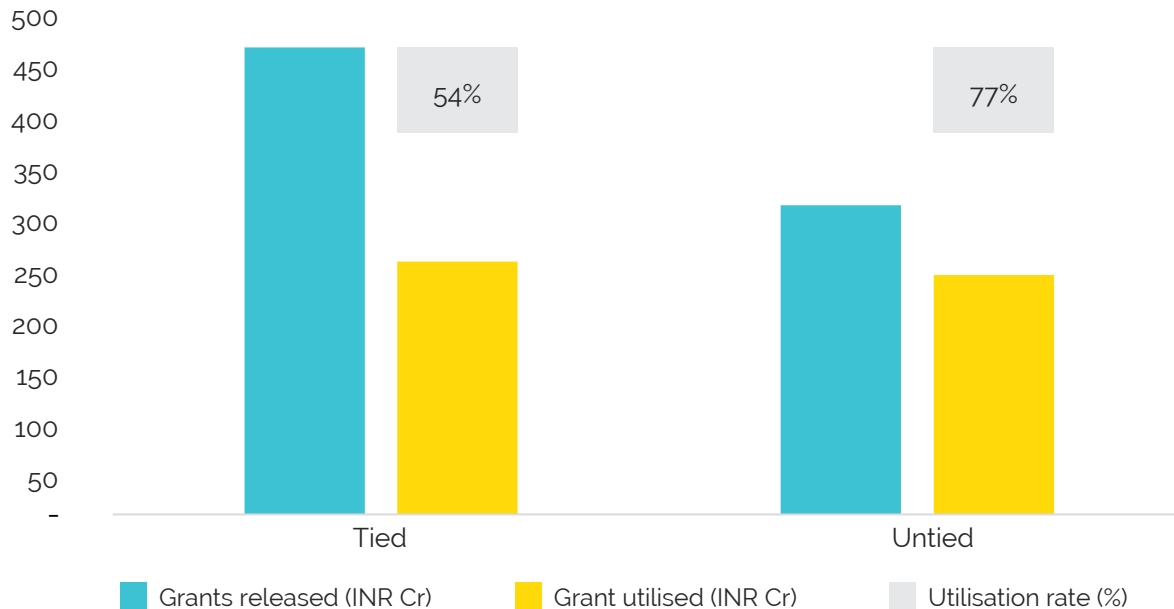


Figure 17: Utilisation rate of tied and untied ULG grants to Telangana during the period 2021-22 to 2023-24

While utilisation of untied grants is high across all ULG population categories⁹⁴, tied grant utilisation varies by ULG size. Metropolitan cities with populations above 4 million achieved exceptional utilisation rates of 98% across all four years. Despite representing a small fraction of the population, these ULGs dominate grant absorption due to their stronger administrative capacity, established systems, and robust project pipelines.

By comparison, medium and small ULGs, particularly those with populations below 1 million, struggled with tied grant utilisation:

1. ULGs in the 1–4 million category started from a very low base of just 7% utilisation in 2020–21 and, despite steady improvement, reached only 37% by 2023–24.
2. ULGs with populations between 100K to 1 million show stagnant or even declining performance in recent years. Utilisation rate for ULGs with populations between 100K–500K fell from 27% in 2021–22 to 19% in 2023–24.
3. ULGs with populations below 100K showed modest gains but plateaued at ~31% utilisation.

⁹⁴ Basis untied grant utilisation data of Telangana, wherein ULGs with population between 500k – 1M have 76% utilisation, 100k – 500k show 80% utilisation and below 100k show 77% utilisation.

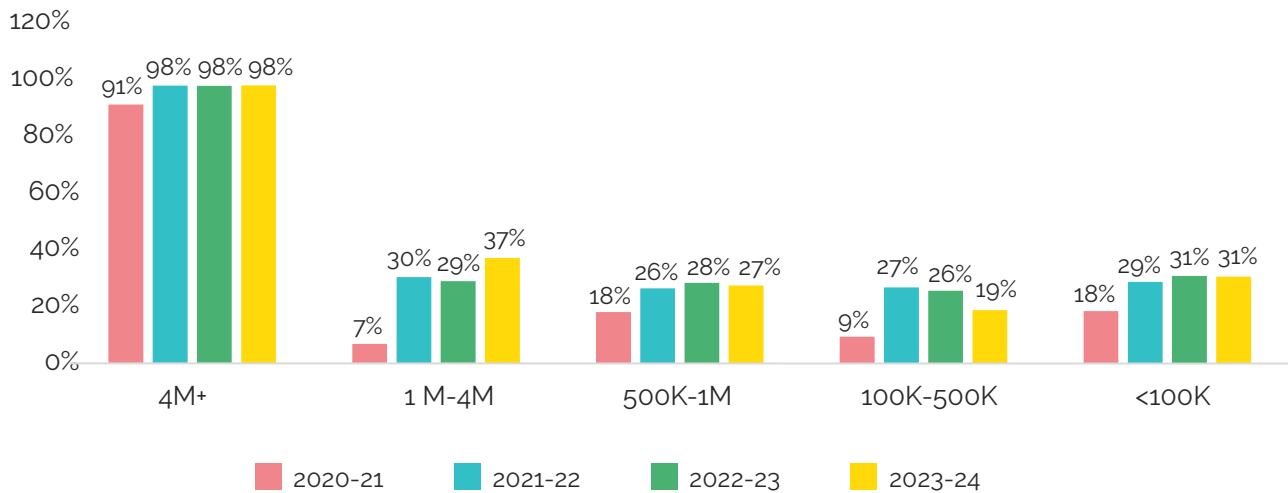


Figure 18: Population category wise utilisation rate of tied grant under XV FC

These patterns reflect the challenges smaller ULGs face in absorbing tied grants. Both sanitation and water are capital-intensive sectors, and tied grant allocations are often insufficient for meaningful projects⁹⁵. Smaller ULGs lack medium-term project planning and execution capacity. They have limited resources to raise own revenue or market funds, beyond Finance Commission grants for large infrastructure investments. Additionally, in many states, parastatal agencies manage water supply or sanitation, preventing direct ULG spending in these sectors. Consequently, rigid grant allocations reduced public expenditure efficiency.

4.4.2.2 Rethinking Tied and Untied Grants for Effective Spending

The 74th Constitutional Amendment envisioned a governance framework where ULGs would act as self-governing institutions, capable of independent planning and spending. As the third tier of government and first-mile service providers, ULGs should have the autonomy to allocate funds based on local priorities. The principle of subsidiarity also emphasises decentralisation and local autonomy, and suggests that decisions made closer to the ground, by those directly impacted, are often more effective and efficient. This is evident in the utilisation data of tied and untied grants, where utilisation of untied grants is at least 20% higher than that of tied grants. It is clear that untied grants offer ULGs the flexibility to align expenditures with local priorities and reduce utilisation hurdles.

Conversely, tied grants impose a restriction on discretionary spending, preventing ULGs from achieving allocative efficiency, i.e. the ability to direct resources toward their highest-priority areas. During the National Conference of Mayors and Chairpersons, organised by the XVI FC in November

⁹⁵ During a field visit, officials from Shamshabad Municipality, Telangana, noted that the quantum of tied grants is inadequate to undertake the scale and type of projects required under the mandated sectors.

2024, many elected representatives noted that tied grants were being spent on projects which were not a priority for the ULG. For instance, the mayor of a ULG in Uttar Pradesh highlighted that the ULG needed funds for machinery maintenance but could not access them due to the mandate for capital expenditure. Similarly, the chairperson from a ULG in Odisha mentioned that ₹97 lakh received for drinking water has remained unutilised as all households in the town panchayat are already connected to drinking water pipelines, while the ULG needed funds for libraries and other amenities but was unable to redirect the allocation. Hence, the contexts in which needs arise for each ULG are different.

Further, in the context where other sources of funding from union and state governments are becoming increasingly tied to purpose, untied grants from the Finance Commission provide crucial flexibility in spending. Tied funds dominate not only CSS and SSS flows but also SFC grants. In Karnataka, between FY 2020–21 and 2024–25, 90.76% of SFC grants to ULGs were tied, much of which was directed toward committed expenses like salaries, electricity payments, and debt servicing, rather than capital investment. The remaining 9.24% was untied⁹⁶ which also had limited flexibility, as they are largely restricted to the creation of capital assets and welfare spending for Scheduled Caste and Scheduled Tribe (SCST). This pattern of tied funding across government levels undermines decentralisation and local autonomy.

These circumstances make a compelling case for 100% untied grants from the XVI FC. Such grants should promote effective spending, which can be achieved by mandating that ULGs prepare Annual Action Plans that guide spending based on local needs and reduce ad-hoc expenditure.

To ensure balanced investment, a spending cap could be introduced, limiting no more than 50% of FC grant utilisation in a single sector over five years. Online grant management systems could track projects and sectoral spending, enabling corrective action — such as training, capacity building, or project preparation support — when ULGs concentrate funds in too few sectors. This approach would improve accountability without compromising flexibility.

4.5 Guiding Principles for Urban Grant Architecture under the XVI FC

The evolution of ULG grant architecture from the X to the XV FCs reveals a progression from simple, unconditional fiscal support towards more sophisticated and purpose-driven transfers. Basic

⁹⁶ Government of Karnataka. Budget allocations for urban local bodies. Finance Department.

grants remain the cornerstone, providing essential funds to all ULGs, while tied grants have gained prominence for promoting specific sectors and functions. Performance grants have evolved from broad institutional reforms to targeted outcome-based transfers for larger ULGs, while special and additional grants have been employed to address specific gaps and encourage innovation in the urban landscape.

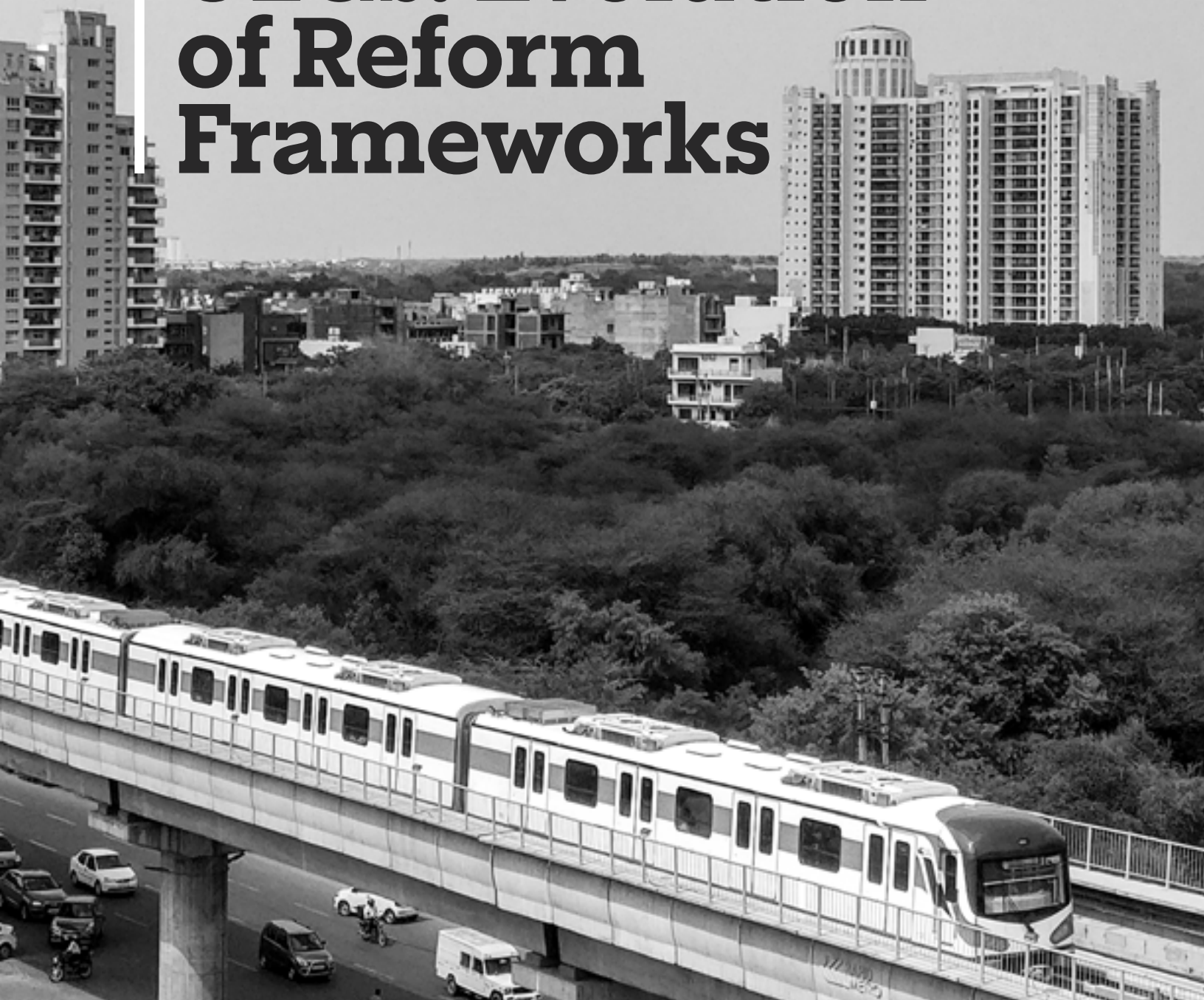
Each Finance Commission has built on the lessons of its predecessors, and the XVI FC now has the opportunity to consolidate these learnings and design a more responsive, outcome-oriented framework. The following principles are proposed to guide this architecture, ensuring that urban grants are not only better targeted and easier to administer, but also more impactful on the ground.

1. **Simplicity in grant structure:** The grant structure should be clear, concise, and easily understood by all (state government, ULGs, and citizens).
2. **Minimum conditionalities for maximum grants:** The largest quantum of grants must be linked to minimal conditions that promote financial governance and accountability.
3. **100% untied grants for all ULGs:** ULGs require predominantly untied grants to address local priorities within the Twelfth Schedule framework. These efforts should be supported by process reforms and capacity building for effective expenditure.
4. **Differentiated approach to devolution:** Grant design must continue the differentiated approach, recognising varying institutional capacities, economic potential, and service delivery needs across ULG typologies.
5. **Shift focus from service delivery to economic growth:** Grant architecture should shift focus to position ULGs as drivers of local economic growth while strengthening basic service delivery.
6. **Smart, functional performance indicators:** Performance indicators must be simple, time-bound, and within jurisdictional control of the ULG.
7. **Efficient disbursement mechanisms:** Maximum funds should be disbursed directly to ULGs through simple, timely processes leveraging digital financial systems.
8. **Robust monitoring and accountability:** Strong data systems and independent verification mechanisms must be established to track fund utilisation and outcomes.

These principles inform the grant architecture recommendations presented in subsequent chapters.

05

Eligibility Conditions for ULGs: Evolution of Reform Frameworks



This chapter examines how successive Finance Commissions have approached reform incentives, tracing the evolution of their approaches and assessing the measurable impact of the XV FC's paradigm shift to mandatory compliance. Building on this historical experience, we propose a refined set of eligibility criteria for the XVI FC that sustains reform progress while addressing implementation challenges.

Overview and Approach

Finance Commissions (FCs) have historically played a dual role: recommending measures to bridge vertical and horizontal fiscal gaps at the third tier of government, and steering vital governance reforms to enhance transparency, accountability, and financial sustainability in Urban Local Governments (ULGs). These reform recommendations, while well-intentioned and ambitious, often lacked commensurate incentives for states and ULGs to implement them. The XV FC marked a turning point by linking reform compliance directly to grant disbursement through clearly defined mandatory eligibility conditions.

This chapter examines this shift within the broader context of previous Commissions' approaches and outlines the priority reforms to be incorporated into the XVI FC framework, with the aim of preserving reform momentum while addressing observed design gaps.

5.1 Systemic Issues and Evolving Commission Approaches: X to XV Finance Commission

From the X FC to the XV FC, successive Commissions have repeatedly identified consistent legacy issues in ULGs such as: the lack of credible financial and service-level performance data, weak revenue mobilisation, and ineffective State Finance Commissions. While the XI and XII FCs made advisory recommendations, the XIII and XIV FCs transitioned to an incentive-based approach and linked portions of grants to performance outcomes. The XV FC went further, linking all grants to compliance with reform conditions.

This section examines the key challenges that successive FCs attempted to address through reforms.

5.1.1 Lack of Financial and Performance Data

Successive Finance Commissions have consistently flagged the lack of reliable, publicly available financial and performance data in ULGs. Without this foundation, effective planning, monitoring, and accountability remain elusive.

Financial Data

Previous Commissions have observed that local government accounts were often incomplete, unaudited, or perfunctorily audited, resulting in an absence of credible financial data. The XI FC recognised that the financial accounts of ULGs were not properly maintained. Anticipating increased fund transfers to the third tier following the 74th Constitutional Amendment Act, the Commission designated ₹2.94 crore from ULG grants to create a financial database and build robust accounting and auditing systems under the technical supervision of the Comptroller and Auditor General (CAG) of India. The XI FC also recommended that the CAG of India should prescribe the format for the preparation of budgets and for keeping of accounts by the local governments, which should be amenable to computerisation. In response, the National Municipal Accounts Manual (NMAM) was developed in 2004 under the aegis of CAG of India to standardise municipal accounting.

XII FC acknowledged that grassroots accounting systems were essential to accurately assess the basic civic and development needs of RLGs and ULGs. The Commission therefore recommended prioritising database creation and account maintenance through modern technology and management systems.

The XIII FC adopted a more structured approach, recommending strengthened State Local Fund Audit (LFA) departments through technical guidance and support to primary auditors by the CAG. The Commission also introduced a performance grant of ₹8,000 crore (35%), contingent upon fulfilling nine conditions, two of which addressed accounting and auditing standards:

1. States should implement an accounting framework in all ULGs consistent with the National Municipal Accounts Manual (NMAM) format and codification pattern, and establish supplementary budget documents.
2. The C&AG must be given Technical Guidance and Supervision (TGS) over local government audits at every tier, and both the Annual Technical Inspection Report and the Annual Report of the Director of Local Fund Audit must be placed before the state legislature.

Both the XIII and XIV FCs used incentive-based frameworks to address the lack of financial data, linking significant portions of grants to performance. Under the XIV FC, 20% of urban grants (₹17,428 crore) were performance-linked, with three conditions in total, one of which required ULGs to

submit and publish audited annual accounts for the previous two years on their websites.

However, these earlier approaches were largely advisory and, as discussed in Chapter 4, the XIII and XIV FC frameworks were not effective enough to drive impact. The per-state annual performance grants were too small to incentivise meaningful reform, with only a few states implementing the changes. The XV FC recognised that without binding conditionality, accountability would remain elusive and made a decisive attempt to advance this agenda.

From FY 2021–22 onward, the XV FC made it mandatory for ULGs to publish their annual provisional accounts and audited accounts for the previous year in the public domain as a condition for accessing grants. The Commission also specified the minimum documents that must be included in annual accounts to prevent misinterpretation: a) balance sheet; b) income and expenditure statement; c) cash flow statement; and d) schedules to these statements. Given the complexities in auditing related to the COVID-19 pandemic, 25% of ULGs were required to meet this condition in 2021–22 and 2022–23, increasing to 100% by 2023–24.

This reform proved transformational. For the first time, every ULG in India was required to make its audited annual accounts publicly available. As of January 2025, 96% of ULGs had complied with the requirement, disclosing their financials on the CityFinance.

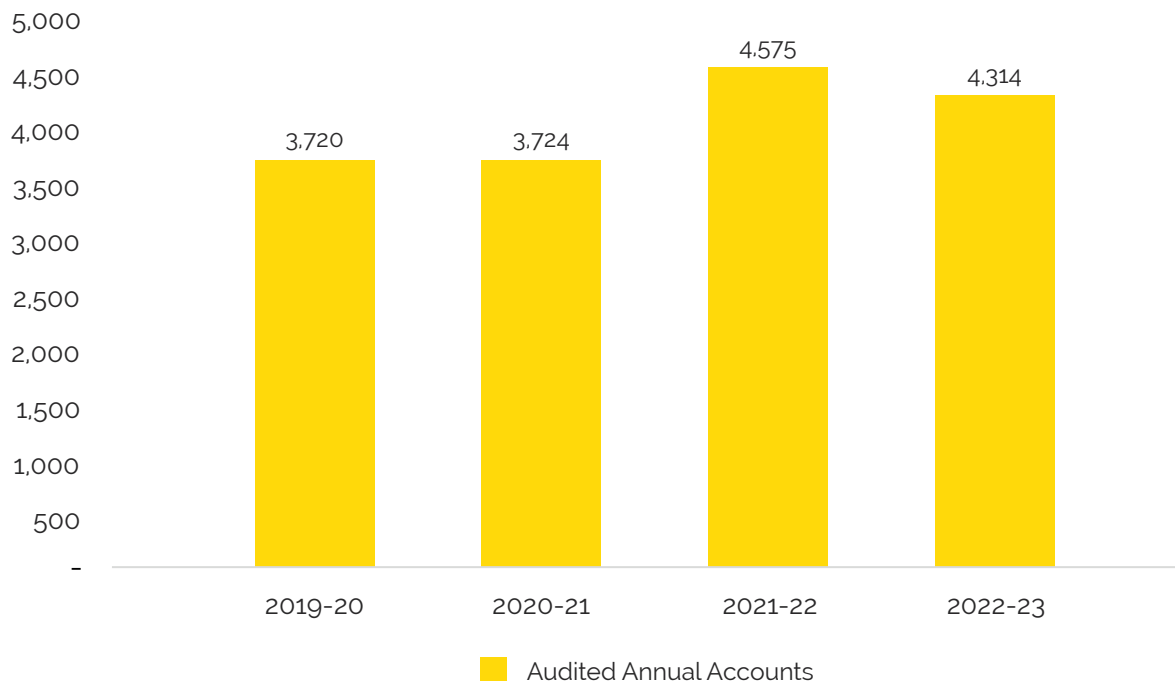


Figure 19: Year-on-year trends of number of audited annual accounts published on CityFinance

This progress has been enabled by capacity building within ULGs and institutional support from states. Both levels of government have institutionalised processes for completing audits and sharing audited statements. Data from 25 states reveals that 18 states primarily rely on external Chartered Accountants for audits, four states use Local Fund Audit Departments (LFAD) exclusively, and three states use a mix of both for auditing annual accounts of ULGs.

With data availability no longer the primary challenge, the focus must now shift towards ensuring that the published accounts meet quality standards and are available in a timely manner. Three key issues affect the quality of audited annual accounts:

1. For many ULGs, **published audited annual accounts may not be based on an accrual system**, as the transition from cash-based single-entry accounting remains a work in progress. Even in states that have transitioned, **contemporary accounting standards and principles are not consistently followed**, undermining the reliability and comparability of financial statements. The fragmented legal framework across municipal acts, regulations and manual further propagates these incongruencies.
2. **Many ULGs continue to maintain both manual registers and digital records** due to outdated state municipal laws that do not mandate electronic recordkeeping. This creates duplication of work and inconsistencies in financial data. Even where digital systems are in place, ULGs often submit financial statements as scanned PDF documents that are not machine-readable. This prevents efficient extraction and analyses of data and hinders the creation of a unified, comprehensive financial assessment across ULGs. The use of non-machine-readable formats undermines the transparency gains from the XV FC's condition.
3. **Most ULGs lack sufficiently trained internal teams** capable of preparing accrual-based, double-entry accounts that accurately reflect assets, liabilities, and depreciation. On the audit side:
 - i. Chartered Accountants (CAs) are often engaged on a contractual basis and do not perform in-depth audits of accrual systems. In many cases, the CAs are not adequately trained in accrual accounting or the NMAM format and tend to only validate numbers without fully understanding or verifying the underlying accounting systems and processes.
 - ii. Local Fund Audit Departments, despite the CAG's TGS initiatives, continue to lag in their ability to audit accrual-based accounts effectively⁹⁷. These capacity constraints weaken both the depth and quality of financial reporting and audit oversight.

To address these quality concerns, ULGs should be required to maintain a single set of audited annual accounts that provide unified, reliable records accurately representing their financial position.

⁹⁷ The World Bank. (2007). Synthesis study of public financial management and accountability in urban local bodies in India (Report No. 41204-IN). World Bank. Retrieved from <https://documents1.worldbank.org/curated/en/820961468049158494/pdf/412040IN.pdf>

Efforts must also be made to ensure timely availability of audited accounts. Under the XV FC's condition, ULGs are required to publish audited accounts for the preceding financial year, which typically results in a two-year gap between the end of the financial year and the public release of the accounts. However, a review of municipal acts in 27 states shows that 12 states (out of the 13 that specify completion periods) mandate audit completion within six months of the financial year's close. A further review of 2,594 audit reports spanning three years (FY 2019–20 to FY 2021–22), available on CityFinance, reveals audit completion delays exceed 12 months in many cases. Nevertheless, performance has improved over the years.

As depicted in Figure 20, the percentage of ULGs completing audits within 12 months rose from 40% in FY 2019–20 to 66% in FY 2021–22. This progress likely reflects ULGs and states institutionalising the requisite financial audit systems and processes in response to the XV FC's eligibility conditions. With further encouragement from the XVI FC and support from the CAG of India, the Institute of Chartered Accountants of India (ICAI) and state governments, ULGs should be able to complete audits and publish audited financial statements by the end of September each year.

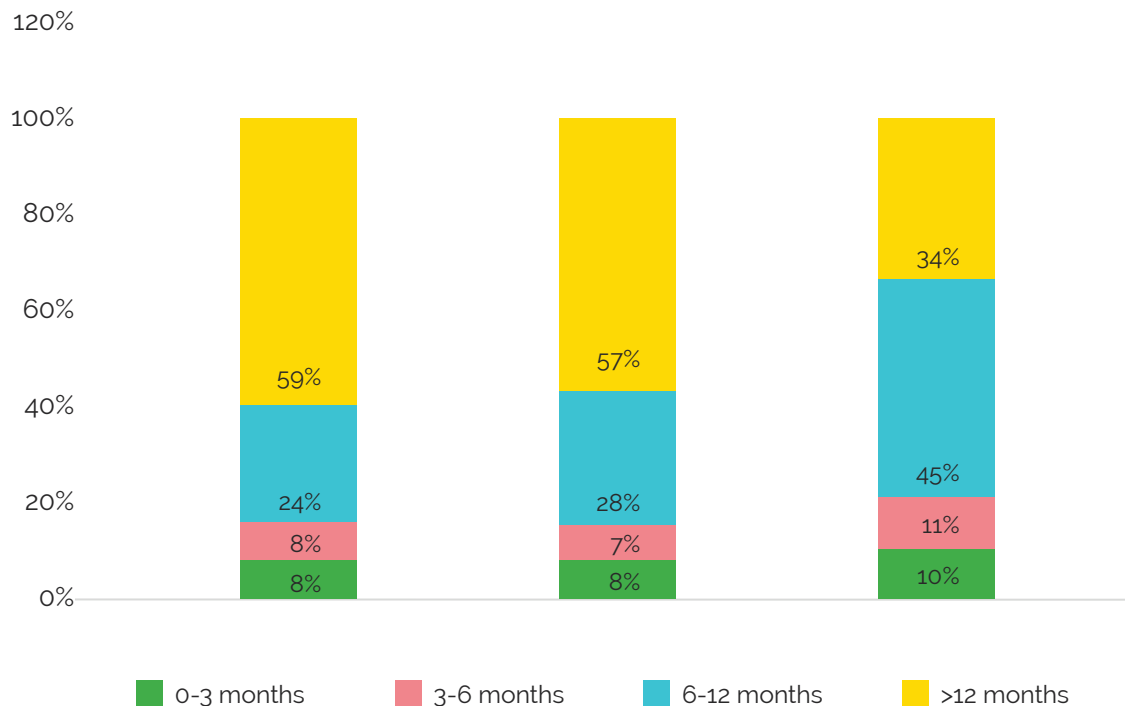


Figure 20: Period of audit completion of 2,594 ULGs, from end of financial years (Source: Analysis of audit reports from CityFinance)

The focus of fiscal accountability and transparency has remained narrow, limited to audited annual accounts while neglecting municipal budgets. Budgets serve as essential tools for transparency and accountability, offering actionable and granular data on allocations and civic works. They also enable citizens to hold governments accountable by comparing promises with delivery. Currently, only 18 states⁹⁸ mandate public disclosure of budgets, despite all ULGs being legally required to prepare them. Implementation remains weak, with only 16 out of 43 major ULGs across 11 states⁹⁹ consistently publishing complete budget documents from 2017–18 to 2023–24¹⁰⁰, highlighting a clear gap between policy and practice.

Box 4: Strengthening financial management in ULGs through revision of National Municipal Accounts Manual

The NMAM is over 2 decades old and there is a need for a comprehensive update given the amendments in statutory ecosystem, advances in digital systems and the current needs of city administrators, citizens, and market participants for real-time, credible data for informed decision-making. Hence, the revised NMAM or NMAM 2.0 is envisaged to move beyond its traditional role as just an accounting tool to a modern, digitally-enabled municipal financial management framework that supports efficient service delivery and evidence-based governance and decision-making.

Following may be some of the guiding principles for revising the NMAM:

- 1. Reorienting NMAM as a framework for municipal financial management and service delivery** that shifts from accounting alone to governance-oriented financial systems that enable resource allocation through budgeting, expenditure controls, performance reviews and comparison and data-driven decision making by city leaders.
- 2. Enabling stakeholder-oriented accounting and reporting system** that generates quality, timely financial & service delivery data in granular formats with cost data (cost accounting), functional mapping and place-based parameters (at the level of street, neighbourhood, ward, zone, city) linking expenditure to outputs and service outcomes.
- 3. Adopting a differentiated approach in accounting/ record keeping and reporting as well as digitization** for swift implementation at scale, as per the different capacities and contexts of ULGs, and their digital maturity.

⁹⁸ Andhra Pradesh, Assam, Bihar, Chhattisgarh, Goa, Gujarat, Haryana, Jharkhand, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Odisha, Punjab, Rajasthan, Tamil Nadu, Uttar Pradesh and West Bengal.

⁹⁹ Gujarat, Himachal Pradesh, Karnataka, Madhya Pradesh, Maharashtra, Meghalaya, Odisha, Rajasthan, Tamil Nadu, Uttar Pradesh and West Bengal.

¹⁰⁰ Praja Foundation. (2024). Fiscal empowerment of city governments: A study of municipal finances in India. Retrieved from https://praja.org/praja_docs/praja_downloads/Fiscal%20Empowerment%20of%20City%20Governments%20Report%202024.pdf

4. **Facilitating gradual digitalization of financial management for capturing transactions digitally at the point of occurrence** such that accounting is automated based on data from digital transaction systems and ULGs have a single digital source of machine-readable accounting information. Digital systems can be based on data standards and interoperability to allow exchange of information across systems (IFMS, PFMS/SNA Sparsh, other municipal systems)
5. **Ensuring minimum disruption to current practices** without significant change in chart of accounts to ease implementation. However, providing for GST and other developments.

This will improve the quality of financial reporting and enable ULGs to publish timely, credible, and standardised audited annual accounts, building on progress made with www.cityfinance.in and XV FC's recommendation. This will usher a shift from accounting alone to governance-oriented financial systems that enable resource allocation, performance reviews and comparison and data-driven decision making by city leaders. This will benefit a range of stakeholders, including ULGs, states, citizens, lenders and investors (such as municipal bondholders), and credit rating agencies.

For successful implementation of NMAM 2.0, states must mandate and adopt new and improved policy and technology framework, systems and processes for municipal financial management. Currently, the legal framework of municipal finance across states is fragmented, with incoherence in municipal acts, municipal finance rules and the manual. The XVI FC, while taking note of this incongruity, can suggest to states to actively synergise the municipal acts, rules and manual.

Performance Data

While significant progress has been made in improving the availability of financial data, **successive Finance Commissions have consistently highlighted a deeper, unresolved challenge: the poor quality and availability of service delivery data.**

Even by the XII FC period, most states lacked accurate and comprehensive data on the service gap of their local governments. The Commission observed that:

"The absence of data necessary for a rational determination of the gap between the cost of service delivery and the capacity to raise resources makes the task of recommending measures for achieving equalization of services almost impossible."

This insight remains acutely relevant today. Despite improvements in fiscal reporting, **ULGs still lack systematic, reliable data on the costs and quality of basic services.**

The XIII FC pioneered Service Level Benchmarks (SLBs) by mandating ULGs to notify minimum service levels for four sectors: water supply, sewerage, stormwater drainage, and solid waste management, as outlined in the Ministry of Urban Development's Handbook (refer to Annexure 5.1). State governments were required to issue notifications by 31 March 2011, committing that all municipalities and municipal corporations would meet the specified minimum service levels for each indicator by 31 March 2012. These levels could vary across ULGs and were determined through consultative processes with ULGs. This notification in the State Gazette was a prerequisite for accessing performance grants under the XIII FC framework.

The XIV FC also mandated the publication of SLBs as a condition for its performance grants (20% of total urban grants). This further institutionalised the culture of performance reporting among ULGs. ULGs were encouraged to capture and report quantifiable service delivery outcomes, incentivising ULGs toward evidence-based planning of citizen services.

The XV FC continued this approach, requiring SLB publication from Million-Plus Cities (MPCs) to claim performance-based grants. In addition to publishing data and targets for all 28 service indicators, MPCs were required to demonstrate performance improvement in four SLB indicators (refer to Annexure 5.2).

MPCs showed commendable progress in complying with these requirements: in 2020–21, 98% of MPCs published their SLBs, increasing to 100% by 2022–23 (refer to Annexure 5.3). Additionally, a significant number of MPCs achieved measurable improvements in service delivery outcomes. Water supply connection coverage improved in 81% of MPCs, while 67% recorded increased wastewater network service coverage. Non-revenue water reduced in 98% of ULGs, reflecting gains in operational efficiency and reduced distribution losses (refer to Annexure 5.4).

However, the XV FC departed from the decade-long practice of the XIII and XIV FCs by requiring only MPCs to publish SLBs, rather than all ULGs. This narrowing of scope risked diminishing the momentum built over two Commission terms. Despite this, uptake remained encouraging, with an average of 90% of ULGs with populations below one million voluntarily reporting SLBs during 2020–21 to 2022–23.

While the reporting of service level data is high, data credibility remains a concern due to following reasons:

1. Disparities in the definitions and methodologies used across ULGs for the same service indicators, leading to inconsistencies in reported data.
2. Ad-hoc data capture processes that lack standardisation or automation.
3. Absence of robust validation mechanisms.
4. Limited awareness among ULG staff about the indicators and capacity constraints to monitor performance.
5. Narrow scope of SLB indicators, which currently cover only a subset of municipal functions (water supply, sewerage, SWM, drainage), thus providing an incomplete assessment of overall service delivery performance.

Nonetheless, the act of publishing SLBs remains valuable. It fosters a culture of transparency and encourages discourse among stakeholders. However, ULGs and state governments need to strengthen data systems and processes. Moreover, as many services are increasingly delivered online, data generated from IT systems should be used for calculating service levels.

▲ Recommendations for the XVI Finance Commission

Previous FC recommendations have institutionalised public disclosure of audited annual accounts and established a foundation for regular reporting on service performance through SLBs. This has introduced accountability mechanisms at state and local government levels for municipal service levels and finance. It has also addressed the concerns of previous Finance Commissions about inaccurate data and information gaps at local levels. Therefore, the XVI FC should shift its focus to data quality.

Financial Data

1. **Discontinue the requirement for provisional accounts and mandate public disclosure of audited accounts by 31 October each year to ensure timely availability.** Such audited accounts should include: (a) auditor's report; (b) balance sheet; (c) income and expenditure statement; (d) cash flow statement; (e) receipts and payments statement; (f) schedules to the balance sheet, income and expenditure statement; and (g) significant accounting policies.
2. **Mandate public disclosure of annual municipal budgets** on the CityFinance to further institutionalise financial transparency across all ULGs.
3. **Encourage the provision of financial statements in machine-readable formats, starting with large ULGs** (populations above 500,000), to enhance comparability and enable large-scale analysis. Further, ULGs with population above 1 million should be held to higher standards of quality, wherein a disclaimer or negative certification from the auditor should attract a penalty or no grant disbursement for the year.

4. **Recommend CAG of India to revise NMAM as a comprehensive financial management framework for ULGs**, which incorporates amendments in statutory ecosystem, digital advancements and contemporary needs of stakeholders such as administrators, elected representatives, civil society and citizens, and investors. This would improve financial efficiency, effectiveness of expenditure and accountability of outputs and service outcomes, by improving the policy framework, accounting and auditing practices and digitalization of financial management in ULGs.

Performance Data

1. **Mandate SLB reporting for all ULGs** to track performance and incentivise strengthening of processes and systems for performance/SLB reporting.
2. **Recommend that MoHUA expand the SLB framework by including more sectors from the 18 functions under the Twelfth Schedule** and develop a robust reporting framework to support states and ULGs in credible reporting.

5.1.2 Weak Revenue Mobilisation

Weak revenue mobilisation has been a persistent challenge for ULGs and a critical reform area for Finance Commissions. While the XI FC primarily focused on enhancing devolution of state revenues to ULGs, subsequent Commissions adopted increasingly direct measures to strengthen local revenue generation.

The XII FC recommended deploying Geographical Information Systems (GIS) and digitisation to improve property tax administration.

The XIII FC took a different approach, focusing on institutional reforms. One of its nine performance grant conditions mandated the establishment of State Property Tax Boards to support ULGs in implementing transparent, efficient property tax assessment systems.

Like the XIII FC, the XIV FC also pursued an incentive-based approach. To access performance grants, ULGs were required to demonstrate an increase in own revenues over the preceding year, based solely on audited accounts. The calculation of revenue improvement excluded proceeds from octroi and entry tax.

In addition, the XIV FC pursued revenue diversification, advocating for broader revenue instruments. It recommended that states empower ULGs to levy vacant land tax, betterment charges, professional tax, service charges, and entertainment tax. The Commission also encouraged states to promote municipal bond financing, particularly through intermediaries to support small and medium ULGs that lack direct market access.

The XV FC noted that while property tax has proven effective internationally, averaging 1.1% of GDP in OECD countries in 2016, in India, collection remains negligible at 0.2%. Recognising that mobilising own-source revenue enhances ownership and accountability, the XV FC made property tax performance a precondition for grant eligibility.

To do this, the XV FC established a phased implementation framework. All states were required to notify a floor rate for property tax and ensure its operationalisation by FY 2021–22. From FY 2022–23, ULGs became eligible for grants only after state notification of this floor rate. From FY 2023–24 onwards, ULGs were required to demonstrate property tax collection growth matching at least the average annual growth rate of their state's GSDP over the previous five years.

While this condition aimed to ensure minimum property tax levies across all ULGs, the ambiguous terminology of 'floor rate' undermined meaningful reform. Since most ULGs already charge some property tax, states could interpret 'minimum rate' as any nominal amount, regardless of property values or market realities.

Property tax collections increased by 28% during the XV FC grant period, from ₹28,556 crore in FY 2020-21 to ₹36,661 crore in FY 2022-23¹⁰¹ (refer to Figure 21). For FY 2023-24, 80% of ULGs from 16 states met the property tax growth condition¹⁰² (refer to Figure 22), demonstrating continued improvement in collections

¹⁰¹ Based on analysis of self-reported property tax data for 3895 ULGs (82% of total ULGs) cityfinance as on 01-04-2024.

¹⁰² Based on analysis of self-reported property tax data for 2,768 ULGs from 16 states of Andhra Pradesh, Bihar, Himachal Pradesh, Jharkhand, Karnataka, Kerala, Maharashtra, Mizoram, Odisha, Punjab, Rajasthan, Tamil Nadu, Telangana, Tripura, Uttar Pradesh and Uttarakhand.

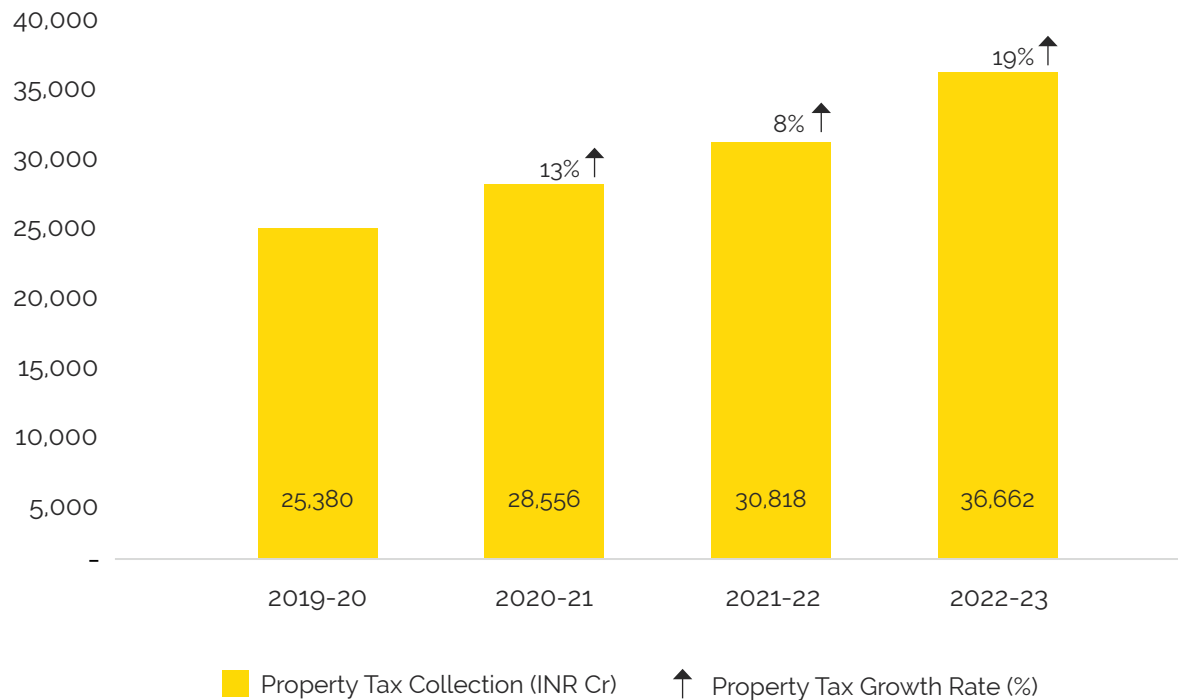


Figure 21: Property tax collection and collection growth rate trend (2019-2024)

However, this growth was uneven and revealed key design flaws. The use of state-level GSDP growth as the benchmark for ULG performance proved problematic due to the following factors:

1. GSDP aggregates reflect macroeconomic trends influenced by diverse sectors, many of which are disconnected from local government jurisdiction and performance. This makes GSDP growth rate a poor indicator for municipal revenue performance.
Moreover, ULGs in high-performing states like Maharashtra and Gujarat, which have significantly higher per capita property tax collections and benefit from high GSDP growth rates, face unrealistic expectations to sustain such high growth rates year after year.
2. When states experience high GSDP growth, smaller ULGs face unrealistic expectations to achieve comparable revenue growth rates. This challenge is particularly evident in fast-growing states like Telangana, where smaller ULGs struggle to match the state's rapid economic expansion through property tax collections alone.
3. Smaller ULGs, with limited administrative capacity and narrow tax bases, found it difficult to demonstrate consistent year-on-year revenue growth. They could not arbitrarily raise property tax rates, and gains from improved coverage or arrear recovery quickly plateaued.
Geographic constraints further compound these challenges. In hilly states like Himachal Pradesh, property tax growth is particularly difficult because limited land availability prevents new construction. Even where ULGs undertake systematic reforms, such as GIS mapping and

comprehensive property assessment, sustaining growth becomes challenging due to these structural limitations.

Hence, ULGs in smaller towns struggled to match GSDP growth rates, which are influenced by macroeconomic factors beyond their control. For instance, **among the 20% of ULGs that did not qualify for grants in FY 2023–24 (706 in number), 90% had populations below 100,000.** This suggests that the grant condition disproportionately affected small ULGs, even where sincere tax effort may have been made.

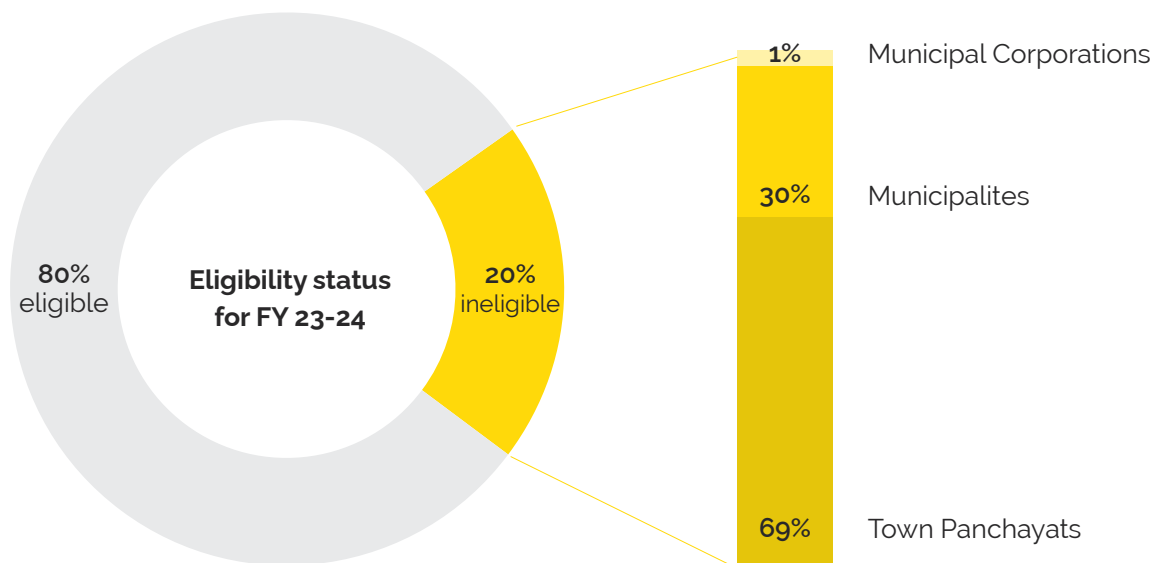


Figure 22: Percentage share of ULGs eligible for property tax condition for the year 2023-24

While property tax has understandably received significant policy attention over the past few Finance Commissions, it cannot be the sole pillar of municipal revenue. Continued over-reliance on property tax poses two risks: it creates pressure on a single instrument for revenue generation, and it overlooks the potential of other underutilised sources.

ULGs must expand their own-source revenues to include user charges for water supply, sewerage, and solid waste management — along with licence fees, development charges, and professional tax. These offer untapped potential and direct accountability links. Moreover, cost recovery through user charges is critical to sustain infrastructure created under programmes like AMRUT, SBM, and tied grants of Finance Commissions. Broad-based revenue diversification is therefore essential to enhance financial resilience, governance credibility, and service quality.

Recommendations for the XVI Finance Commission

1. **Discontinue the condition for notifying a floor rate for property tax.** In practice, floor rates did not ensure consistency, fairness, or significant gains in tax collection, as many states lacked a sound basis for setting them.
2. **Exclude ULGs with populations below 500,000 from the revenue growth condition altogether¹⁰³.** These ULGs typically lack the administrative and economic scale to meet aggressive revenue targets and should instead be supported through capacity-building and process reforms.
3. **For ULGs with populations above 500,000, expand the revenue growth condition to include all own-source revenues, not just property tax.** This should encompass user charges for services such as water supply, sewerage, and solid waste management; licence fees; building permit and development charges; advertisement tax or fees; and professional tax.

5.1.3 The Inconsistent Constitution of State Finance Commissions (SFCs) and Fragmented Implementation of Their Recommendations

The ineffectiveness of State Finance Commissions (SFCs) has been a long-standing institutional challenge. Union Finance Commissions (FCs) are mandated under Article 280 to recommend measures to augment municipal finances, based on SFC recommendations. However, inconsistency in the constitution and reporting of SFCs, and in the implementation of their recommendations, has severely undermined this process.

Successive FCs have sought to address this gap through different approaches. The XI FC recommended amendments to Article 243I to synchronise the publication of SFC reports with the deliberation timelines of FCs. It also urged states to publish Action Taken Reports (ATRs) alongside SFC reports, thereby improving coordination and transparency.

The XII FC addressed institutional continuity, suggesting the establishment of permanent SFC cells within states to ensure ongoing support and timely availability of data.

The XII FC focused on timely SFC constitution, quality reporting, and constitutional amendments to synchronise SFC and FC cycles. It proposed a standardised template for SFC reports and suggested forming similar bodies for states and areas not covered under Part IX of the Constitution. The XIV FC reinforced the need to strengthen SFC capacity and recommended proper institutional support, adequate resources, and timely legislative submission of reports with action-taken notes.

¹⁰³ This will lead to exclusion of 4,737 ULGs with population below 500,000, having limited capacity, from the revenue growth condition.

The XV FC noted that despite these repeated exhortations, many states continue to undermine the constitutional mandate of SFCs, with several having moved no further than their second or third SFC in over two decades. The Commission therefore chose to link local government grant releases directly to compliance with this core constitutional requirement.

Under this framework, **states were required to constitute a State Finance Commission, act on its recommendations, and lay an explanatory memorandum before the state legislature by 31 March 2024.** The XV FC further recommended that no local government grants be released to states failing to comply with these constitutional requirements after this date.

Linking SFC formation to grant eligibility under the XV FC drove progress, with 11 states constituting SFCs post-introduction of the condition. However, data regarding SFC notifications, constitutions, reports, action taken reports, and implementation status remains largely unavailable in the public domain.

Table 14: Impact of Mandatory Condition of SFC Constitution (Status as on March 2025)

Status	No. of States	States
Formed post-introduction of condition	11	Andhra Pradesh, Goa, Gujarat, Jharkhand, Karnataka, Punjab, Tripura, Uttar Pradesh, Uttarakhand, Telangana, Chhattisgarh
New SFC not yet constituted	2	Arunachal Pradesh, Manipur
Consistently constituting SFCs	11	Assam, Bihar, Himachal Pradesh, Kerala, Madhya Pradesh, Mizoram, Odisha, Rajasthan, Sikkim, Tamil Nadu, West Bengal

Note: Information on SFC formation is based on publicly available data as of March 2025. Meghalaya, Mizoram, and Nagaland are exempted from forming SFCs under the 73rd and 74th Constitutional Amendment Acts, 1992, though Nagaland constituted its first SFC in August 2008 and Mizoram in September 2011. Data on Maharashtra's current SFC status is unavailable. The remaining state accounts are included in the categories above.

While holding ULGs accountable for actions that fall entirely under state government jurisdiction, such as SFC constitution may not be ideal, SFCs remain crucial for addressing vertical and horizontal fiscal imbalances at the local government level through formula-based devolution. Moreover, both SFC operations and state implementation of their recommendations require greater public scrutiny to ensure better functioning of local governments.

▲ Recommendations for the XVI Finance Commission

1. Continue the requirement for timely SFC constitution to institutionalise this practice among state governments.
2. Mandate additional transparency measures to enhance public oversight of SFC operations and hold states accountable for implementing SFC recommendations, including:
 - i. Submitting Action Taken Reports (ATRs) to state legislatures within a stipulated period.
 - ii. Publishing notifications, Terms of Reference, SFC reports, ATRs, and annual implementation reports in the public domain.

5.14 New Conditions Introduced During the XV FC Term

The Department of Expenditure (DoE) introduced additional eligibility requirements focused on financial oversight and constitutional compliance during the XV FC period.

The first condition required states to submit certificates of unspent XIV FC grant balances. This was introduced to prevent fund parking at the ULG level. While well-intentioned, the condition resulted in delays in XV FC grant disbursement. Although no grants were ultimately withheld, the condition nevertheless created compliance burdens and delayed grant releases.

These issues can be better addressed through improved expenditure monitoring systems. System integration and digitised grant management platforms offer more effective solutions, as will be elaborated in Chapter 7 on Grant Administration.

This experience demonstrates that operational conditions not recommended by the Finance Commission can create implementation challenges. **The DoE should align any additional requirements with the broader framework and intent of FC recommendations to maintain consistency and support effective fiscal devolution.**

The second condition introduced by DoE was that only duly elected local governments would be eligible for XV FC grants. This, too, led to grant losses and release delays in some states where elected local governments were not in place. However, this is a welcome and necessary measure that reinforces the legitimacy and constitutional significance of elected local government. This condition highlighted a broader governance challenge: the latest data suggests that 61% of ULGs in major states have experienced delays in holding elections. Many ULGs in Maharashtra, Gujarat, and Telangana are functioning without elected representatives and consequently face grant delays or reductions. For instance, Bruhat Bengaluru Mahanagara Palike (BBMP), Karnataka's largest ULG, has

operated without an elected council for more than three years. These delays are often politically motivated, with state legislators reluctant to cede control over governance and municipal finances to elected local governments¹⁰⁴.

Recommendations for the XVI Finance Commission

1. **Discontinue the requirement for ULGs to declare unspent balances from previous Finance Commissions**, as such information can now be readily accessed through integrated digital systems. The design of an appropriate tracking mechanism will be discussed further in Chapter 7.
2. **Institutionalise the elected local government condition for grant eligibility**. This could incentivise states to adhere to constitutional mandates for regular local elections.

5.2 Summary of Recommendations: Minimum Eligibility Criteria for XVI FC Grant Disbursement

The XV FC marked a significant departure from previous Commissions by linking 100% of urban grants to clearly defined eligibility conditions. Despite initial concerns about this approach, evidence demonstrates that these conditions have strengthened the culture of reform, transparency, and compliance among ULGs.

Table 15: XV FC Eligibility Conditions to be Continued, Discontinued or Amended

Sl. No.	XV FC Condition	Impact	Recommendation (Keep/ Discontinue/ Amend)	Proposal/ Recommendation to XVI FC
1	Publication of provisional and audited annual accounts	As of January 2025, 96% of ULGs have complied with this requirement , publishing their audited financial statements on the CityFinance for the first time.	Keep + Expand	Mandate audited accounts be published by 31 October of the following year to eliminate the need for provisional accounts . Mandate online publication of approved budget by 31 May (18 states already mandate public disclosure).

¹⁰⁴ Deshpande, A. (2025, April 15). 'There is no hope': Debate over Bengaluru's missing local government resurfaces. Hindustan Times. Retrieved from <https://www.hindustantimes.com/cities/bengaluru-news/debate-over-bengaluru-s-missing-local-government-resurfaces-101744690009084.html>

Sl. No.	XV FC Condition	Impact	Recommendation (Keep/ Discontinue/ Amend)	Proposal/ Recommendation to XVI FC
2	Mandatory reporting on 28 SLBs for Million-Plus Cities	100% of MPCs published data by 2022-23 and demonstrated significant improvements: 81% improved water supply coverage; 67% increased wastewater network coverage; 98% reduced non-revenue water. On average, 90% of NMPCs voluntarily reported SLBs.	Amend	Mandate publication of SLBs for all ULGs on CityFinance Incentivise strengthening of processes and systems for performance/SLB reporting
3	Notification of floor rate for property tax	22 states met the condition to notify minimum property tax rates.	Discontinue	Discontinue this condition. The ambiguous terminology of 'floor rate' did not result in meaningful reforms, consistency, or fairness in tax collection. Many states lacked a sound basis for rate-setting.
4	Annual growth in property tax collection matching state's GSDP growth	For 2023-24, 80% of ULGs from 16 states qualified for the grant condition. More than 90% of disqualified ULGs had populations below 100,000.	Amend	Expand scope to include all own-source revenues with a target of 7.5% annual growth; exclude ULGs with populations below 500,000.
5	Constitution of SFC, implementation of recommendations, and laying of the ATR before the legislature	11 states constituted SFCs during the XV FC term.	Continue + Expand	Continue requirement for timely SFC constitution and mandate enhanced transparency measures: - Publication of Terms of Reference, reports, and ATRs - Annual reports on implementation of SFC recommendations.

Sl. No.	XV FC Condition	Impact	Recommendation (Keep/ Discontinue/ Amend)	Proposal/ Recommendation to XVI FC
6	Grant eligibility limited to duly elected ULGs	61% of ULGs in major states have experienced delays in holding elections.	Continue	Continue the condition. This condition is fundamental to democratic local governance. It incentivises states to adhere to constitutional requirements for regular elections.
7	Certificate requirement for unspent XIV FC grant balances to access XV FC grants	Condition created compliance burdens and delayed XV FC grant releases. No grants were ultimately withheld on this basis.	Discontinue	Discontinue this requirement and track grant utilisation through digital grant management systems.

In light of this **demonstrable success**, it is strongly recommended that the **XVI FC retain and institutionalise the eligibility condition framework to advance key municipal finance reforms for financial discipline and transparency**. Doing so will not only preserve and deepen the reform gains achieved under the XV FC, but also promote a culture of proactive disclosure, compliance, and accountability among states and ULGs. Drawing from the XV FC experience with conditionalities for grant eligibility, we propose a refined set of minimum eligibility criteria for the XVI FC. These criteria aim to build on the progress made under the XV FC period while addressing observed gaps and ensuring timely grant transfer to ULGs.

To facilitate timely disbursement, compliances are spread across two instalments: the first instalment by 31 May and the second by 31 October. These proposed conditions align with existing processes and do not impose additional compliance burdens on ULGs. Instead, they promote basic standards of transparency, financial discipline, and data availability in urban governance.

Table 16: Mandatory Eligibility Conditions for All ULGs to Access XVI FC Urban Grants

For claiming first instalment (preferably by 31 May)	
1.	Public disclosure of annual budget, approved by the council, on CityFinance.
2.	Annual availability (as relevant) of the applicable notification of SFC constitution, SFC report, action taken report, and yearly implementation report, without extending SFC recommendations beyond the original term.
For claiming second instalment (preferably by 31 October)	
1.	Public disclosure of audited accounts of the previous year on CityFinance, preferably in machine-readable format, including: • Auditor's report • Balance sheet • Income and expenditure statement • Cash flow statement • Receipts and payments statement • Schedules to balance sheet, income and expenditure statement • Significant accounting policies
	• From third year onwards, grant disbursement to ULGs would be linked to public disclosure of audited accounts as per revised NMAM and adherence to government accounting standards.
2.	Public disclosure of Service Level Benchmarks (SLBs), on CityFinance.
<i>Only duly elected ULGs shall be eligible for the grants.</i>	

These minimum eligibility conditions provide a foundation for continued reform while ensuring timely grant transfers and reducing administrative complexity.

The next section extends the discussion on grant architecture under the XVI FC by addressing the heterogeneity of ULGs and proposing a grant structure tailored to their institutional capacity and economic potential.

06

Differentiated Grant Architecture for ULGs



This chapter addresses the core question of urban grant architecture under the XVI Finance Commission (FC): the distribution of grants among Urban Local Governments (ULGs) within states based on their varying typologies and capacities. The analysis examines two dimensions: population-based classification of ULGs, and the types of grants best suited to enable meaningful urban outcomes. The chapter proposes a differentiated grant architecture that accounts for these disparities, builds on historical lessons, and addresses contemporary urban governance challenges.

Overview and Approach

In the previous chapter, we detailed minimum eligibility conditions applicable to all ULGs, regardless of size or typology. These conditions focus on transparency, accountability, and financial discipline, and serve as a critical foundation for effective public expenditure across municipal governments.

Building on this foundation, this chapter develops and recommends a differentiated approach to grant design for the XVI FC. Given the Finance Commission's constitutionally defined tenure and the non-revisable nature of its recommendations, the proposed architecture must be both evidence-based and implementable. The framework ensures that ULGs not only receive grants but are equipped to utilise them effectively.

6.1 A Differentiated Approach to Grant Architecture

The XV FC's differentiated approach marked a welcome departure from the 'one size fits all' model, recognising that ULGs vary widely in their institutional capacities, economic potential, and growth trajectories. Previous chapters examined the evolution of urban grant architecture through three dimensions: the types of grants, their intended end-use, and conditionalities for accessing them. Drawing from these insights and lessons, the XVI FC must advance this differentiated approach by refining ULG classification and aligning grant architecture to ULG population size.

We recommend that ULGs be grouped into **three categories based on population size**:

Category I: Small Cities (Population below 500,000)

Category II: Large and Medium Cities (Population between 500,000 and 4 million)

Category III: Metros (Population above 4 million)

These categories reflect differences in economic and revenue-generating potential along with institutional and administrative capacities. The differentiated approach enables tailored grant structures that calibrate the type, purpose, and conditionality of grants to match city contexts. The framework ensures that ULGs with greater economic potential are incentivised to higher performance standards, while smaller ULGs are equipped to deliver services.

6.1.1 Rationale for Differentiated Grant Architecture

The recommendation for differentiating grant architecture across three population categories rests on three interrelated premises:

1. Cities must be recognised as economic drivers

India's economic trajectory is closely linked to urbanisation. Urban areas contributed 51.7% to the country's GDP in 1999–2000, rising to 62% by 2009–10 (HPEC, 2011), and projected to exceed 70% by 2030¹⁰⁵.

Despite this economic significance, ULGs continue to be treated as implementation arms of union and state schemes rather than autonomous economic actors. This pattern is evident across states: a CAG audit found that no state among 18 examined has effectively devolved the function of 'Planning for Economic or Social Development,' with 16 states offering ULGs minimal role in economic planning¹⁰⁶. While functions such as land-use regulation and building permissions have been delegated to ULGs in many states, the broader policy and regulatory environment remains shaped by union and state governments.

In the absence of a clear city-level economic vision, these delegated functions are implemented in isolation, without alignment to broader economic goals. As the Asian Development Bank (2024) highlights, this results in fragmented urban growth, where city master plans focus narrowly on spatial and zoning regulations, with little guidance for infrastructure investment that could catalyse productivity and employment.

Without economic planning, the benefits of urbanisation remain constrained. Globally, a 1% increase in urbanisation is associated with a 3.9% increase in per capita GDP¹⁰⁷. In India, this is only 1.7%¹⁰⁸. This underperformance stems from the limited fiscal and strategic autonomy of ULGs. Grant

¹⁰⁵ McKinsey Global Institute. (2010, April). India's urban awakening: Building inclusive cities, sustaining economic growth. McKinsey & Company

¹⁰⁶ Comptroller and Auditor General of India. (2024). Compendium of Performance Audits on the Implementation of the 74th Constitutional Amendment Act, 1992 (Volume I). Author. <https://cag.gov.in/uploads/StudyReports/SR-Compendium-067346fdd7000e9-76046538.pdf>

¹⁰⁷ World Resources Institute. (2021). The State of the Cities Report.

¹⁰⁸ Ibid.

architecture must therefore shift from uniformity to empowering cities based on their economic potential.

While the XV FC introduced differentiated grants for Million-Plus Cities and Non-Million-Plus Cities, these focused on service delivery rather than economic growth. The XVI FC must go further and must position cities as drivers of national growth.

2. Grant architecture must account for varying revenue-generating capacity

While addressing the vertical fiscal gap is important, it is equally crucial to recognise the horizontal disparities in the capacity of ULGs to raise revenue. Some cities, particularly metropolitan areas, possess inherent advantages due to historical and geographical factors. They typically have broader tax bases, more mature institutions, and greater administrative capacity, enabling them to mobilise significantly higher levels of own-source revenue (OSR) and implement reforms more effectively.

As a result, the grant financing needs of metro cities are fundamentally different from those of smaller ULGs. With adequate fiscal decentralisation, metro cities may generate significant revenues for managing not only operational expenditure but part of their capital expenditure as well.

In contrast, smaller ULGs are fiscally weaker, understaffed, and often dependent on fiscal transfers from union and state governments. The following table illustrates this stark disparity by analysing the revenue-generating capacity of different typologies of ULGs, using three parameters: per capita total revenue, per capita own source revenue, and per capita property tax.

Table 17: Per Capita Analysis Based on Audited Financial Statements of 3,803 ULGs for 2021-22

City Population Category	Type	Number of ULGs	Urban Population (%)	Per Capita Revenue (INR)	Per Capita Own-Source Revenue (INR)	Per Capita Property Tax (INR)
>4 M	Metro Cities	7	15	15,542	10,987	2,060
1-4 M	Large & Medium Cities	36	17	7,817	5,073	1,830
500k-1 M		44	9	4,117	1,633	501
100K-500K	Small Cities	377	23	3,324	1,245	451
<100k		4,360	36	2,966	862	280
Total		4,824	100			

Note: The per capita analysis is based on audited financial statements available for 3,803 ULGs for FY 2021-22. The population category-wise numbers shown in the table reflect the total number of ULGs (4,824). The difference arises because audited accounts were not available for all ULGs; therefore, the per capita analysis uses the subset of ULGs with complete data.

The analysis reveals stark disparities across ULG population categories, with three key findings:

- i. ULGs with populations above 4 million raise over ₹10,000 in per capita OSR, while ULGs with populations below 500,000 raise barely ₹1,000–1,600, a tenfold gap. Even large ULGs in the 1–4 million population range mobilise only half the per capita OSR of metros.
- ii. The share of OSR in total revenue declines sharply with ULG size: 71% in metros, 60% in cities with populations between 500,000 and 4 million, and only 33% in smaller towns. This low revenue-generating capacity makes smaller ULGs far more dependent on fiscal transfers. (refer to Annexure 6.1)
- iii. On average, the per capita property tax in ULGs with populations below 500,000 is only one-sixth that in ULGs with populations above 4 million. Land values and assessment rates in small towns are much lower, leading to poor yields.

This substantial gap in revenue-raising capacity means that smaller ULGs with populations below 500,000 cannot generate the same per capita revenue as ULGs with populations above 4 million, even with comparable effort.

3. The grant architecture must reflect administrative and institutional capacity as well as accountability for performance

Administrative capacity of ULGs varies widely based on population category. ULGs with populations above 500,000 typically have dedicated departments for town planning, engineering, sanitation, finance, and IT systems.

In contrast, smaller ULGs struggle with chronic understaffing. Data from across the country reveals that while about 35% of sanctioned posts are vacant in large municipal corporations, this figure increases to 41% in municipalities and 58% in town panchayats, which mostly have populations below 500,000¹⁰⁹. Many small-town administrations operate with skeletal staff and often lack qualified town planners, accountants, engineers, or IT professionals. Field visits revealed that several smaller ULGs do not have even a full-time municipal commissioner or technical officer to oversee infrastructure works or service delivery reforms¹¹⁰.

These capacity constraints affect not only the utilisation of grants but also the ability to comply with conditionalities, monitor outcomes, and submit timely utilisation reports. Consequently, uniform performance-based grants may inadvertently penalise smaller ULGs that lack institutional scaffolding, leading to underutilisation or poor absorption of funds. Hence, we propose that larger ULGs should be held accountable to performance while smaller ULGs should be supported with capacity building.

¹⁰⁹ Janaagraha Centre for Citizenship and Democracy. (2023). Annual Survey of India's City-Systems 2023 (ASICS 2023).

¹¹⁰ Based on field visits to select ULGs Shamshabad Municipality and Pedda Amberpett Town Panchayat in Telangana and Madhusudangarh Town Panchayat in Madhya Pradesh.

6.2 Category-wise Type of Grants

For the XVI FC's grant architecture, we propose a differentiated approach based on size and capacity. This ensures that larger ULGs are incentivised to perform, while smaller ULGs receive predictable, untied support for essential services. ULGs will receive a mix of basic, output-linked, and outcome-based grants tailored to their population category, as depicted in Figure 23 and detailed in Table 18.

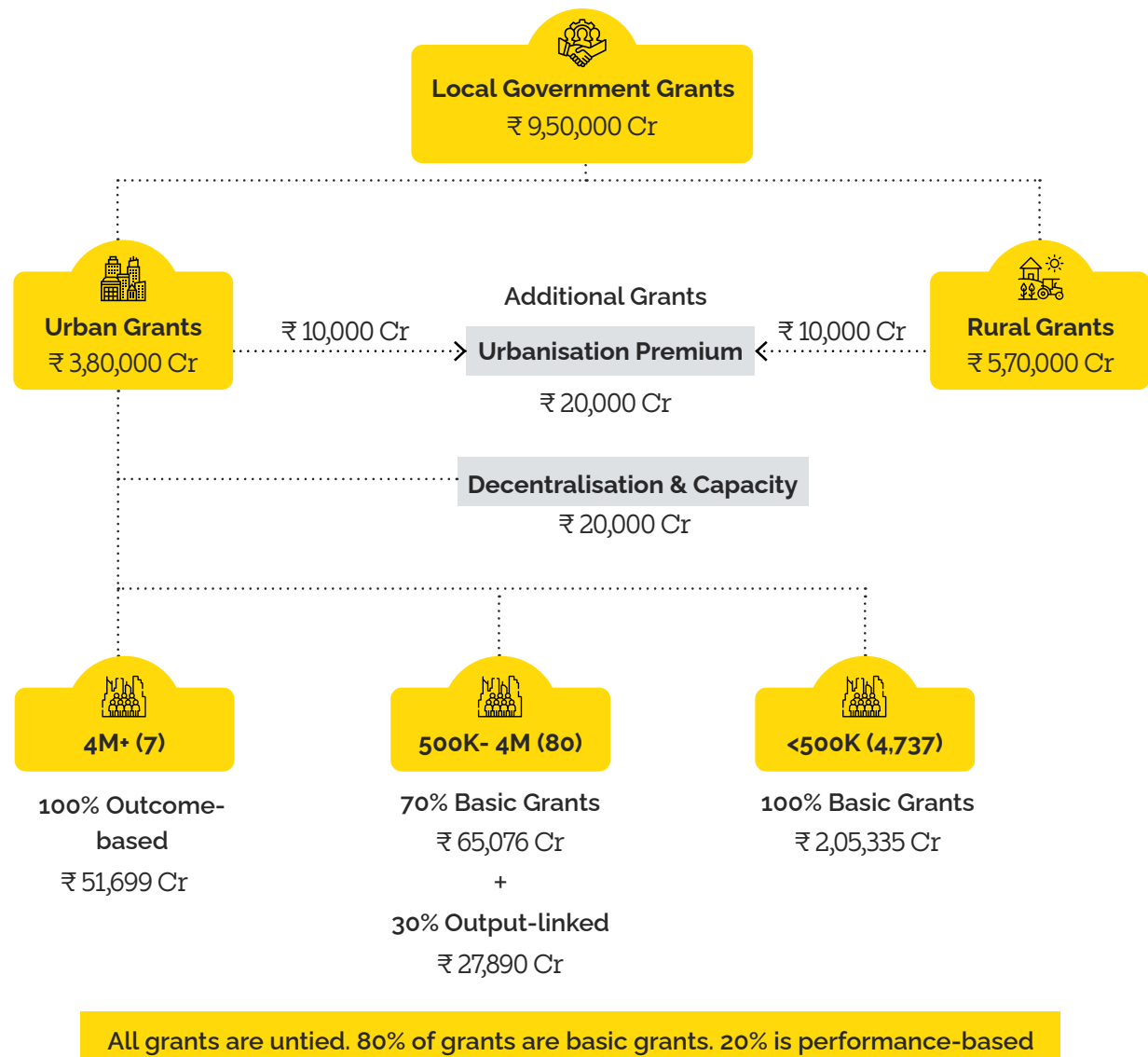


Figure 23: Recommended grant architecture for the XVI FC

Table 18: Key Components of Proposed Grant Architecture for the XVI FC

Key Components			
Population Categories	ULGs <500K population	ULGs 500K–4 million population	ULGs >4 million population
Type of Grant	100% basic grants	70% basic grants 30% output-based grants	100% outcome-based grants
Method of Allocation	Proportional to each ULG's share of the state's total urban population , ensuring uniform per capita allocation across all population categories.		
Quantum (INR crore)	₹ 2,05,335 Cr	₹ 92,966 Cr (65,076 basic + 27,890 output-linked)	₹ 51,699 Cr
End Use	100% untied grants. ULGs have complete discretion to allocate funds across the 18 functions of the Twelfth Schedule.		
Performance Linkage	None beyond basic eligibility compliance.	30% of allocation linked to measurable outputs and reforms.	100% of allocation linked to achievement of pre-defined outcomes and reforms.

Irrespective of population category, we recommend that **100% of ULG grants should be untied** (a detailed analysis on the effectiveness of tied and untied grants is discussed in Chapter 4, Section 4.4.1). ULGs should have the autonomy to align expenditures with local priorities, based on a City Action Plan (CAP) or an Annual Action Plan. Performance incentives for larger ULGs can still be introduced through a separate, differentiated framework, particularly for those with higher capacity and reform readiness. Further, to ensure effective utilisation of FC grants, critical enablers such as the Decentralisation and Capacities grant, initiatives such as Capital Investment Plans (CIP) and CAP, and improvements in grant administration and reporting, are being proposed.

The proposed allocation structure ensures that 80% of the total grant pool is allocated as basic grants, linked only to basic eligibility conditions (discussed in Chapter 5). This aims to provide financial stability to the majority of ULGs. **Only 20% of the grant pool is performance-based¹¹¹** and targeted primarily at 87 large ULGs with the capacity to undertake reforms (refer to Annexures 6.2 and 6.3 for a list of ULGs). **If the performance-linked grants remain unclaimed, they should be redistributed among ULGs with populations below 500,000, providing an additional layer of financial support.**

Further, within each state, the inter-city allocation of grants to individual ULGs should be proportional to their share of the state's total urban population. This ensures uniform per capita

¹¹¹ 30% of grants for ULGs with population between 500,000 and 4 million linked to outputs and 100% of grants linked to outcomes for 7 ULGs with above 4 million population.

grant allocation while allowing variation in grant type and conditionalities, based on ULG capacity and size.

We have also proposed **two additional grants**. The **Urbanisation Premium** will support urbanising rural areas and encourage states to adopt rural-to-urban transition policies (as discussed in Chapter 2), while the **Decentralisation and Capacities Grant** will help all ULGs, except those with populations above 4 million, to build the systems and staffing needed to use FC grants effectively (discussed in Section 6.3.2).

Unlike sector-specific grants (health, air quality etc) that were introduced by the XV FC, these additional grants will focus on developing infrastructure in transitioning areas and strengthening ULGs by enabling them to plan, deliver, and govern more effectively through targeted capacity-building support.

6.2.1 Grants for Category I ULGs (Small Cities with Population Below 500,000)

India's small cities with population below 500,000 represent the most neglected segment in the urban hierarchy. Though they account for 4,737 of India's ULGs and house nearly 59% of the country's total urban population, these cities have been consistently underrepresented in national urban missions such as AMRUT, Smart Cities, and Metro Rail programmes. They contend with limited financial capacity, weak institutional frameworks, and minimal capital investment planning or professional staffing.

Many of these small ULGs struggle to provide basic services and infrastructure. In most cases, their only capital expenditure is funded by higher tiers of government through FC grants and Centrally Sponsored Schemes (CSS). CSS, with strict guidelines and limitations, often adopt a 'one size fits all' approach irrespective of ULG size or region. Tying grants to performance or end use in such ULGs prohibits them from responding to local needs and often results in funds going unutilised, exacerbating existing inequities. This is evident from utilisation data of XV FC tied grants for Non-Million-Plus Cities (NMPCs) (discussed in Chapter 4, Section 4.4.1.2).

The XV FC mandated that 60% of urban grants be tied to sectors, even for small ULGs. An analysis of 2,056 Detailed Utilisation Reports for XV FC tied grants in 2023-24 (as reported on CityFinance) shows that ULGs with populations below 500,000 have a utilisation rate of 25% compared to 54% for ULGs with populations above 500,000. In Telangana, utilisation data for 140 ULGs between 2021-22 and 2023-24 shows a 54% utilisation rate for tied grants, compared to 77% for untied grants (refer to Annexure 4.20).

Drawing insights from this experience, we recommend that **all Category I ULGs receive 100% basic untied grants, with no output- or outcome-based conditions.** ULGs should have the autonomy to prioritise spending according to local needs across the 18 functions in the Twelfth Schedule of the Constitution. Ideally, **spending priorities should be determined through a bottom-up consultative planning process, capturing project details in a City Action Plan or Annual Action Plan, similar to the rural counterpart – Gram Panchayat Development Plan.**

Box 5: Learnings from Gram Panchayat Development Plans

The launch of the Gram Panchayat Development Plan (GPDP) in 2015-16 by the Ministry of Panchayati Raj, Government of India, initiated a nationwide effort to institutionalise participatory planning at the grassroots level. Gram Panchayats (GPs) were encouraged to undertake local-level planning under the People's Planning Programme, and were supported by a substantial allocation of ₹2 lakh crore under the XIV FC as well as significant resources through Mahatma Gandhi National Rural Employment Guarantee Scheme (MGNREGS).

The GPDP process promotes convergence across schemes such as MGNREGS, Swachh Bharat Mission (SBM), National Rural Livelihoods Mission (NRLM), and health and education missions. States, including Kerala, Maharashtra, and West Bengal, have demonstrated improvements in service delivery, notably in sanitation, rural infrastructure, and livelihood programmes through this process.

Over 95% of GPs now prepare GPDPs annually, with more than 2.56 lakh plans uploaded on the e-Gram Swaraj portal for 2021-22, signalling near-universal coverage¹¹².

A key milestone in this process was the integration of Village Poverty Reduction Plans, prepared by Self Help Groups under the NRLM, into the GPDP framework. This convergence helped align community aspirations with resource allocation, leading to more grounded and responsive planning. Over the last ten years, GPDP implementation has revealed its transformative potential in deepening participatory governance across India—from bamboo bridges in flood-prone Assam and rainwater harvesting in drought-affected Jharkhand to sanitation drives in Goa. GPDP's progress proves that locally driven plans produce targeted and effective interventions¹¹³.

¹¹² Ministry of Panchayati Raj. (2021). People's Plan Campaign: Sabki Yojana Sabka Vikas (2021-22): A handbook for frontline workers. Government of India. Retrieved from http://gdpd.nic.in/PPC/resources/PPC-2021_Booklet.pdf

¹¹³ The Economic Times. (2016, July 29). How Gram Panchayat Development Plan is changing the villages of India. Retrieved from <https://economictimes.indiatimes.com/news/politics-and-nation/how-gram-panchayat-development-plan-is-changing-the-villages-of-india/articleshow/53458749.cms>

City Action Plans in Practice: The Assam Experience

As part of its urban governance reform agenda, the Government of Assam is institutionalising City Action Plans (CAPs) as a key tool for city-level planning and accountability. These bottom-up, participatory plans identify and address local urban challenges through structured community engagement and city-wide consolidation. A leading example is the state's flagship initiative, Doh Shafer Ek Rupayan (Ten Cities, One Vision), spearheaded by the Department of Housing and Urban Affairs (DoHUA).

Implemented in ten ULGs outside Assam's capital region, Doh Shafer Ek Rupayan adopts a place-based, citizen-driven approach to improving urban quality of life, offering a replicable framework for future urban policy and planning. At its core, the initiative integrates City Action Plans as operational tools, anchoring local development in participatory diagnostics and targeted interventions.

Doh Shafer Ek Rupayan is structured around seven core components — solid waste management, safe drinking water, public infrastructure, blue-green infrastructure, traffic management, street lighting, and urban planning — which address key service delivery and infrastructure gaps. These are supported by three enabling levers: human resources, rationalisation, digital and online service delivery, and financial strengthening of ULGs.

By embedding City Action Plans within Doh Shafer Ek Rupayan, Assam is pioneering a shift from scheme-bound urban reforms to institutionalised, locally tailored planning processes. This model offers important lessons for other states aiming to embed participatory planning into urban governance systems.

We recommend allocating 59% of total urban grants (estimated to be ₹2,05,335 crore) to Category I ULGs over the five-year award period. Individual ULGs would receive grants based on their population share within their respective state's urban population. This keeps the formula simple and easily understandable by all stakeholders.

These grants will be disbursed only to duly elected ULGs who meet the basic eligibility conditions (as defined in Chapter 5). However, once this eligibility is met, **no further conditions will apply** to grant usage.

6.2.2 Grants for Category II ULGs (Large and Medium Cities with Population between 500,000 and 4 million)

India is home to approximately 80 ULGs with populations between 500,000 and 4 million. These medium to large-sized ULGs serve as critical economic and administrative regional hubs across states. They provide viable alternatives to metropolitan centres struggling with challenges such as flooding, congestion, high housing and living costs, and poor solid waste management. Emerging cities like Visakhapatnam, Coimbatore, Vadodara, Jaipur, and Kochi are increasingly attracting investment and skilled workers, while staying ahead in innovation. A 2022 CBRE report noted that Tier 2 cities provide a 10–35% cost advantage compared to their metropolitan counterparts¹¹⁴, while also offering their citizens improved infrastructure and a better quality of life.

Despite their growing importance, most of these ULGs continue to exhibit limited fiscal capacity and moderate economic output. They often represent a transition zone — significant enough to drive regional growth, yet requiring targeted support to unlock this potential. To unlock this potential, these ULGs require both foundational support and targeted performance incentives. Hence, we propose a grant design that combines basic assured financial support with performance grants linked to outputs that contribute to economic growth. We are cognisant that the performance grant amount should be substantial enough for ULGs to prioritise performance, yet not so large as to overshadow basic grants¹¹⁵. **Given that these 80 ULGs (refer to Annexure 6.3 for the list of ULGs) account for 26% of the population in statutory towns, we recommend allocating 26% of ULGs grant to them (estimated to be ₹92,966 crores). Of this:**

1. **70% of the grant will be basic in nature** and can be used by ULGs for any purpose except salaries and establishment costs. ULGs will be eligible to receive this basic grant upon fulfilling the mandatory eligibility conditions outlined in Chapter 5. Basic grants will be disbursed in two instalments in **May and October each year**.
2. **30% of the grant will be output-linked**, connected to measurable reforms and milestones in four areas: Own Source Revenue (OSR), public land inventory, Capital Investment Planning (CIP), and publication of economic data. **ULGs will be eligible for this portion only upon meeting additional performance conditions.** Output-linked grant will be **disbursed as a single instalment in October each year**, following verification that the ULG has met the specified conditions outlined in Table 20.

¹¹⁴ Ghatak, K. (2023, March 14). Exploring the shift: GCCs moving to Tier-2 cities for cost and talent advantages. EY India. https://www.ey.com/en_in/insights/consulting/exploring-the-shift-gccs-moving-to-tier-2-cities-for-cost-and-talent-advantages

¹¹⁵ The per capita grant allocation of ₹11,045 was used to estimate annual grant entitlements for ULGs with populations between 500,000 and 4 million. To contextualize this quantum relative to their municipal revenues, we analysed budget data for 42 ULGs (out of a total of 80 cities in this population category) for FY 2021–22, sourced from CityFinance. The share of the estimated annual grant was then calculated as a percentage of each ULG's total annual budget size. On average, the projected grant accounts for 13% of a ULG's annual budget.

6.2.2.1 Performance Conditions Under Output-linked Grants for Category II

We recommend that the 80 ULGs in Category II receive performance-based grants of ₹27,890 crore over five years, contingent on four output-linked conditions that assess quality of governance and developmental foresight. These conditions aim to augment own revenue generation and unlock land assets, creating an enabling environment for market financing. Enhanced revenues can, in turn, finance urban infrastructure resulting in improved quality of life and ease of doing business. This strengthens public trust and tax compliance, initiating a virtuous cycle of better urban governance.

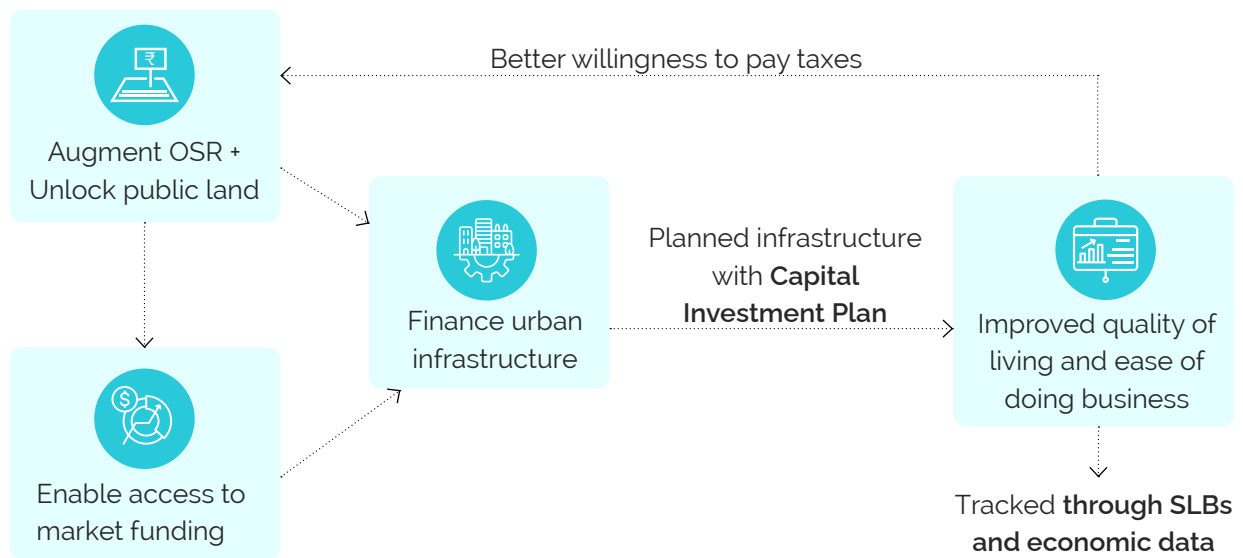


Figure 24: Urban reform cycle under Category II grants

1. Annual Increase in Own Source Revenue (OSR)

A ULG's capacity to generate and grow its Own Source Revenue (OSR) determines its fiscal sustainability. In the absence of own revenues, ULGs remain heavily dependent on grants and cannot exercise meaningful fiscal autonomy. This dependency not only limits their ability to invest in infrastructure and services but also constrains their capacity to attract private or multilateral financing. A ULG's OSR, therefore, goes beyond municipal finance — it serves as a proxy for assessing quality of governance, administrative effectiveness, and institutional maturity.

India's urban revenue performance, however, remains weak by global standards. In OECD countries, property tax collections average 1.1% of the GDP but in India, this figure stands at 0.2% — one-sixth the benchmark¹¹⁶. India's total municipal revenues amount to just 0.4% of the country's

¹¹⁶ Awasthi, R., & Nagarajan, M. (2020). Property taxation in India: Issues impacting revenue performance and suggestions for reform (World Bank Working Paper No. 852151587668989296). The World Bank. <https://documents1.worldbank.org/curated/en/852151587668989296/pdf/Property-Taxation-in-India-Issues-Impacting-Revenue-Performance-and-Suggestions-for-Reform.pdf>

GDP, while in countries like South Africa and Brazil, ULGs mobilise 6% and 7.4% of the GDP from own sources alone — a stark contrast that underscores the country's fiscal dependency¹¹⁷. As per our analysis of audited financial data from CityFinance, the share of OSR of large and medium ULGs was ~60%. While FC grants made up 10% of total ULG revenue receipts in 2017–18, they were equivalent to a substantial 23.5% of ULGs' OSR in the same year¹¹⁸. This represents a sharp increase from 2010–11, when FC grants accounted for less than 10% of OSR¹¹⁹. This increasing share indicates that union government grants are increasingly compensating for stagnant municipal revenues, rather than supplementing a growing local revenue base — an unsustainable fiscal trend for urban governance.

To address this, **we propose ULGs demonstrate a minimum annual OSR growth of 7.5% in each financial year to qualify for the grant.** This target has been informed by an analysis of 46 ULGs across the country, covering the years 2019–20 to 2021–22. The analysis (refer to Annexure 6.4) revealed that while several ULGs have already achieved double-digit OSR growth, others have struggled with stagnation or decline. Setting a uniform, yet attainable, benchmark of 7.5% ensures that underperforming ULGs are encouraged to improve, while stronger performers continue to be incentivised. To ensure clarity and consistency, OSR components for this grant will be defined in alignment with the National Municipal Accounting Manual (NMAM). Only recurring and stable revenue heads that reflect true municipal fiscal effort will be included. These cover:

- i. Property tax, including current demand and excluding arrears
- ii. User charges for services such as water supply, sewerage, and solid waste management
- iii. Licence fees
- iv. Building permit and development charges
- v. Advertisement tax or fees
- vi. Professional tax, where collected and retained by the ULG.

One-off or non-recurring revenue items will be excluded, as they do not provide a stable base for performance assessment. These include sale or hire charges, land sales, rent from assets, interest income, and fines or penalties. Similarly, all forms of grants, tied or untied, will be excluded to ensure growth truly reflects own revenue mobilisation. Compliance with the 7.5% OSR growth requirement will be evaluated through annual growth rate reports submitted by ULGs and certified by the Municipal Commissioner. These reports must include supporting evidence from the Demand, Collection, and Balance (DCB) registers of ULGs. A data entry module can be integrated into the CityFinance grant management system to facilitate standardised reporting, including structured fields for each OSR component and provision for uploading relevant DCB extracts as supporting documentation.

¹¹⁷ Panwar, T. S. (2024, January 12). Give India's cities their due. Deccan Herald. <https://www.deccanherald.com/opinion/himalayas-municipalities-funds-cities-finance-commission-property-tax-gst-2845956>

¹¹⁸ Ramanujam, S. R. (2024, December 16). Fiscal Transfers to Cities: Designing Principles for the Future. Paper presented at the Workshop on 'Urban Finances - Issues before Sixteenth Finance Commission' Joint workshop by Sixteenth Finance Commission and Asian Development Bank, New Delhi

¹¹⁹ Ibid.

The DCB register is recommended as the primary source of data over Audited Financial Statements (AFS) or budget documents for several reasons. First, the DCB operates on a cash basis and is typically finalised by the end of the financial year, allowing for timely and consistent assessment. In contrast, budget documents vary widely in format and nomenclature across states and ULGs, making comparisons across ULGs. Moreover, budget documents generally provide actuals that are two years old, limiting their relevance for current-year grant assessment. Similarly, while AFS are more standardised, they are prepared on an accrual basis, making them unsuitable for output-linked grant disbursement.

Output:

- a. Verified year-on-year OSR growth of 7.5% from Year 1 to Year 5. If a ULG fails to meet the 7.5% target in a year but achieves a cumulative growth rate equivalent to 7.5% CAGR over two years, it should be eligible for the grant for the previous year as well.

2. Public Inventory of Urban Land Assets

Public lands are among the most valuable assets held by governments, especially in urban areas. Yet, they are often underutilised, encroached upon, or misappropriated without due process due to the absence of clear records.

A comprehensive, digitised land inventory would enable ULGs to proactively identify surplus or underused parcels, align land use with infrastructure priorities, and unlock economic value through lease, sale, or development. It would also allow ULGs to treat land as a strategic asset rather than a neglected resource. This can generate substantial revenue for ULGs, reducing dependence on state and union transfers and supporting much-needed investment in infrastructure and public services¹²⁰. Research demonstrates that developing public lands could also raise property values considerably, further enhancing this revenue potential. However, most ULGs lack clear records or valuation frameworks for land held by state departments, parastatals, and the ULG itself¹²¹.

Beyond fiscal gains, such inventories also promote efficient use of land. Without accurate records, ULGs cannot effectively plan for housing, transport, or public amenities, often leading to fragmented development, poor land utilisation, and missed investment opportunities. A public inventory provides urban planners with visibility into land availability and suitability, supporting compact and sustainable urban growth¹²².

¹²⁰ Confederation of Indian Industry (CII). (n.d.). Managing publicly held land as an asset and for public interest. CII Blog. Retrieved from <https://ciiblog.in/managing-publicly-held-land-as-an-asset-and-for-public-interest/>

¹²¹ Smart Growth America. (2024, August 7). New paper: Unlocking the potential of public lands in Richmond, Virginia. Smart Growth America. Retrieved from <https://www.smartgrowthamerica.org/knowledge-hub/news/new-paper-unlocking-the-potential-of-public-lands-in-richmond-virginia/>

¹²² Jha, D., Dubey, M., & Goswami, A. (2023). Urban land and property record systems in India: The case and agenda for reform (Policy Brief). Indian Institute for Human Settlements. <https://doi.org/10.24943/ULPRSICAR11.2023>

Given these compelling benefits, we recommend that ULGs be mandated to develop and publish an inventory of public land assets by Year 2, including land held by the ULG, state agencies, and parastatals. By Year 3, the inventory should be updated with market valuations for key parcels to enable evidence-based planning and monetisation.

Although the process will be led by ULGs, they must coordinate with the State Town and Country Planning Department. Parastatal agencies such as Development Authorities, State Housing Boards, and Metro Rail Corporations must actively disclose their landholdings.

Output:

- a. Inventory of public land assets published by Year 2.
- b. Market valuation completed and updated by Year 3.

3. Capital Investment Plan (CIP)

Most infrastructure projects in ULGs today are implemented in a fragmented, reactive, and short-term manner. This issue is particularly acute in medium and large-sized ULGs, where rapid and largely unplanned expansion of urban areas has created a pressing need for new infrastructure and services. ULGs face growing demands to invest in physical and social infrastructure that supports economic development and basic service delivery. However, these investments often require capital that far exceeds their limited financial resources¹²³.

Medium and large-sized ULGs are routinely forced to make difficult choices within highly constrained budgets. It is therefore crucial that they strengthen their financial planning and project prioritisation capacities. In the absence of structured capital planning, many infrastructure assets, such as Sewage Treatment Plants (STPs), remain underutilised or become non-functional due to the lack of sufficient funds for operations and maintenance. This highlights the necessity of embedding a formal, forward-looking investment planning framework within municipal systems¹²⁴.

In this context, a Capital Investment Plan (CIP) serves as a vital tool. CIP¹²⁵ is a multi-year framework that enables ULGs to schedule and financially plan their infrastructure investments in alignment with their strategic vision, service delivery goals, and fiscal realities. It focuses on identifying and prioritising capital projects based on service delivery needs, available financial resources, and operational capacity. This framework provides a practical mechanism for connecting a city's development objectives with its budgeting and execution capabilities, and is designed to complement, not replace, existing spatial planning processes.

¹²³ Center for Water and Sanitation, CEPT University. (2021, August). City sanitation investment plan for Wai Municipal Council. Accessed from https://pas.org.in/Portal/document/UrbanSanitation/uploads/City_Sanitation_Investment_Plan_for_Wai.pdf

¹²⁴ Ibid

¹²⁵ CIP is distinct from statutory planning processes such as Master Plans or the functions of urban development authorities. While Master Plans primarily focus on land use zoning and spatial growth regulations, typically led by state-level town and country planning departments or development authorities, a CIP is a multi-year financial and investment planning tool that aligns capital projects with a city's service delivery goals and fiscal capacity.

The importance of CIPs was first formally recognised under national programmes like Jawaharlal Nehru National Urban Renewal Mission (JNNURM) (2005–2015) and Urban Infrastructure Development Scheme for Small and Medium Towns (UIDSSMT) (2005–2014), which mandated city-level planning and introduced project pipelines reflecting sectoral priorities. While these schemes helped institutionalise planning to some extent, the practice has not continued consistently across states or been scaled adequately to newer or smaller urban settlements.

Hence, we recommend that each ULG be mandated to develop and publish a CIP by Year 2, outlining sector-wise capital projects over a 5-year horizon.

The CIP must:

- a. Outline **sector-wise capital** projects over a minimum **5-year horizon**.
- b. Include **estimated project costs, phasing, financing strategies, and operations and maintenance (O&M) requirements**.
- c. Be **approved by the Municipal Council** and published on the ULG website and CityFinance.

From Year 3 onwards, capital projects identified in the CIP must be integrated into the ULG's annual budget documents, thereby institutionalising the practice of linking planning to budgeting. CIP ensures that ULGs are not just reacting to immediate pressures but planning systematically for the future. By embedding CIPs into City Development Plans and aligning them with annual budgets, ULGs can move towards fiscally responsible, transparent, and service-oriented urban development.

Output:

- a. CIP published and approved by the Municipal Council by Year 2.

4. Publication of City-level Economic Data

ULGs with populations between 500,000 and 4 million are India's economic engines-in-waiting. Yet, they often operate in a data vacuum when it comes to local economic activity. Without reliable, disaggregated economic data at the city level, these urban centres cannot understand their growth drivers, plan effectively, or monitor the outcomes of public investment and reform.

Meaningful progress requires accurate baseline measurements; only then can improvement be tracked and validated. Whether a city aims to boost employment, attract industry, enhance productivity, or increase tax revenues, performance must be measured against reliable baseline data. The absence of consistent city-level data on GDP, sectoral outputs, employment, land use, or real estate dynamics makes it impossible for city leaders to diagnose problems or assess the impact of interventions. Without data, policy becomes guesswork.

Such data proves essential for city-level investment promotion, regulatory reform, and labour market analysis. Most mid-sized ULGs currently lack mechanisms to track or publish economic activity indicators. Publishing economic data builds institutional discipline, incentivising local governments to establish robust systems for collection, validation, and publication. Moreover, making this data publicly accessible enables citizens, media, and researchers to hold ULGs accountable for economic outcomes.

Hence, we recommend that ULGs with populations between 500,000 and 4 million should publish economic data annually on CityFinance.

Output:

- a. Publish economic data annually from Year 1 to Year 5.

Table 19: List of Data to be Published Under Output-linked Grants

Data Point	Source Authority	Availability
Number of commercial establishments	ULG	High; available with ULG
Commercial property tax collections	ULG	High; available with ULG
Trade licenses issued	ULG	High; available with ULG
Property registrations (value and volume)	State Revenue Department	Medium; available but requires coordination
Vehicle registrations (RTO)	State Transport Department	Medium; available but requires coordination
Investments announced/implemented	State Industries Department	High; accessible to ULGs
Commercial power consumption	State Power Department	High; accessible to ULGs

Table 20: Conditions for Category II Output-linked Grants

Conditions	Year 1	Year 2	Year 3	Year 4	Year 5
1. Annual year on year increase of OSR by 7.5%	✓	✓	✓	✓	✓
2a. Public inventory of public land on CityFinance (state+parastatal+ULG)		✓			
2b. Market valuation of public land assets			✓		
3. Prepare and publish CIP		✓	✓	✓	✓
4. Publish economic data	✓	✓	✓	✓	✓

6.2.3 Grants for Category III ULGs (Metros with Population Above 4 million)

India's urban economic output is heavily skewed towards its metro cities (with populations above 4 million). Nearly 10% of India's GDP is generated by just 5 metropolitan regions — Bengaluru, Chennai, Hyderabad, Kolkata, and Mumbai¹²⁶. Though they represent just a fraction of the national population, they contribute disproportionately to the national GDP, demonstrating 1.5 to 2 times higher economic productivity relative to their population share. For instance, Greater Mumbai accounts for 20% of Maharashtra's GDP (2021-22); Bengaluru for 36% of Karnataka's GDP (2021-22); Hyderabad for 18% of Telangana's; and Chennai for 8% of Tamil Nadu's GDP (2019-20)¹²⁷.

Metros also host India's most vibrant startup and innovation ecosystems. Bengaluru has emerged as India's technology and startup capital, ranking 14 globally in the 2025 Startup Genome Ecosystem Report. This is a significant improvement from 21 in 2024 and places the city in the company of top hubs like Paris and Seattle¹²⁸. Bengaluru alone has produced 42 unicorns (startups valued >\$1B) while Mumbai has 17 unicorns¹²⁹. This concentration of high-growth startups in the metros signals tremendous entrepreneurial energy and job creation potential. The innovation infrastructure — skilled talent pools, investors, incubators — is in place. However, experts note that leveraging the economic potential of these metros depends on addressing structural constraints.

Inadequate urban infrastructure and quality of life issues are already impeding growth in India's metros. These cities consistently perform poorly in global city performance rankings. Mumbai, India's financial capital, was ranked only 427 in a recent global cities index (out of 1,000 cities) when measured across parameters of economy, human capital, quality of life, environment, and governance. In the Economist Intelligence Unit's Global Liveability Index¹³⁰ both Delhi and Mumbai rank 141 out of 173 cities. Other Indian cities in the list include Chennai (144), Ahmedabad (147), and Bengaluru (148). These quality of life deficits directly constrain economic growth by hampering talent retention, deterring investment, and reducing productivity, limiting the metros' ability to fully capitalise on their economic advantages.

To unlock the full economic potential of India's largest urban centres, **we recommend outcome-based grants exclusively for the seven ULGs with populations above 4 million**. These metros have significant own-source revenue for meeting basic expenditure needs and can generate additional resources by improving operational efficiencies, given their strong economic foundations.

¹²⁶ Gandhi, S., & Pethe, A. (2017). Emerging challenges of metropolitan governance in India. *Economic and Political Weekly*

¹²⁷ Singh, M. K., Sidharth, R., & Shah, A. (2025, January 29). CityGST: Direct city financing [Report, forthcoming].

¹²⁸ Startup Genome. (2025, June 17). Bengaluru climbs to 14th place in Global Startup Ecosystem Report 2025. *The Economic Times*. <https://economictimes.indiatimes.com/tech/startups/bengaluru-climbs-to-14th-place-in-global-startup-ecosystem-report-2025/articleshow/121830491.cms?from=mdr>

¹²⁹ Tiwari, A. (2023). Mapping the Start-up Ecosystem in India. https://doras.dcu.ie/29724/1/Mapping_the_Startup_Ecosystem_in_India.pdf

¹³⁰ The EIU's index assesses the liveability of cities based on factors like stability, healthcare, culture, environment, and infrastructure.

Fiscal transfers to these ULGs should therefore focus on enhancing economic productivity rather than basic service provision. Recent experience with reform-oriented schemes such as the Special Assistance to States for Capital Investment has demonstrated that both states and ULGs are increasingly willing and able to undertake reforms when incentivised through targeted fiscal mechanisms. Accordingly, **we propose a total allocation of ₹51,699 crore (15% of total ULG allocations, equivalent to their share in urban population) over the XVI FC period for these outcome-based transfers.**

The XVI FC can pursue an ambitious approach by linking grants for these metros to improvements in service level benchmarks while driving higher economic growth. We propose linking Finance Commission transfers to performance across three parameters, weighted to reflect both ULG capacity and growth potential:

1. **Service Level Benchmarks (50%)**
2. **Land and Planning (30%)**
3. **Economic Growth (20%)**

Given that ULGs currently play a limited role in direct economic growth activities, the 20% weight for economic growth represents a strategic starting point. The indicators identified focus on areas where ULGs can actively contribute to growth management within their jurisdictional capacity.

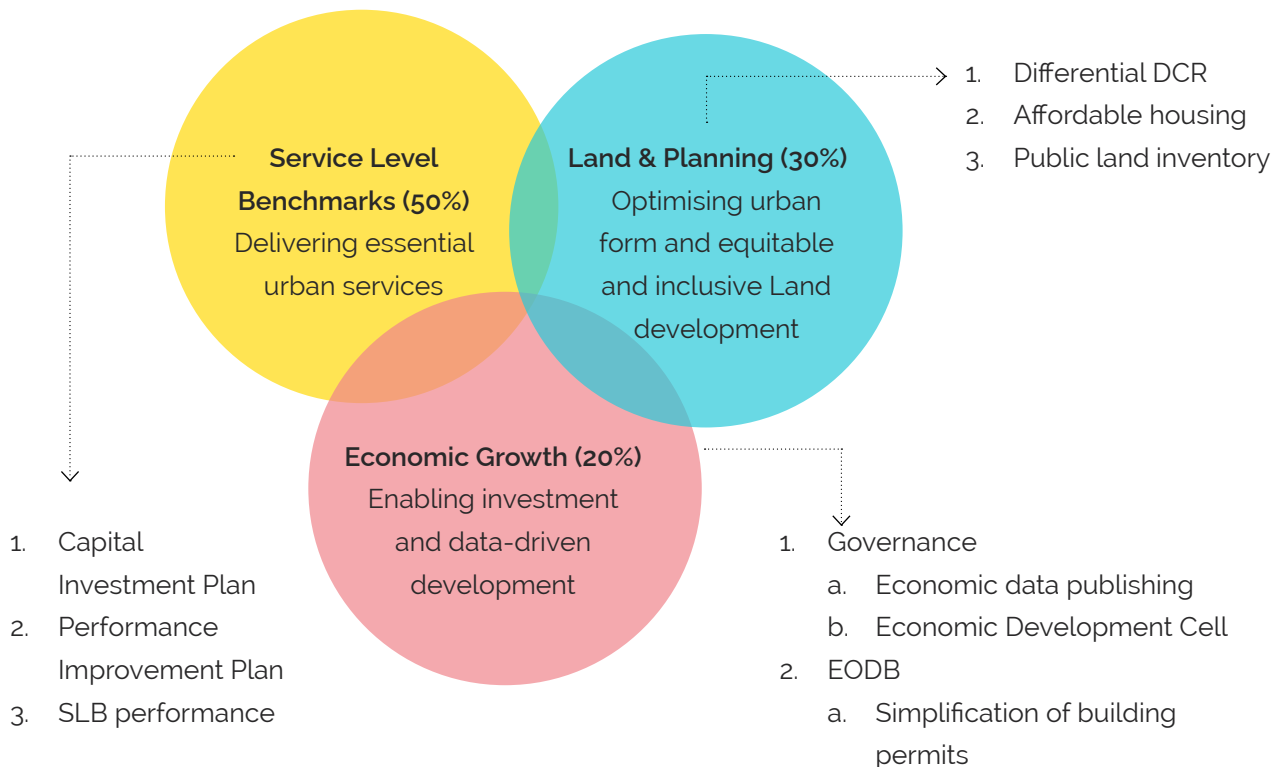


Figure 25: Grant architecture for Category III

Parameter 1: Service Level Benchmarks (Delivering Essential Urban Services)

Despite being economic engines of the country and amongst the most resource-abundant in terms of revenues and workforce, India's metros still struggle to deliver basic services. According to a McKinsey report, service standards in Indian cities fall significantly below basic benchmarks, highlighting the urgent need for better monitoring and capacity building¹³¹. These service gaps and inadequate infrastructure manifest in everyday challenges, reducing both quality of life and economic efficiency.

Bengaluru and Kolkata rank amongst the slowest cities globally for commutes¹³². Such bottlenecks exact a heavy productivity cost. Bengaluru loses ₹20,000 crore just from traffic congestion. Poor infrastructure not only lowers quality of life but also economic efficiency – e.g., firms face higher logistics costs, workers face long commutes, and cities become less attractive for talent. Frequent floods and waterlogging each monsoon due to inadequate drainage also cost cities; in 2015, Chennai floods caused \$3 billion in damages¹³³. Water scarcity presents another critical challenge — in 2024¹³⁴, Bengaluru faced shortages of 500 million litres daily due to groundwater depletion and dried lakes¹³⁵.

Such infrastructure deficits undermine economic efficiency — firms face higher logistics costs, workers endure lengthy commutes, and metros become less competitive in attracting businesses, talent, and investment. Service delivery improvements, therefore, are critical for sustained economic growth.

Given this imperative, we recommend that improvements in service level benchmark constitute the most important parameter, carrying 50% weightage in overall performance assessment.

ULGs should select one priority area from the four service level themes defined in MoHUA's 2008 Handbook on SLBs: water supply, wastewater management, solid waste management, or stormwater drainage. However, recognising that some metros face other pressing challenges, such as mobility constraints, the XVI FC may consider expanding eligible service areas to include traffic management, public transport (including non-motorised transport), and walkability. This would require MoHUA to develop corresponding benchmarks for these additional sectors.

In coordination with MoHUA, the Department of Expenditure (DoE), and state governments, ULGs will identify one major challenge area, set ambitious targets, and address infrastructure and service deficits in that sector using a substantial allocation of Finance Commission funds. Performance scoring will be calculated based on targets set versus actual achievement, with

¹³¹ India's Urban Awakening: Building Inclusive Cities, Sustaining Economic Growth. 2010. McKinsey Global Institute.

¹³² TomTom. (2023). Traffic Index Report: Global City Rankings. Retrieved from <https://www.tomtom.com>

¹³³ C. Bandyopadhyay, M.K. Bindal, and M. Manna, Chennai Floods 2015 (New Delhi: National Institute of Disaster Management, Ministry of Home Affairs, 2021).

¹³⁴ Singh, M. K., Sidharth, R., & Shah, A. (2025, January 29). CityGST: Direct city financing [Report, forthcoming].

¹³⁵ Business Today. (2024, March 19). Bengaluru facing shortage of 500 million litres water per day, says Karnataka CM. <https://www.businesstoday.in/india/story/bengaluru-facing-shortage-of-500-million-litres-water-shortage-per-day-says-karnataka-cm-421978-2024-03-19>

scores proportional to the percentage of targets met.

To ensure effective implementation of this performance parameter and improve service delivery, a systematic approach is needed to address two structural issues:

a. The absence of reliable, verifiable data on service delivery

Over the past decade, performance measurement has increasingly been adopted as a tool to monitor, plan, and improve urban service delivery. MoHUA's SLB framework offers a standardised structure for tracking outcomes across ULGs. However, in practice, **the reliability of this self-reported data remains questionable. Without well-functioning Management Information Systems (MIS) and third-party audits, ULGs often overstate performance**, not necessarily with the intent to misrepresent but because they are not incentivised to generate credible service level data. Additionally, ULGs do not maintain or publish service level data by zones or wards. Significant inequities exist within ULGs in terms of service delivery. Reliable spatial data on service delivery would enable more nuanced understanding of current status and gaps.

b. Fragmented infrastructure planning processes

In many ULGs, infrastructure investments are implemented in a reactive and ad hoc manner, disconnected from statutory Master Plans or Development Plans. **This unsystematic approach is exacerbated by the absence of a framework for integrated infrastructure and medium-term financial planning at the ULG level.** As a result, there is no structured process to assess service delivery gaps, define priorities, and develop a shelf of projects. This severely limits the ability of ULGs to strategically allocate resources or deliver sustained improvements.

To address these concerns, we propose a phased implementation approach: grants can be linked to input improvements during the first three years and to output-based performance in the last two years.

Operationalisation Parameter 1

As discussed above, the objective of the parameter is to improve service delivery in India's metros. To achieve this, this performance parameter focuses on ULGs establishing a strong foundation in the first three years through: (i) reliable data ecosystems and (ii) infrastructure planning. In subsequent years, performance is tracked through improvements in SLBs, that is, outputs.

In the first quarter of Year 1, before receiving first-year grants, ULGs will undertake a baseline study across the four SLB sectors — water supply, sanitation, solid waste management, and stormwater drainage — or the additional sectors as finalised by the Finance Commission. The baseline study will help identify where the ULG is underperforming and establish targets for that area over the

subsequent four years. Once a sector has been selected, each ULG will develop a comprehensive Performance Improvement Plan (PIP) for that sector during the first year.

Box 6: Performance Improvement Plans – Framework and Benefits

A Performance Improvement Plan (PIP) enables ULGs to adopt a systematic and data-driven approach to improving urban service delivery, institutional performance, and financial sustainability. It represents a departure from traditional infrastructure-focused methods toward comprehensive service improvement.

This report utilises the PIP framework developed by the Centre for Water and Sanitation (CWAS), CEPT University, which emphasises the role of performance planning in strengthening local governance and accountability. A well-designed PIP supports ULGs in:

- i. Diagnosing service delivery gaps and understanding current performance levels
- ii. Defining priority actions linked to clear, time-bound outcomes
- iii. Ensuring financial sustainability by planning realistic capital and O&M interventions and
- iv. Strengthening institutional capacity, enabling cities to adopt best-fit strategies for long-term service and fiscal improvement

By anchoring improvement efforts in a structured and data-driven framework, PIPs provide ULGs with a pathway to move from reactive responses to proactive, accountable urban governance.

Building on this framework, Table 21 presents the four essential components that should be integrated into every PIP for systematic service level improvements.

Table 21: Key Components of Performance Improvement Plans

Component	Description
Data improvement plans	Recommendations for technology adoption (for example, SCADA for water, GPS/IoT/RFID/GIS for solid waste management); creation of MIS units; integration with ICCCs to strengthen real-time tracking.
Process/policy reforms	Identification of regulatory or administrative barriers to effective service delivery, and actions to address them through targeted reforms.
Existing system upgrades	Low-cost enhancements to current infrastructure or operations that can yield measurable improvements.
New infrastructure planning	Development of a list of high-priority projects based on gap analysis for inclusion in the Capital Investment Plan.

In Year 2, ULGs will begin implementation of the PIP through action on the first three components (Table 21). For the fourth component, ULGs should prepare a Capital Investment Plan (CIP). The CIP must outline the prioritisation and sequencing of physical investments, estimated fiscal requirements for capital and O&M expenditure, and technical and institutional capacity required for implementation. It should also establish clear outcome targets for the selected sector over the three-year implementation period. This will determine the release of grants in Year 3.

From **Year 3 onwards (2029–30 to 2030–31)**, ULGs shall progressively demonstrate improvements in **SLB indicators** for the selected theme. These improvements must be backed by data sourced directly from the digital systems implemented under the PIP — such as SCADA, GIS-based tracking, or MIS dashboards. Reporting should be **independently verified by third-party agencies empanelled by MoHUA or the respective state governments**.

Table 22 outlines the year-wise performance conditions for parameter 1 that ULGs must achieve to claim grants in the given year.

Table 22: Year-Wise Performance Conditions for Parameter 1 (Service Level Benchmarks)

Year	Performance Conditions
Year 1	Publication of baseline service-level assessment across the four SLB sectors (or other additional sectors identified by the FC) and establishment of targets in coordination with MoHUA, DoE, and state government for the selected sector.
Year 2	Publication of Performance Improvement Plan
Year 3	Publication of Capital Investment Plan
Year 4 & 5	Performance achievement against established targets for the selected sector

Parameter 2: Land and Planning (Optimising Urban Form and Equitable Land Development)

ULGs in India face a crisis of land mismanagement. Urban land is not efficiently utilised and land development is neither inclusive nor equitable. This crisis stems from three interconnected issues that reinforce each other: restrictive density regulations that encourage sprawl, systematic exclusion of the poor from formal housing markets, and the widespread underutilisation of valuable public land.

a. Urban sprawl and density restrictions

India's cities have been growing rapidly and are expanding outward rather than upward. Instead of compact, efficient growth, they are sprawling inefficiently toward the peripheries driven by

rigid building regulations, inflated land prices, and the absence of zone-specific planning¹³⁶. Development Control Regulations (DCRs), which govern building heights, land use, and Floor Space Index (FSIs), are often outdated, overly restrictive, and applied uniformly across vastly different cities. The result is inefficient land use, limited economic agglomeration, and a built environment that drives jobs and affordable housing to the outskirts, deepening spatial inequality.

For instance, the peripheral zones of Bengaluru have grown nearly seven times faster than the city core over the last decade, straining infrastructure and increasing commute times. Building regulations limit the construction of high-rises in the city core, resulting in reduced available space for households and firms. This in turn inflates land prices and drives further sprawl¹³⁷. This pattern is visible across many Indian metros. Moreover, restrictions on land use intensity reduce agglomeration economies and limit productivity¹³⁸. Land, which should be an enabler, becomes a constraint. **According to the India Infrastructure Report (2009), issues related to land acquisition and availability account for nearly 70% of delays in infrastructure and development projects¹³⁹.**

The lack of city-specific DCRs is a core reason behind this inefficiency. As of today, only 29 Indian cities have their own DCRs. In contrast, 16 states impose uniform regulations on over 1,900 cities, regardless of their size, density, land values, or economic role. Cities as varied as Nagpur and Ratnagiri, or Cuddalore and Coimbatore, are governed by the same height limits, setback rules, and FSIs. This 'one-size-fits-all' approach suppresses the development potential of central business districts, transit corridors, and mixed-use zones, leading to low-rise, underutilised urban cores and artificially inflated land prices.

By contrast, global cities like New York and Tokyo have deployed flexible, zone-specific DCRs to enable compact, mixed-use, and transit-oriented development. These reforms have generated both public amenities and economic value.

b. Shortage of affordable housing

Land availability and regulation have a direct impact on housing supply, specifically affordable housing. By 2030, India's ongoing urbanisation will see over 40% of the population residing in urban areas¹⁴⁰, creating an expected shortfall of 31.2 million affordable housing units with a potential market of ₹67 trillion¹⁴¹.

¹³⁶ Singh, M. K., Sidharth, R., & Shah, A. (2025, January 29). CityGST: Direct city financing [Report, forthcoming].

¹³⁷ Ibid

¹³⁸ Ibid

¹³⁹ Sivam, A. (2002). Constraints affecting the efficiency of the urban residential land market in developing countries: a case study of India. *Habitat International*, 26, 523–537.

¹⁴⁰ Press Information Bureau, Government of India. (2024, August 7). Economic survey of rural-urban population (Release No. 2042542). Ministry of Statistics & Programme Implementation.

¹⁴¹ Confederation of Indian Industry. (n.d.). Press release: India's affordable housing market set to reach 67 Tn; demand expected to be 31.2 mn units by 2030: CII - Knight Frank India Report.

While government schemes such as PMAY have made progress, demand for housing, especially among low-income migrants, continues to outpace supply. Where affordable housing is available, it is inconveniently located, often on the peripheries, and lacks access to basic services.

India's urban housing crisis is, therefore, not just a question of supply but of location, quality, and equity. To address this, we must shift from reactive slum redevelopment to proactive slum prevention. This will require integrating affordable housing into mainstream urban planning and land use strategies.

c. Underutilised or misallocated public land

India's public land holdings spanning union ministries, state agencies, and ULGs represent one of the country's most significant underutilised assets. At present, public land management lacks transparency, hampering efforts to leverage these assets for societal and economic benefits.

For example, a pilot public land inventory in Ahmedabad found that over 30% of all developable land within the ULG limits was publicly owned. The Ministry of Defence is India's largest landowner, with holdings of over 7 lakh acres, of which about 0.7 lakh acres are outside cantonments, many in prime urban areas¹⁴². This represents substantial opportunity costs. Prime urban land that could house millions or generate revenue for public services instead remains underutilised. A transparent land asset registry could reveal the true wealth of cities that can be harnessed to provide for amenities, public space, and economic growth.

To unlock the economic potential of metros while addressing spatial inequities, we recommend that land and planning constitute the second parameter, carrying 30% weightage in overall performance assessment. Performance under this parameter should be linked to meaningful progress on two critical fronts:

1. Reforming urban planning and land-use regulations and integrating affordable housing into development strategies through proactive, spatially informed action.
2. Creating comprehensive inventories and valuations of public land assets.

Operationalising Parameter 2

This performance parameter is structured across three phases: (i) diagnosis and planning, (ii) regulatory action and piloting, and (iii) implementation. This phased approach provides ULGs with sufficient time and resources to move from intent to action while ensuring measurable progress over the XVI Finance Commission period.

¹⁴² Annez, P. C., & Gangopadhyay, S. (Eds.). (2013). India's public lands: Responsive, transparent, and fiscally responsible asset management. IDF Research. https://www.idfresearch.org/uploads/R_a_c_e/1547204311_92201612234653.pdf

Phase 1: Diagnosis and planning

In Year 1, ULGs, in partnership with State Town and Country Planning Departments, will begin preparatory work by:

- i. Conducting multi-stakeholder consultations with planners, real estate developers, parastatal agencies, and citizen groups for developing DCRs.
- ii. Initiating the creation of a public land inventory across ULG, state, and union agencies.

ULGs will not be required to meet any performance conditions under this parameter in Year 1. This period is intended for the preparatory work required for regulatory reforms and assessment of land inventories.

Phase 2: Regulatory action and piloting

In Year 2, ULGs will publish and notify differentiated DCRs after identifying distinct growth zones within their jurisdiction, such as the city core, peri-urban expansion areas, transit-oriented corridors, and industrial zones. These zones will serve as the basis for differentiated planning and regulation. State government, in partnership with ULGs, will be expected to formally adopt the revised DCRs, ensuring they are officially integrated into development control systems. State Town and Country Planning Departments will be responsible for the formal notification process and will provide technical approvals while ensuring policy alignment with broader state-level planning frameworks. To incentivise compliance and attract private sector participation, ULGs could incorporate creative zoning incentives into the new DCRs. These could include increased Floor Space Index allowances in exchange for public benefits (such as affordable housing, public plazas, or infrastructure improvements), tax breaks for inclusive development, or conditional fast-tracking of approvals. Additionally, ULGs will prepare and publish a Slum Proofing Action Plan (SPAP) to proactively integrate affordable housing into urban planning. This will include:

- i. Demand-supply gap assessments
- ii. Typology-based solutions (for example, rental, dormitory, and transitional housing)
- iii. Identification of public land for housing projects
- iv. Housing quality and liveability benchmarks.

The SPAP will also define spatial and service delivery standards for future housing to ensure quality and liveability. Each ULG will facilitate coordination across internal departments such as planning, engineering, and social development to ensure the SPAP is fully integrated into the ULG's development systems and processes.

Parastatal agencies including Development Authorities, Metro Rail Corporations, and State Housing Boards will be expected to align their landholdings and infrastructure projects with the revised DCRs and SPAP targets.

Each ULG must also develop and publish a comprehensive inventory of public land assets in Year 2. This inventory should include land held by the ULG, state departments, and parastatal agencies, and must be mapped and made accessible through online spatial systems. The objective is to create transparency in landholding and open up underutilised land for productive use.

Phase 3: Implementation

In Year 3 (2029–30), the focus will shift from regulatory and policy action to implementation.

Each ULG must identify a core area development or redevelopment project, ideally located in the central business district or another high-impact zone where the revised DCRs and affordable housing provisions will be piloted. This pilot will allow ULGs to test new planning instruments and build public and institutional confidence in the revised framework. **ULGs should prepare Detailed Project Reports (DPRs) for both the core area project and the identified affordable housing pilot.** They should also initiate procurement processes such as issuing Expressions of Interest (EOIs) or Requests for Proposals (RFPs).

Alongside this, a **ULG-level land market valuation report** should be published. This report will provide a reference point for understanding prevailing land values across the ULG, and support land allocation, pricing, and monetisation strategies for affordable housing and public infrastructure. Market valuation of land parcels can be undertaken using:

- i. Circle rates and transaction history from the past decade
- ii. FSI utilisation data to assess underdevelopment or inefficiency
- iii. Proximity to key infrastructure and transit nodes
- iv. Current and proposed land use under notified plans
- v. Comparative valuation of nearby private parcels, where available

In Year 4 and 5, ULGs are expected to demonstrate concrete progress toward implementation of the identified **core area development or redevelopment project and the identified affordable housing pilot project**.

Hence, from Year 4 onwards, grant disbursement will be progressively linked to implementation milestones. These include:

- i. Verified progress in the core area development or redevelopment and affordable housing projects, such as infrastructure provision, construction initiation, or completion of defined phases.
- ii. Development of a real-time monitoring dashboard to track execution.

Table 23: Year-wise Performance Conditions for Land and Planning

Year	Performance Conditions
Year 1	No condition; ULG to undertake preparatory work
Year 2	• Publish and notify zone-specific DCRs and Slum Proofing Action Plan (SPAP) • Publish public land inventory
Year 3	• Finalise DPRs for DCR pilot and affordable housing; issue EOIs/RFPs • Publish market valuation of the public land inventory
Year 4 & 5	• Demonstrate project implementation progress in core zone (affordable housing and DCRs) • Operationalise real-time monitoring dashboard for tracking progress

Parameter 3: Economic Growth (Enabling Investment and Data-driven Development)

ULGs are primarily seen as service delivery agents, executing schemes designed by higher levels of government. Under the current framework, ULGs have limited say in shaping their economic future. There is no executive authority tasked with overseeing the economic growth of a ULG. According to the NITI Aayog–ADB report, *Cities as Engines of Growth*, ULGs remain confined to land use, roads, and building control, without actively engaging in investment promotion or economic strategy¹⁴³. This limits urban growth potential. The XVI Finance Commission can use performance grants to incentivise ULGs to take an active interest in urban economic development.

To enable metros to assume greater responsibility for economic strategy and investment promotion, we recommend that economic growth constitute the third parameter, carrying 20% weightage in overall performance assessment. This comprises three sub-parameters:

- i. Setting up an Economic Development Cell within ULGs (5%)
- ii. Measuring and reporting city-level economic data (5%)
- iii. Improving ease of doing business (10%)

a. Setting up an Economic Development Cell within ULGs (5%):

Each ULG should establish an Economic Development Cell to oversee economic development activities. The EDC will lead ULG-level investment promotion, coordinate across stakeholders, monitor regulatory simplification, and support enterprise engagement, particularly with MSMEs and priority sectors.

Primary responsibilities of the EDC may include:

- i. Publishing and reviewing city-level economic indicators on a quarterly basis
- ii. Coordinating with industry bodies (for example, CII, FICCI, NASSCOM) to promote the city as an investment destination
- iii. Reviewing local business regulations and licensing processes

¹⁴³ NITI Aayog & Asian Development Bank. (2022, May). *Cities as engines of growth: Executive summary* (TA-9508: Strengthening the States for broad-based urban development). New Delhi: NITI Aayog.

- iv. Mapping investment opportunities and underutilised municipal assets
- v. Conducting consultations and recommending reforms to support MSMEs

ULGs should also establish a councillor committee to engage elected representatives in economic development activities.

b. Measuring and reporting city economic data (5%)

Currently, ULGs lack consistent and reliable data on their economic performance. There is no system of regular reporting on city GDP, sectoral output, or employment figures, preventing the design and deployment of targeted growth strategies.

Global cities routinely publish quarterly economic indicators to guide development. The Government of India has recognised this gap and is attempting to address it: MoHUA has established a committee to develop methodologies for measuring city-level economic output. This move acknowledges that measuring ULG performance is key to developing them as 'engines of growth'¹⁴⁴.

The absence of ULG-level economic data also hampers planning, budgeting, and private sector engagement to address the needs of different kinds of businesses. MSME requirements are often overlooked in industrial planning, and many ULGs lack the historical data visibility needed to identify and build upon economic clusters.

To improve economic visibility, inform infrastructure and sector planning, and support private investment decisions, ULGs should be required to publish a core set of economic indicators on their website and on CityFinance. This data should cover commercial activity, real estate, tax collections, infrastructure use, and employment. **For Year 2, ULGs can publish their first quarterly economic dataset in the prescribed format, drawing from existing sources.** From Year 3 onwards, the data requirements can be increased.

Operationalising Parameter 3

The objective of these sub-parameters is to institutionalise economic oversight within ULGs while establishing regular publication of economic data for evidence-based planning. Economic Development Cells provide the institutional authority for economic strategy and investment promotion, and systematic data collection enables targeted reforms and informed decision-making.

Phase 1: Institutional setup and initial data reporting

In Year 2, ULGs establish Economic Development Cells and begin publishing quarterly datasets from existing sources covering seven economic indicators.

¹⁴⁴ NITI Aayog & Asian Development Bank. (2022, May). Cities as engines of growth: Executive summary (TA-9508: Strengthening the States for broad-based urban development). New Delhi: NITI Aayog.

Table 24: List of Data Requirements for Parameter 3(B), Phase 1

Sl. No	Data Point	Source Authorities	Availability
1	Number of commercial establishments	ULG	High; available with ULG
2	Commercial property tax collections	ULG	High; available with ULG
3	Trade licenses issued	ULG	High; available with ULG
4	Property registrations (value and volume)	State Revenue Department	Available; requires coordination
5	Vehicle registrations (RTO)	State Transport Department	Available; requires coordination
6	Investments announced/implemented	State Industries Department	High; accessible to ULGs
7	Commercial power consumption	State Power Department	High; accessible to ULGs

Phase 2: Expand data collection

From Year 3 onwards, in addition to indicators listed in Table 24, ULGs can publish two additional data sets on enterprise and employment.

Table 25: List of Additional Data Requirements for Parameter 3(B), Phase 2

Sl. No	Data Point	Details Point
1	Number of MSMEs	Sector classification, employment, spatial distribution
2	Number of startups	Sector classification, employment, spatial distribution

ULGs must publish quarterly data on both the city-level metrics on CityFinance. State governments and MoHUA will monitor compliance through dashboards and independent audits. Data publication and functioning of the EDC will be reviewed annually as part of grant renewal. The goal is to institutionalise a data culture where economic indicators inform decision-making, budgeting, and outreach.

c. Improving ease of doing business (10%)

India demonstrated a marked improvement in Ease of Doing Business (EoDB), climbing from the 142nd rank in 2015 to 63rd in 2020. However, the country still lags behind others like China (ranked 31) and South Korea (ranked 5)¹⁴⁵.

¹⁴⁵ World Bank. (2020). Doing Business 2020: Comparing Business Regulation in 190 Economies. Retrieved from <https://www.doingbusiness.org>

At the ULG level, the regulatory ecosystem remains cumbersome. Starting a business, obtaining construction permits, registering property, and contract enforcement can be protracted processes in major metros. ULG-level regulations (for example, signage, health, trade licences) often overlap with state rules, creating red tape. An analysis by NITI Aayog (2022) noted "lack of business and investment-friendly initiatives and regulations" in urban and peri-urban areas as a key factor limiting ULG growth. There is a strong positive correlation between EoDB and per capita GDP.

Globally, ease of obtaining building permits is considered a core indicator of the health of the construction sector and the broader economy. Construction accounts for nearly 8–10% of India's Gross Value Added (GVA)¹⁴⁶. Effective permitting and inspection systems strengthen property rights and contribute to capital formation, while poorly functioning systems promote rent-seeking and corruption¹⁴⁷. Since building permits typically involve licensing requirements from multiple agencies, they pose a critical challenge to entrepreneurs deciding where to invest. Importantly, construction permits are one of the few EoDB parameters that are directly controlled by ULGs. India's dramatic improvement in EoDB rankings from 2014 to 2020 was largely attributed to reduced timelines and streamlined processes for construction permits, which improved the country's construction permitting rank from 184 to 27 during the same period¹⁴⁸.

Regulations serve an essential public function by addressing market failures and protecting welfare. However, regulations that are duplicative, outdated, or unclear impose significant costs without adding corresponding public value. The problem is not the existence of regulation itself, but rather the persistence of red tape and opaque procedures that delay investment, increase costs, and create avenues for corruption. The objective, therefore, is to retain the regulatory intent while eliminating inefficiencies that provide no public benefit.

To streamline regulatory processes and enhance investment attractiveness, we recommend that building permits reform be assigned 10% weightage for metros. This reform will follow a structured framework: (i) legislative amendments, (ii) implementation of streamlined processes, and (iii) continuous monitoring. The aim of this reform is to ensure that, by Year 4, at least 80% of building permits are issued within 45 days¹⁴⁹.

The objective of this sub-parameter is to streamline building permits while maintaining regulatory standards. Implementation begins with baseline establishment and legal framework preparation in Year 1, followed by progressive target achievement from Years 2-5 to ensure measurable improvement in processing efficiency.

¹⁴⁶ CRISIL. (2024). Assessment of the construction industry in India. Retrieved from <https://vclgroup.in/public/upload/uploads/20240930164312.pdf>

¹⁴⁷ World Bank. (n.d.). Dealing with construction permits: Why it matters. Retrieved from <https://subnational.doingbusiness.org/en/data/exploretopics/dealing-with-construction-permits/why-matters>

¹⁴⁸ Embassy of India, The Hague. (n.d.). Ease of doing business in India. Retrieved from <https://www.indianembassynetherlands.gov.in/page/ease-of-doing-business-in-india/#~:text=Construction%20Permits%3A%20India%27s%20ranking%20on,obtaining%20construction%20permits%20in%20India>

¹⁴⁹ The 45-day timeline encompasses all four key stages of the building permit process: (1) online building plan approval, (2) plinth level inspection and approval, (3) completion certificate, and (4) occupancy certificate. This timeline excludes the duration required for obtaining or submitting any mandatory No Objection Certificates (NOCs) from external agencies.

Phase 1: Legislative amendments

In Year 1, MoHUA, DPIIT, DoE, and relevant state governments will identify legal amendments and procedural changes at the state and ULG levels that can reduce timelines to obtain building permits. All ULGs must publish baseline data on current timelines and set targets for:

- i. Approval time for building permits
- ii. Percentage of permits processed within target timeframe.

Phase 2: Implementation and monitoring

From Year 2 onwards, grant disbursement will be linked to achieving outcome targets. The 45-day timeline for building permits should be achieved in 40% of permits in Year 2, in 60% by Year 3, 80% by Year 4, and 100% by Year 5.

ULGs must also implement real-time monitoring dashboards to enable data transparency and third-party validation. While ULGs may self-report data, MoHUA should support audit and verification processes to ensure data credibility.

In addition to meeting targets, the reform should institutionalise a governance culture that values transparency, efficiency, and investor confidence.

Administrative Mechanism for Outcome-based Grants

At the beginning of the award period for the XVI FC, MoHUA, DoE, state governments, and the seven ULGs will jointly establish baselines, outcome targets, implementation roadmaps, and monitoring and verification mechanisms for each reform area. ULGs will report progress on indicators through the CityFinance, and data will be verified by independent third-party evaluators engaged by MoHUA or state governments.

Based on verified performance, grants will be disbursed as a single instalment in October each year. The quantum of grant disbursed will be proportional to the score obtained by the ULG. Even if a ULG secures at least 70% of the total score, it will be eligible to receive 100% of its grant allocation for that year. The Finance Commission may define additional score-based disbursement brackets and instruct MoHUA to operationalise these through implementation guidelines.

Table 26 summarises the conditions under the three parameters that Category III ULGs must meet to claim their outcome-based grants.

Table 26: Performance Conditions to Access the Outcome-based Grants

Performance Conditions for Accessing Grants			
Year	Service Level Benchmarks (50%)	Land and Planning (30%)	Economic Growth (20%)
Year 1	- Conduct and publish baseline assessment for all service level indicators - Identify a priority sector/theme, define targets for priority sector improvements for 4 years	No conditions; preparatory work	- Undertake and publish the study for baseline data on building permits timelines - Define target for: - Approval time for building permits (suggested: 45 days) - Percentage of permits processed within target timeframe. Year 2: 40% Year 3: 60% Year 4: 80% Year 5: 100%
Year 2	Publish Performance Improvement Plan (PIP)	- Publish and notify zone-specific DCRs and Slum Proofing Action Plan (SPAP) - Publish public land inventory	- Establish Economic Development Cell (EDC) in ULG - Publish Phase 1 economic dataset (Refer Table 24 (commercial establishments, trade licences, power use) - Ensure $\geq 40\%$ (indicative) of building permits are issued within 45 days
Year 3	Publish Capital Investment Plan (CIP)	- Finalise DPRs for: a) core area development/ redevelopment and b) affordable housing; issue EOIs/RFPs - Publish market valuation of the land inventory	- Continue quarterly publication of Phase 1 economic data - Ensure $\geq 60\%$ (indicative) of building permits are issued within 45 days
Year 4	Demonstrate performance against the set targets for the priority theme/ sector	- Demonstrate progress on: a) development/ redevelopment project using DCR in core zone and b) affordable housing project - Operationalise real-time monitoring dashboard for tracking progress	- Publish Phase 1 and Phase 2 data (enterprise and employment: MSMEs, startups) (Refer Table 24 and 25) - Ensure $\geq 80\%$ (indicative) of building permits are issued within 45 days
Year 5	Demonstrate performance against the set targets for the priority theme/ sector	Demonstrate progress on: a) development/ redevelopment project using DCR in core zone and b) affordable housing project	- Publish Phase 1 and Phase 2 data (enterprise and employment: MSMEs, startups) - Ensure 100% (indicative) of building permits issued within 45 days.

In addition to the above performance conditions, **the seven ULGs with populations above 4 million must also achieve year-on-year growth in own-source revenue of 7.5% for each year of the grant period.**

6.3 Additional Grants Under Local Government Grants

We propose two additional grants under local government grants to respond to systemic gaps in India's urban transition and governance capacity:

- i. Urbanisation Premium
- ii. Decentralisation and Capacities Grant

These are designed to complement the main grant-in-aid to ULGs by responding to specific needs that might not be addressed by traditional, formula-based transfers.

6.3.1 Urbanisation Premium

We recommend the establishment of an Urbanisation Premium amounting to ₹20,000 crore for the 2026–31 period. This fund will incentivise states to manage rural–urban transitions in a planned, capacity-ready manner. It will be sourced equally from Finance Commission allocations to rural and urban local governments, acknowledging that rural–urban transitions involve shared governance responsibilities between the two. The fund will support transitional and newly constituted ULGs and serve as a catalytic incentive for states to adopt Rural–Urban Transition Policies (RUTPs).

While the grant quantum may not fully meet the infrastructure needs of transitioning areas, it provides an essential boost for foundational investments such as water supply, sewerage, drainage, street lighting, connectivity and other urban infrastructure.

A detailed discussion on the rationale, design, and allocation methodology for this grant is provided in Chapter 2.

6.3.2 Decentralisation & Capacities Grant

The effective decentralisation of funds, functions, and functionaries is crucial to a ULG's responsiveness and accountability. Variations in contexts and capacities across ULGs necessitate localised decision-making for meaningful action on issues such as economic growth, equity, public health, and environmental sustainability.

The 74th Constitutional Amendment Act (CAA) marked a significant step forward in empowering ULGs as effective units of self-governance. It established the constitutional framework for

decentralisation: Article 243W devolved 18 functions to ULGs under the Twelfth Schedule; provisions were introduced for regular elections and the constitution of state finance commissions, metropolitan planning committees, and other institutional reforms. The Amendment was designed to enable independent decision making in local governments, to promote efficient service delivery, and to support sustainable urban development. It envisaged elected representatives as the single point of accountability for cities, ensuring responsiveness to citizen needs. However, three decades later, the promise of decentralisation remains unfulfilled.

Municipal functions have not been fully devolved to all ULGs. A CAG performance audit¹⁵⁰ on the implementation of the 74th CAA found that only 4 functions out of 18 were effectively devolved to ULGs. In many states, parastatal agencies continue to dominate service delivery in essential sectors such as water supply, sanitation, and planning. The absence of role clarity, institutional mechanisms for coordination, or monitoring of devolution further entrenches this imbalance.

Another critical issue is the disempowerment of elected representatives. Despite constitutional provisions, in many ULGs, elected representatives do not hold the executive powers to oversee key urban functions. Several ULGs also operate under the 'Commissioner as Chief Executive' model where an executive-appointed commissioner holds decision-making powers¹⁵¹. In fact, 61% of ULGs in 17 states did not have an elected council at the time of the CAG's performance audit¹⁵².

If India's cities are to successfully address the urban challenges of equity, economy, environment, and engagement, we must resolve fundamental systemic issues. Here, decentralisation emerges as a critical tool for enabling urban transformation. Evidence from Africa, Asia, and Latin America indicates that where 'decision space' (local discretion over functions like financing, service delivery, and human resources) has been effectively established, local capacity and accountability for these services are significantly stronger¹⁵³. However, decentralisation is not solely about transferring powers; it is about how those powers are devolved. While greater autonomy gives ULGs more responsibility for managing urban services, they must also possess the institutional capacity to deliver on these functions¹⁵⁴. Ultimately, the positive impacts depend on the quality of governance and the effectiveness of supporting systems.

Most ULGs continue to face deep institutional and capacity constraints that hinder their ability to function as effective units of self-governance. Chronic human resource shortages, unrealistic

¹⁵⁰ Comptroller and Auditor General of India. (2024). Compendium of performance audits on the implementation of the 74th Constitutional Amendment Act, 1992: Landscape across India (Vol. I).

¹⁵¹ Empowering city administration: Addressing India's problem with its urban local leadership. (2021, July 20). Law School Policy Review. <https://lawschoolpolicyreview.com/2021/07/20/empowering-city-administration-addressing-indias-problem-with-its-urban-local-leadership/>

¹⁵² Comptroller and Auditor General of India. (2024). Compendium of performance audits on the implementation of the 74th Constitutional Amendment Act, 1992: Landscape across India (Vol. I).

¹⁵³ Faguet, J.-P., & Pöschl, C. (2015). Is decentralization good for development? Perspectives from academics and policy makers. In J.-P. Faguet & C. Pöschl (Eds.), *Is decentralization good for development? Perspectives from academics and policy makers* (pp. 1-29). Oxford University Press

¹⁵⁴ Muringani, Jonathan and Dahl Fitjar, Rune and Rodríguez-Pose, Andrés (2018) Decentralisation, quality of government and economic growth in the regions of the EU. Retrieved from https://eprints.lse.ac.uk/91023/1/Rodriguez-Pose_Decentralisation-quality-of-government.pdf

budgets, and weak own-source revenue mechanisms are widespread. The CAG audits reveal a 37% average vacancy in sanctioned municipal positions, with several states exceeding 50%¹⁵⁵.

Digital and data infrastructure also remain severely underdeveloped. Most ULGs operate in fragmented digital environments where finance, public works, tax, and service delivery systems function in silos or on manual registers. This hampers integrated decision-making. A recent review by the National Institute of Urban Affairs (NIUA) found that fewer than 30% of small ULGs had integrated e-governance platforms; where they had been integrated, these platforms were rarely interoperable¹⁵⁶. The absence of integrated digital infrastructure limits real-time tracking of expenditures and service outputs, eroding citizen trust and operational efficiency.

Without urgent and dedicated investments in institutional strengthening, most ULGs will remain unable to absorb and effectively utilise their share of XVI FC urban allocations. This perpetuates a cycle of weak governance, underinvestment, and poor service delivery, particularly affecting small and medium-sized cities.

National urban missions already reflect the importance of investing in institutional and human capacities as a prerequisite for effective programme delivery. AMRUT 2.0 assigns 3.25% of its annual budget allocation (₹2,169 crore central share) specifically for capacity building and administrative expenses, with dedicated support for both individual and institutional components¹⁵⁷. Similarly, the Smart Cities Mission designates 5% of its funding under Administrative and Office Expenses (A&OE), supporting activities such as the preparation of Smart City Proposals (SCPs), engagement of PMCs, pilot studies, deployment of smart solutions, and approved capacity-building interventions¹⁵⁸. These provisions underscore a broader recognition that dedicating resources for capacity building is essential to ensure effective and efficient use of public funds.

As discussed, decentralisation and institutional capacity building are mutually reinforcing processes. Building on this logic, we recommend an **additional grant of ₹20,000 crore (~5% of the XVI FC's urban allocation) exclusively for 4,817 ULGs with populations below 4 million. The grant should be shared 50:50 between states and ULGs**, with each level having a distinct role in enabling and implementing reform.

Objectives of the grant

This Additional Grant aims to:

- i. Improve effectiveness of XVI FC grant utilisation.
- ii. Build robust institutional capacity within small and medium-sized ULGs.

¹⁵⁵ Comptroller and Auditor General of India. (2024). Compendium of performance audits on the implementation of the 74th Constitutional Amendment Act, 1992: Landscape across India (Vol. I).

¹⁵⁶ NIUA (2023). Urban Governance Digital Infrastructure Review: Status of Digitalisation in Indian ULGs. National Institute of Urban Affairs.

¹⁵⁷ Government of India, Ministry of Housing and Urban Affairs. (2021, October 26). AMRUT 2.0 operational guidelines [PDF]. https://amrut.mohua.gov.in/uploads/AMRUT_2.0_Operational_Guidelines.pdf

¹⁵⁸ Government of India, Ministry of Housing and Urban Affairs. (n.d.). Financing. Smart Cities Mission. <https://smartcities.gov.in/financing>

- iii. Facilitate professionalisation of municipal finance and urban planning functions.
- iv. Accelerate the effective decentralisation of functions, funds, and functionaries in line with the 74th Constitutional Amendment.

6.3.2.1 Eligibility for the Grant

ULGs with populations below 4 million and state governments will be eligible for this grant. This includes municipal corporations, municipalities, and nagar panchayats across all states that fall within this population threshold.

6.3.2.2 Proposed End-use of the Grant

1. State-level Use (50% of grant): Ecosystem building and reform support

i. Strengthen decentralisation

- a. Publish an annual 'State of Urban Decentralisation' report based on the state's performance audits and 74th CAA indicators.
- b. Establish dedicated teams to clarify functional roles between parastatals and ULGs, and monitor the devolution of funds, functions, and functionaries.

ii. Strengthen the municipal finance ecosystem

- a. Establish or enhance state-level Municipal Finance & Governance Reform Units.
- b. Provide advisory support for project preparation, appraisal, and financing strategies.
- c. Build capacity in ULGs to access market-based instruments like bonds and land value capture.

iii. Drive digital transformation

- a. Develop state-wide platforms for grant/scheme tracking and integrated works management.
- b. Enable real-time expenditure and output tracking, and public dashboards for transparency.
- c. Lead efforts for end-to-end digitalisation of finance and accounts, in accordance with NMAM 2.0 or the national city finance framework.

iv. Institutionalise human resource capacity

- a. Notify and operationalise a municipal finance and engineering cadre across ULGs.
- b. Introduce shared services centres for financial and technical services.
- c. Provide certification-based skilling programmes for municipal staff and elected representatives.

2.ULG-level Use (50% of grant): Direct capacity strengthening

i. City planning and visioning

- a. Prepare needs-based, participatory City Vision Documents linked to capital investment plans and ward-level action plans.
- b. Develop a shelf of projects with financing strategies and environmental-economic integration.

ii. Asset and land management

- a. Update asset registers and publish inventories of public land to support capital planning and land-based financing.

iii. Professional services and project execution

- a. Contract external professionals for DPR preparation, project finance, contract management, and F&A functions.

iv. Digitalisation of core functions

- a. Implement NMAM 2.0 or national city finance framework
- b. Implement integrated e-governance platforms for budgeting, accounting, billing, service tracking, and grievance redressal.
- c. Adopt digital transaction systems to capture transactions at point of occurrence such that accounting is automated based on data from the system

v. Reform revenue systems

- a. Undertake reforms related to OSR and other municipal finance.

vi. Improve service monitoring

- a. Establish robust systems for collecting, analysing, and reporting service-level benchmark data across sectors.

6.3.2.3 Minimum Eligibility Conditions

Decentralisation and Capacities grant will be apportioned across states based on each state's proportion of the total urban population, as per the 2011 Census. Within each state, the inter-city allocation of grants to individual ULGs should be proportional to their share of the state's total urban population.

To be eligible for this grant, states must meet the following conditions:

- i. States must have constituted SFCs and demonstrated progress on implementing SFC recommendations.
- ii. Additionally, to ensure predictability and transparency of fiscal transfers, states should publish ULG-wise transfer allocations under various budget heads as part of the state budget. This practice, already adopted by states like Karnataka, Bihar, and Assam, was also recommended by the XIII FC.

6.3.24 Operationalisation of the Grant

The grant will be disbursed in a single annual instalment every May, allocated on a per capita basis to eligible states. States must transfer the funds to ULGs within 10 working days of receipt to ensure timely utilisation. Unlike other performance-based grants, there will be no requirement for ULGs or states to submit utilisation reports, reducing administrative burden and allowing greater flexibility in fund deployment. However, to promote knowledge sharing and best practices, MoHUA will collect and publish innovative initiatives undertaken by states and ULGs under this grant, enabling peer learning.

07

XVI FC Grant Administration for Efficient and Accountable Spending



This chapter reimagines the digital administration of urban grants under the XVI Finance Commission (FC), building on lessons from the XV FC period. The analysis identifies core challenges across the grant lifecycle, from burdensome compliance processes to fragmented data systems and limited public visibility. The recommendations propose streamlined compliance and verification processes, real-time rolling disbursements, and comprehensive digital integration with public disclosure. These reforms are grounded in principles of fiscal autonomy, digital interoperability, and administrative ease to ensure timely, accountable, and effective utilisation of Finance Commission grants.

7.1 Background: Evolution of Grant Administration During the XV FC Award Period

The XV FC introduced a structured and systematic framework to manage the grant cycle, along with process-focused improvements. These included a workflow-based system that provided tracking and visibility of the compliance process. The adoption of a digital process with the CityFinance facilitated faster, data-driven decision-making around approval of grant claims from ULGs. Similarly, the use of Public Financial Management Systems (PFMS) by the XV FC advanced digital release and payment processing, allowing digital tracking of release and utilisation of grants across states.

These efforts by the XV FC on digital grant administration to improve efficiency and accountability marked a significant shift from the XIV FC, where grant administration remained primarily paper-based.

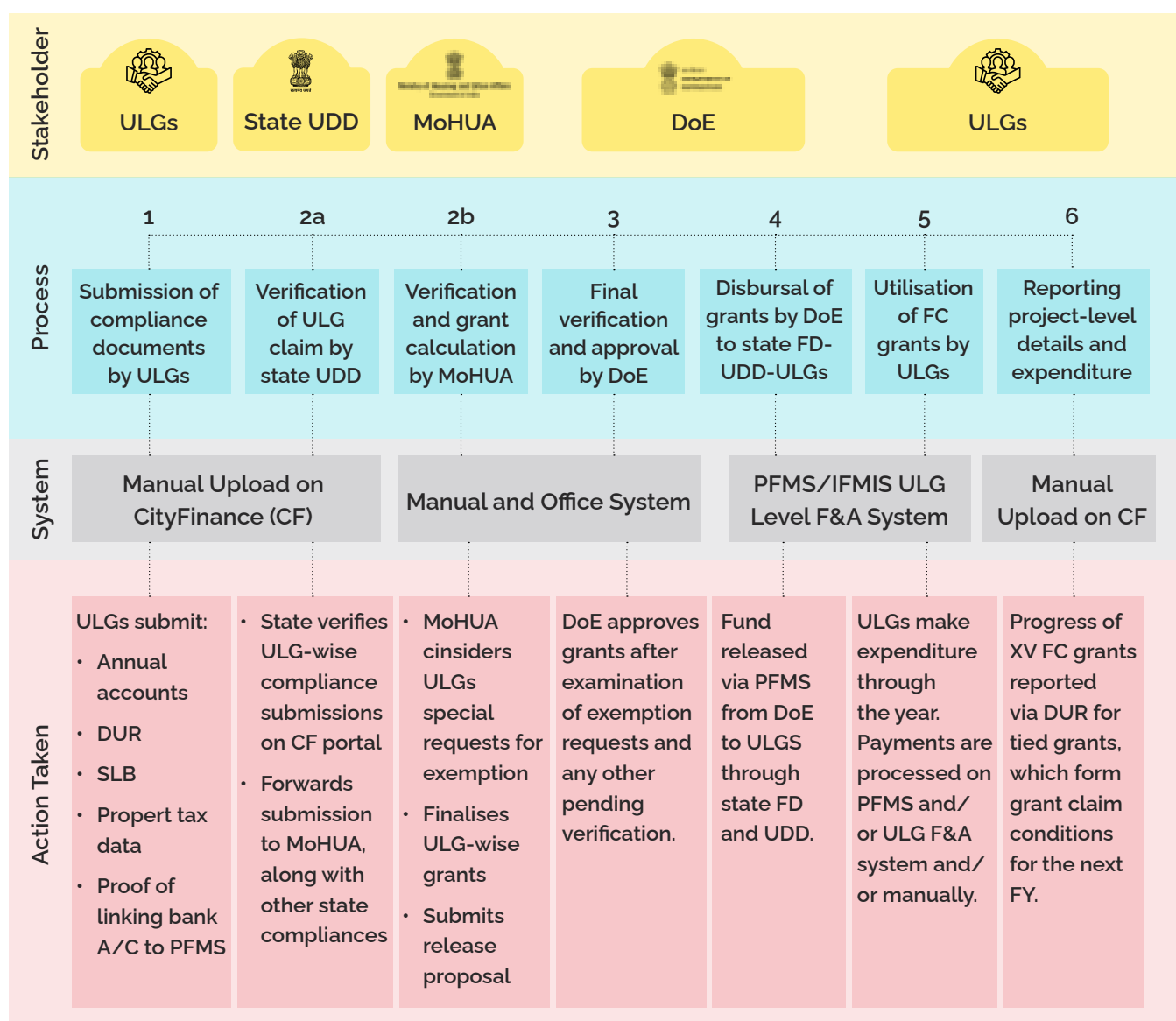


Figure 26: XV FC grant administration process mapping stakeholders and digital systems

The XV FC grant process comprises six steps outlined in Figure 26 and described below:

Step 1 - Compliance Reporting

The grant cycle starts with ULGs submitting compliance¹⁵⁹ related documents to the state Urban Development Department (UDD) on the CityFinance. This is based on the guidelines issued by the Department of Expenditure (DoE).

¹⁵⁹ Following are the documents to be submitted by Non-Million-Plus Cities (NMPCs): (1) Linking of ULG account with PFMS, (2) Grant Transfer Certificate, (3) Detailed Utilisation Report, (4) Publish Annual Accounts, (5) Publish Service Benchmarks, (6) Consistent improvement in Property Tax condition. Additionally, for Million-Plus Cities (MPCs): (1) SLB target achievement, (2) Submission of ODF and GFC Certificates, (3) Work Completion Certificate for mandatory projects undertaken.

Step 2 - Verification by UDD

The documents are verified and approved by the UDD following which the state makes a submission to MoHUA requesting grant release to ULGs. Typically, when most ULGs have met the conditions, the state submits a one-time grant release request for every instalment.

Step 3 - Verification and Grant Calculation

MoHUA then verifies the completeness of ULG compliance submissions and conducts a thorough check of state-level compliances¹⁶⁰.

Following verification and internal approvals, MoHUA calculates the ULG-wise grant allocation (or entitlement) based on the ULG's eligibility status. Requests from ULGs to be exempt from meeting certain conditions are also considered at this stage. For instance, newly transitioned ULGs may ask for exemption from meeting the condition of growth in property tax. MoHUA then submits a proposal for grant release to the DoE.

Step 4 - Approval and Disbursal of Grants

The DoE makes the final decision on grant release, including acceptance (or rejection) of ULG-specific requests for exemption¹⁶¹. There is significant coordination between the UDD, MoHUA, and DoE during this process before final approval. Once approved, grants are released to state governments (Finance Department and then UDD), who subsequently release them to ULGs using PFMS.

Step 5 - Expenditure by ULGs

ULGs either undertake expenditure directly or transfer funds to other implementation agencies (for instance, parastatals in the case of water supply in some states). Expenditure is processed through PFMS or the ULGs' Finance and Accounting (F&A) modules or manually (in some cases).

Step 6 - Reporting

ULGs then report on project-level details and financial progress from XV FC tied grants (in addition to their own record-keeping) through Detailed Utilisation Reports (DUR) prescribed by MoHUA. In addition, MPCs are required to submit work completion certificates. These become a part of grant claim conditions for the following financial year.

Each of these steps is critical to the grant cycle. Every step prior to grant release takes considerable time, creating a protracted process that undermines timely access to critical funding.

¹⁶⁰ State level compliances include GTC, list of duly elected ULGs and work completion certificates.

¹⁶¹ These requests typically refer to requests for exemptions from meeting conditions such as property tax collection growth for newly transitioned ULGs, having duly elected ULGs, among others.

7.2 Critical Challenges in XV FC Grant Administration

Despite digital advancements and streamlined processes, significant challenges were noted in the implementation of XV FC grants, particularly in grant release timeliness and in visibility across the grant cycle. These are reflected in the observations below:

1. **On average, ULGs (MPCs and NMPCs) received their grants 11.64 months after the start of the financial year.** In FY 2023-24 and 2024-25, most ULGs received their first instalment in February-March (near the end of the financial year), when they should have received it in June (third month of the FY).
2. XV FC grants had an annual allocation of ₹21,783 crore. Over five years, ₹65,952.36 crore was released to ULGs across states. For many ULGs, these grants remain the primary source of revenue for capital works.

However, this significant public investment cannot effectively be linked to on-the-ground service delivery outputs by ULGs, states, union government, or citizens. This represents a critical accountability gap, driven by the current self-reporting mechanisms for the XV FC grants.

The challenges observed above are rooted in a combination of structural, procedural, and technological factors. Chief among them is the high administrative burden placed on ULGs and state agencies, arising from limited use and interoperability of digital systems, overlapping processes, and multiple reporting requirements. Low levels of trust in ULG submissions leads to duplication of verification efforts, prolonging the grant release process. Additionally, existing systems do not provide a comprehensive, real-time view of the status of grant approval, release, utilisation, and physical progress, limiting predictability, accountability, and informed decision-making.

The following section elaborates on these challenges across every stage of grant administration.

7.2.1 Compliance Reporting

1. **The compliance process relies heavily on self-reporting and manually prepared documents by ULGs and the state.** For instance, the Grant Transfer Certificate (GTC) is manually prepared by the state rather than generated from PFMS. While certain documents can be machine-generated and directly uploaded through interoperable exchange protocols, information is typically entered or uploaded manually even where digital systems make automation feasible.

This manual approach results in several critical consequences:

- i. **Increasing administrative burden:** During the XV FC period, ULGs manually entered details relating to their property tax on CityFinance, even in states where digital systems could have automatically fetched DCB registers and related documents. This increased the workload of capacity-constrained ULG officials.
- ii. **Delayed compliance:** Manual processes significantly delay completion of compliance conditions, leading to overall delays in grant disbursement to ULGs.
- iii. **Data quality issues:** Submissions frequently contain errors and are of poor quality, making verification a lengthy process. Property tax growth rate data, for example, often contained errors such as incorrect entries (figures in thousands instead of lakhs) and missing entries. States sometimes identified these issues during verification, resulting in prolonged back-and-forth processes.

7.2.2 Verification by State UDD

1. **Inefficient and unreliable verification process results in delays:** State UDDs attempt to verify the accuracy of ULG submissions despite lacking reliable verification mechanisms. Without a unified source of truth for ULG submissions or established data validation standards, it is difficult to verify the substance or authenticity of submissions. For instance, state UDDs cannot easily verify whether every ULG has accurately reported property tax figures, yet considerable time and administrative effort is devoted to this verification process.
2. **Manual verification processes compound delays:** Existing processes to ensure completeness of documents are not automated. For instance, ensuring that all ULGs have submitted annual financial statements is currently manually verified, adding avoidable administrative effort and time.
3. **Absence of a rolling mechanism delays access for proactive ULGs:** The UDD typically waits for the majority of ULGs to submit their compliance documents before making a formal grant release request to MoHUA. This results in severe delays for proactive ULGs that complete compliance early in the year.

7.2.3 Verification and Grant Calculation by MoHUA

MoHUA verifies the completeness of compliance, calculates the ULG-wise grant allocation, and submits its fund release recommendations to the DoE for approval:

1. **Absence of standardised processes creates discretionary delays:** Well-defined SOPs or shared frameworks are lacking for key processes: final verification and approval of ULG grant submissions, consideration of exemption requests, and calculation of ULG-wise grant entitlements. There is little clarity on basic parameters, such as the source for updated lists of ULGs or grant calculation data (population, area, etc.). This absence of clear SOPs makes decision-making discretionary and time-consuming. It results in repeated back-and-forth between DoE, MoHUA, and state UDDs during final verification and approval processes.
2. **Limited digital systems undermine transparency and predictability:** Communication across union and state stakeholders during verification relies on phone calls, email exchanges, and e-Office systems. The lack of a digital trail on CityFinance reduces traceability of decisions and eliminates visibility for ULGs until they receive grants, undermining the effectiveness of fiscal transfers as a reliable instrument for capital planning and execution at the city level.

7.2.4 Approval and Disbursal of Grants by DoE

Once DoE approves grant release, grants flow through the State Finance Department, then the UDD, before reaching ULGs.

1. **Batch disbursal system discourages early compliance:** DoE releases grants to all qualifying ULGs in a state simultaneously rather than on a rolling basis. This delays funds to proactive ULGs and discourages early compliance.
2. **State-level bottlenecks delay final transfers:** Multiple layers of approval at the state level prevent ULGs from receiving grants within the stipulated 10-day period. This has been observed across multiple states. Despite the presence of digital systems like PFMS and IFMS, sanctioning and bifurcation of ULG-wise grants are often carried out through offline or partially manual processes. This reduces oversight for ULGs and union-level stakeholders while slowing fund flow due to additional manual processing time.

7.2.5 Expenditure by ULGs

1. **Fragmented payment systems prevent consolidated expenditure tracking:** Although ULGs are required to process FC payments (expenditure, advances, or transfers) through PFMS to ensure proper tracking and accountability, various challenges are observed on ground:
 - i. In some ULGs, a combination of PFMS and manual processing is used due to capacity constraints and system limitations. As a result, PFMS may not completely reflect total expenditure.

- ii. In some cases, ULGs process payments on their F&A systems and then re-enter information on PFMS, adding to their administrative burden.
- iii. In smaller ULGs or those with limited digital capacity, payments are processed manually, with data entered into PFMS as a post-facto formality, if at all.

7.2.6 Reporting by ULGs

ULGs report on project-level details and financial progress from XV FC tied grants.

1. **Current reporting mechanisms are unable to provide a real-time understanding on the quality of public expenditure. Key challenges include:**
 - i. **Lack of standard parameters for data capture related to expenditure and outputs at the ULG level prevents comprehensive understanding.** For instance, although PFMS is used for FC payments, the information captured at the point of payment processing is not adequate to provide a full picture of expenditure on different grant components, projects completed, or sector-wise expenditure.
 - ii. **Only a few states have systems in place to track financial and physical progress of projects in a unified manner.** Where they exist, inadequate exchange of information across different systems results in incomplete or fragmented visibility into the financial and physical outputs achieved. This undermines the ability of decision-makers to assess how funds are used, what services were delivered, and what course corrections are needed.
 - iii. **DURs (mandated for tied FC grants) are largely based on self-reported or manual, post facto data entry** into CityFinance. This results in duplicated efforts and project progress reports with low levels of trust. Additionally, DURs capture information on tied grants only, providing an incomplete picture of projects undertaken from FC grants.
2. **The absence of mandated public disclosure of compliance, expenditure, outputs and service level data limits external accountability. Without adequate information, it becomes difficult for citizens to evaluate the impact of FC grants on urban infrastructure and services.**

These existing challenges are a combination of (i) policy limitations, (ii) process and system inefficiencies, and (iii) limited human resource capacity¹⁶² to optimise the time and effort required at every stage of grant administration. The XVI FC has the opportunity to address all three challenges through a reimagined grant administration mechanism, discussed in the following section

¹⁶² Specifically, capability constraints have been observed on multiple fronts - (i) poor quality submissions from ULGs indicate gaps in data literacy, training, or understanding of compliance requirements; and (ii) limited use of digital systems (such as PFMS, IFMIS and CityFinance) at all levels were noted, due to lack of training, unfamiliarity, or usability issues.

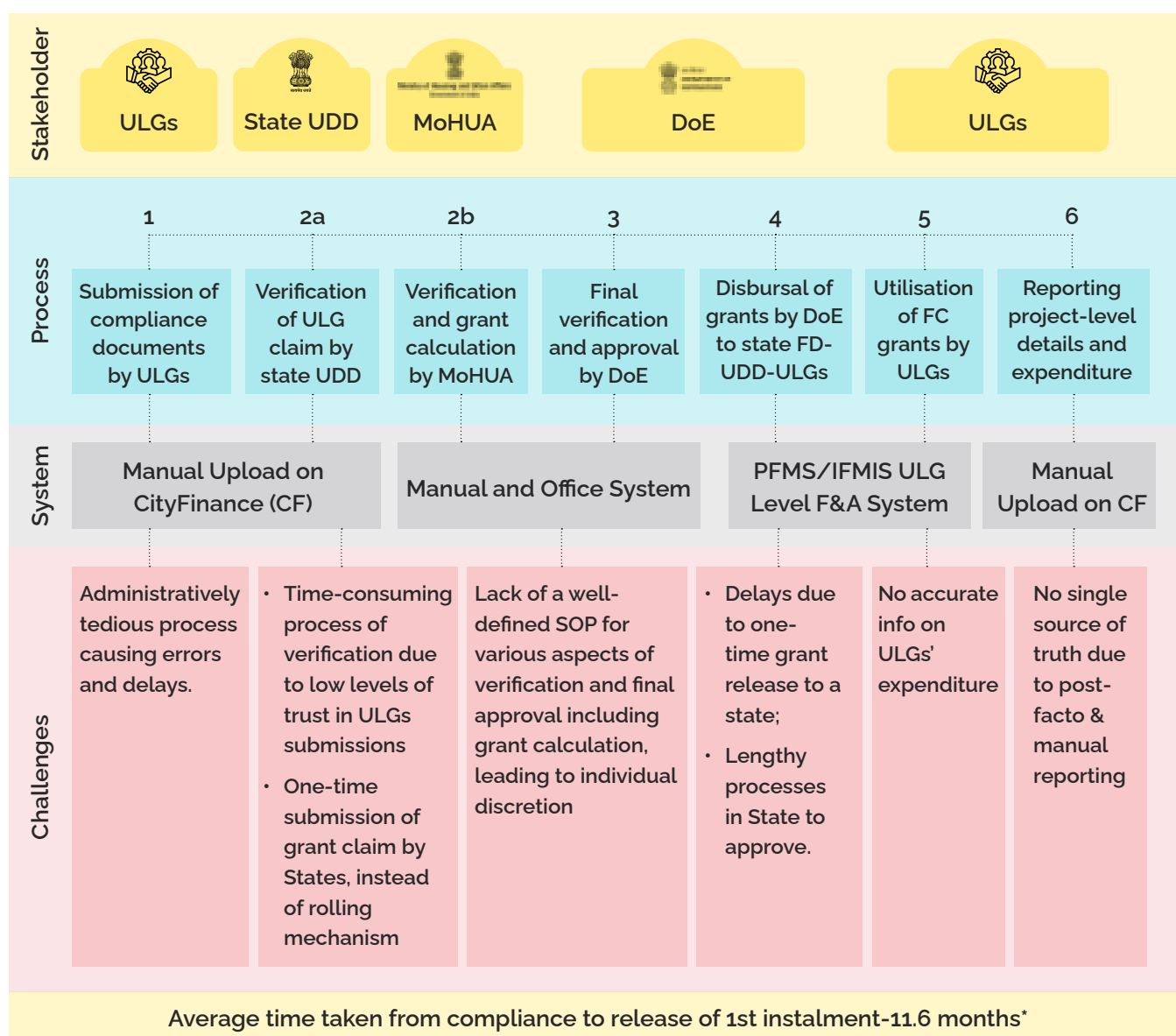


Figure 27: Overview of core issues faced in every stage of the XV FC grant cycle

7.3 Envisioning an Efficient and Effective XVI FC Grant Administration Mechanism: Recommendations and Pathways

ULGs play a critical role in delivering essential services to India's urban population. Delays in FC grant disbursement therefore directly impact infrastructure development and service quality. While multiple factors contribute to service delivery deficiencies, those related to public finance administration, particularly delayed releases and poor utilisation tracking, can and must be addressed by the XVI FC.

To this end, we recommend to design and operationalise an efficient digital grant administration system during the XVI FC award period. This system should enable timely release of grants and effective utilisation of funds, thereby contributing to improved urban service delivery.

With many ULGs increasingly adopting digital infrastructure for planning, budgeting, and execution, the XVI FC has a unique opportunity to recommend an end-to-end digital grant administration system. Such a system would enhance timeliness (in grant utilisation) through seamless workflows and strengthen real-time observability of public funds from outlays to outputs, empowering all stakeholders to make faster, better-informed decisions across the grant life cycle.

Three key recommendations follow to operationalise this approach. This includes proposals for policy, process, and system-level improvements that are based on a detailed mapping of FC grant processes and diagnostic assessments of digital systems in current use.

Recommendation 1: Establish a mechanism for rolling, automated transfers from the union to ULGs within 10 business days from the date of approval by the DoE. Shift from batch-based disbursements (based on submissions by states after most ULGs in the state qualify) to a continuous release model that rewards early compliance and improves fund flow predictability for ULGs. **Therefore, ULGs that make timely submissions should receive their first instalment in the first quarter of the financial year and second instalment in the third quarter.**

Recommendation 2: Mandate MoHUA & DoE to develop an end-to-end paperless digitalised grant administration system by building on the existing system on CityFinance. The digital grant administration system should have the following functionalities:

- a. **Simpler compliance and verification processes that eliminates duplication:**
 - (i) Automatic submission of compliances (Audited financial statements, Budgets, Service Level Indicators, Revenues, expenditure) through APIs from source systems such as PFMS, IFMS, Municipal Finance Systems; In case information is not available in source systems, provide a simple interface for ULGs to upload submissions. (ii) Documents submitted through APIs from trusted systems can be fast-tracked based on system checks, without any manual verification. In the case of manual, there should be clear SOPs on 'who' should verify the document (for e.g. state or MoHUA) and 'what' should be verified, along with a specification of time period for verification. During operationalisation, two-three states with higher levels of digital maturity can be chosen as pilot states to implement re-engineered compliance and verification processes. (iii) All other processes such as 'calculation of ULG-wise grant allocation' and processing of grant claims (by MOHUA and DOE) should be system enabled.
- b. **Streamlined processes of grant release and expenditure:**
 - (i) Improvements to CityFinance and PFMS to allow ULGs to track status of grant verification and release of funds in real-time. (ii) At union and state level, generation of sanction order and payment instruction through PFMS or state IFMS; (iii) At ULG level, process all payments relating to FC grants through PFMS (or ULGs' F&A systems with interoperability) and ensure capture of key financial and project level information¹⁶³ at the time of payment processing.
- c. **Real-time observability (or trackability) through:**
 - (i) Establishment of policies that support interoperable systems, open APIs and other related system design principles critical to improve grant administration; and (ii) corresponding system improvements to facilitate machine to machine exchange of relevant information¹⁶⁴, based on pre-determined data standards. This will be aimed at establishing a 'single source of truth' and eliminating multiple sources for the same information.

Recommendation 3: Mandate complete public disclosure of information across the XVI FC grant lifecycle, on a dashboard on CityFinance to enable accountability and performance-based dialogue. This will include disclosure of (i) status of grant from recommendation to utilisation – to include grant, allocation, status of compliance, grant released, expenditure occurred; and (ii) list of completed and ongoing projects and/or works, including status of completion and other attributes outlined in recommendation 2.b.

Recent advances in public financial management across union, state, and local governments support the viability of these recommendations. The Ministry of Panchayati Raj has demonstrated the effectiveness of key elements underlying Recommendations 2 and 3 for rural local governments (Refer to Box 7). Additionally, platforms supporting Direct Benefit Transfers have proven India's

¹⁶³ Project details will include: Project ID, name of project, geo-location, sector, size/ capacity, tendered amount, actual expenditure, status of project/stage of completion (approved, ongoing, and completed), contractor name, date of completion and photos.

¹⁶⁴ Amongst CityFinance, PFMS, IFMS, municipal finance & accounts systems, property tax systems etc.

capacity to deliver funds to millions of beneficiaries in real time.

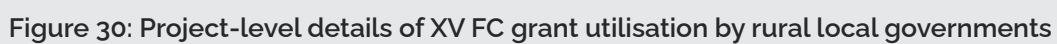
These precedents confirm that extending transparent, timely transfers to 4,800 ULGs is achievable. Existing systems —such as CityFinance, PFMS, ULG finance and accounting modules, and initiatives under the National Urban Digital Mission — provide the foundation for this evolution.

Box 7: e-Gramswaraj - The Ministry of Panchayati Raj's Digital Grant Framework

The Ministry of Panchayati Raj's e-Gramswaraj platform is a digital grant administration model that integrates information gathering, micro-level planning, expenditure tracking, and work-based accounting for Gram Panchayats (GPs).

The platform serves 2.7 lakh GPs across 28 states and 6 union territories. Through automated data exchange, e-Gramswaraj enables preparation of Gram Panchayat Development Plans (GPDPs), tracking of physical and financial progress, and real-time monitoring of FC grant utilisation alongside union and state schemes. Moreover, the system ensures public disclosure of this information, showing how budget allocations translate to actual outputs (see screenshots below). The transparency and accountability standards set by e-Gramswaraj can be replicated at the ULG level.

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The recommendations in this chapter are grounded in an understanding of ULGs' context within the federal framework and a recognition of their constitutional position as an independent third tier of government. Operationalising these recommendations requires coordinated action across multiple systems and stakeholder levels:

- i. **Design a unified framework for standards-based¹⁶⁵ digital grant management** that enables real-time data exchange across existing ULG, state, and union systems (to include CityFinance, PFMS, IFMIS, municipal finance & accounts systems, property tax systems, among others).
- ii. **Implement targeted upgrades to CityFinance, PFMS, and state-level and ULG-level systems** to enable interoperability and automated data exchange.
- iii. **Redesign grant cycle processes to eliminate redundancies and reduce administrative burden** by assessing each stakeholder's role and value addition.
- iv. **Issuing clear guidance to states and ULGs on adopting digital workflows** while accommodating varying levels of digital system maturity during the transition.
- v. **Strengthening of capabilities at different tiers of the Government** through:
 - a. Upskilling officials on digital workflows at ULG, state, and MoHUA levels, focusing on improved uptake of system-driven compliance and verification (better use of CityFinance, PFMS) and consistent understanding of standard operating procedures.
 - b. Incentivising early submissions by ULGs and states.
 - c. Strengthening data literacy and trust through quarterly audits comparing system-generated versus manual records, publishing results, and refining verification processes.
- vi. At the Union level, **Ministry driven institutionalised governing mechanisms to deliver on envisioned reforms** – this will include steering committees and technical working groups that are tasked with specific responsibilities to build and operationalise a system that aligns with the vision of timely grant release, timely utilisation and reliable data across the grant lifecycle.

Building on the discussion so far, Table 28 outlines the processes for key stages of the grant lifecycle. These should be detailed and operationalised at the point of initiation of the XVI FC award period.

¹⁶⁵ Standards enable comprehensible information exchange, while ensuring and respecting ULG autonomy and agency.

Table 27: Proposed Process Reforms for XVI FC Grant Administration**Streamlining compliance and verification processes –**

1. For compliance:
 - a. Deploy system-generated prompts to ULGs and states for timely compliance with grant conditions, such as automated reminders for audit deadlines.
 - b. Adopt differentiated approaches based on state and ULG digital maturity. In states where ULGs have adopted digital finance systems, audited financial statements, budgets and other documents can be directly uploaded through system-to-system interoperability, reducing administrative burden, enhancing data trust, and accelerating verification processes. Simple upload options can be provided on CityFinance where automated uploads are not feasible.
2. For verification: Institute a differentiated approach of automated vs. manual verification tracks
 - a. Automated verification should trigger immediate system approval when conditions are met. Manual verification will require clear standard operating procedures specifying responsible parties (state or MoHUA), verification scope, and time limits.
 - b. To illustrate, for Category I ULGs (population below 500,000), submissions such as budgets, audited financial statements, and service level benchmarks¹⁶⁶ can be auto-verified on CityFinance, as their compliance is confirmed simply by the presence or absence of documents. In such cases, additional manual checks add little value, and the priority should be timely verification and approvals. For Category II and III ULGs, a differentiated approach is required: routine documents can be system-verified, while more complex submissions can undergo manual verification.
3. Once verified (automatic or manual), CityFinance displays green-tick indicators to show qualifying ULGs. These indicators should be visible to ULGs and trigger grant entitlement calculation and final approval processes.
4. For qualifying ULGs, the system will calculate entitlement amounts using a 'grant calculation formula' on CityFinance that draws population, area, and other parameters from single sources of truth, such as the local government directory for updated ULG lists and other designated sources for population and area data.
5. MoHUA and DoE will provide final approval – this will be based on clear standard operating procedures and rules enabling consistent decisions on qualifying ULGs and exemptions from conditions. These rules should be codified into the system to enable automated decisions where feasible.
6. Lastly, the verification, grant calculation, and final approval process requires:
 - a. Digital tracking of all decisions, including exemptions for ULGs unable to meet certain conditions, visible to all stakeholders.
 - b. Formal mechanisms for swift resolution of pending grant approval matters.

¹⁶⁶ Budget (instalment 1), AFS and SLBs (instalment 2) are the list of documents to be submitted by category 1 ULGs to qualify for FC grant. Reference in table 16 of chapter 5.

Instituting a continuous rolling mechanism for verification and release of grants –

1. Approval of ULG submissions individually (automatically or manually), rather than waiting for batch submissions. Aimed at timely release, this will be a key departure from XV FC practice. Once verified on CityFinance, ULGs are eligible and need not wait for others in the state to qualify.
2. DoE will release funds individually to qualifying ULGs through PFMS-initiated transfers within 10 business days of approval, replacing batch releases. PFMS should be enhanced to enable visibility of grant release to all levels of government.
3. State Finance Departments should ensure that once funds are received from the DoE, transfers to ULGs are made within stipulated timeframes through streamlined and verifiable processes. This can be enabled by codifying pre-defined instructions, introducing automated sanction orders, and eliminating manual redundancies to the extent possible.

Strengthening expenditure processes –

1. Enhance PFMS and ULGs' finance and accounting systems to provide comprehensive expenditure visibility on every FC grant component through:
 - a. Digital processing of all XVI FC grant payments by ULGs or any other implementing agencies (for instance, parastatals).
 - b. Clear definition of attributes/parameters to be captured during payment processing.
 - c. System improvements to PFMS (where it is the primary system) for accurate capture of all FC grant expenditure.
 - d. Capture of project-level information in real-time during payment processing to eliminate manual and post-facto reporting . This will require improvements to PFMS as well as ULG finance and accounting systems and/or work management modules.

Annexure



Annexure 1.1: Urban and Rural Local Governments Covered During Field Visits

Sl. No.	ULG	State
1	Golakganj Municipal Board	Assam
2	Jamugurihat Municipal Board	Assam
3	Goalpara Municipal Board	Assam
4	Hutti Town Panchayat	Karnataka
5	Kavital Town Panchayat	Karnataka
6	Maski Town Municipal Council	Karnataka
7	Shamshabad Municipality	Telangana
8	Pedda Amberpet Town Panchayat	Telangana
9	Greater Hyderabad Municipal Corporation	Telangana
10	Greater Chennai Corporation	Tamil Nadu
11	Poonamallee Municipality	Tamil Nadu
12	Bhopal Municipal Corporation	Madhya Pradesh
13	Madhusudangarh Town Panchayat	Madhya Pradesh
14	Mandideep Municipal Coucil	Madhya Pradesh
15	Shimla Municipal Corporation	Himachal Pradesh
16	Kandaghat Town Panchayat	Himachal Pradesh
17	Parwanoo Municipal Council	Himachal Pradesh
18	Kaiserganj Nagar Panchayat	Uttar Pradesh
19	Mohanlalgarh Town Panchayat	Uttar Pradesh
20	Achalgarh Town Panchayat	Uttar Pradesh
21	Lambhua Nagar Panchayat	Uttar Pradesh
22	Hindol Notified Area Council	Odisha
23	Ranpur Notified Area Council	Odisha

Sl. No.	RLG	State
1	Bakaitari Gram Panchayat	Assam
2	Belma Gram Panchayat	Karnataka
3	Talapady Gram Panchayat	Karnataka
4	Konaje Gram Panchayat	Karnataka
5	Kakori	Uttar Pradesh

Annexure 2.1: Definition of Statutory Towns Across 28 States in India

Sl.No.	State	Large Urban Area	Smaller Urban Area	Transitional Urban Area
1	Arunachal Pradesh	- Area with population 75,000 and above - At least 85% employment in non-agricultural activities	- Area with population between 25,000 and 74,999 - At least 85% employment in non-agricultural activities	- Area with population less than 25,000 - At least 85% employment in non-agricultural activities
2	Bihar	- Area with population 2,00,000 and above - At least 75% employment in non-agricultural activities	- Area with population between 40,000 and 1,99,999 - At least 75% employment in non-agricultural activities	- Area with population between 12,000 and 40,000 - At least 75% employment in non-agricultural activities
3	Goa	There are three types of municipal areas based on population size: Class A (more than 50,000), Class B (10,001–50,000), and Class C (less than 10,000). However, these classifications do not correspond to the categories of large, small, and transitional urban areas as outlined in the Constitution.		
4	Haryana	Area with population above 3,00,000	Area with population between 50,001 and 3,00,000	Area with population 50,000 and less
5	Himachal Pradesh	- Area with population more than 50,000 - At least ₹2,00,00,000 annual tax or non-tax revenue	- Area with population more than 5,000 - At least ₹10,00,000 annual tax or non-tax revenue	- Area with population more than 2,000 - At least ₹5,00,000 annual tax or non-tax revenue
6	Jharkhand	Area with population 1,50,000 and above	Area with population between 40,000 and 1,49,999	Area with population between 12,000 and 39,999
7	Karnataka	- Area with population above 3,00,000 - Density of population 3,000 per sq km - At least ₹6,00,00,000 annual tax or non-tax revenue or ₹200 per capita p.a. whichever is higher - At least 50% employment in non-agricultural activities	- Area with population between 20,000 and 3,00,000 - Density of population 1,500 per sq km - At least ₹9,00,000 annual tax or non-tax revenue or ₹45 per capita p.a. whichever is higher - At least 50% employment in non-agricultural activities	- Area with population between 10,000 and 19,999 - Density of population 400 per sq km - At least 50% employment in non-agricultural activities
8	Kerala	The Governor may have regard to the population of the area, the density of the population therein, the revenue generated for local administration, the percentage of employment in non-agricultural activities, the economic importance or such other factors as he may deem fit, specify by public notification [the urban areas] under the Acts.		
				- Area with population more than 20,000 - Density of population 4,000 per 2.59 sq. km. - At least ₹ 5 per capita per annum - More than 75% employment in non-agricultural activities

Sl.No.	State	Large Urban Area	Smaller Urban Area	Transitional Urban Area
9	Maharashtra	Area with population 3,00,000 and above	- Area with population 25,000 and above. - At least 35% employment in non-agricultural activities	- Area with population between 10,000 and 25,000. - At least 25% or 50% employment in non-agricultural activities depending on proximity to a large town¹⁶⁷
10	Mizoram	Area with population 5,00,000 and above	Area with population 1,50,000 and above	Area with population 10,000 and above
11	Nagaland	The Act specifies three types of municipal areas on the basis of population size: 1. Municipal Council (20,000 or more), 2. Town Council (20,000 or more), 3. Urban Station Committee Area (population between 1,000 and 4,999)		
12	Odisha	Area with population 3,00,000 and above	Area with population 25,000 and above	Area with population 10,000 and above
13	Sikkim	- Area with population 70,000 and above. - At least 50% employment in non-agricultural activities	- Area with population between 5,000 and 69,999. - At least 50% employment in non-agricultural activities	- Area with population less than 5,000. - At least 50% employment in non-agricultural activities
14	Tamil Nadu	Article 243Q of the Constitution	Article 243Q of the Constitution	Area with population 30,000 and above
15	Telangana	- Area with population 3,00,000 and above. - Density of population 5,000 per sq km.	- Area with population between 40,000 and 3,00,000. - Density of population 500 per sq km. - At least ₹60,00,000 annual tax or non-tax revenue - At least 40% employment in non-agricultural activities.	- Area with population between 20,000 and 40,000. - Density of population 400 per sq km - At least ₹40,00,000 annual tax or non-tax revenue. - At least 25% employment in non-agricultural activities.

¹⁶⁷ 25% and more in non-agricultural employment if less than 20 kilometres away from a Municipal Corporation or a Class A Municipal Council, or 50% and more in non-agricultural employment if less than 20 kilometres away from a Municipal Corporation or a Class A Municipal Council.

Sl.No.	State	Large Urban Area	Smaller Urban Area	Transitional Urban Area
16	Tripura	• Area with population 5,00,000 and above. • Density of population 500 per sq km. • More than 50% employment in non-agricultural activities.	• Area with population 50,000 and more. • Density of population 500 per sq km. • More than 50% employment in non-agricultural activities.	• Area with population less than 50,000. • Density of population 500 per sq km. • More than 50% employment in non-agricultural activities.
17	West Bengal	• Area with population 5,00,000 and above • Density of population 3,000 per sq km • More than 75% employment in non-agricultural activities	The government may declare any town as a municipal area if it meets the following criteria: a population of 30,000 or more, a population density of at least 750 per sq km, and more than 50% employment in non-agricultural activities	
18	Andhra Pradesh	In accordance with Article 243Q of the Constitution, the governor may, by public notification, specify the areas to be classified as urban under the relevant Acts, taking into consideration factors such as: the population of the area, its population density, revenue generated for local administration, the percentage of employment in non-agricultural activities, economic importance, or such other factors as may be deemed appropriate.		
19	Chhattisgarh			
20	Gujarat			
21	Madhya Pradesh			
22	Manipur			
23	Punjab			
24	Rajasthan			
25	Uttar Pradesh			
26	Uttarakhand	No criteria specified; no reference to Article 243Q of the Constitution		
27	Meghalaya			
28	Assam			

Source: Assessment of 82 municipal acts across 35 states/UTs as of 1 March 2023. Data for Kerala has been taken from G.O MS 108/67/HLD dt.2nd March 1967

Notes:

1. Union territories have been excluded from this analysis as their municipal acts have no criteria specified for statutory towns.
2. In Arunachal Pradesh, Bihar, and Jharkhand, the state government may, by notification, prescribe separate conditions for declaring certain areas, such as hill regions, pilgrim centres, tourist destinations, or mandis, as municipal areas.
3. In Jharkhand, a Smaller Urban Area (Municipal Council) is further categorised into Class A (population between 1,00,000 and 1,49,999) and Class B (population between 40,000 and 99,999). The state government may, by notification, declare any area a Nagar Panchayat, irrespective of population size, taking into consideration factors such as economic importance and other factors it deems fit.

4. In Karnataka, a district headquarters and a taluk headquarters may be designated as a Smaller Urban Area and a Transitional Urban Area respectively, even if their population falls below the prescribed threshold. A Smaller Urban Area is further classified into a City Municipal Council (population of 50,000 or more) and a Town Municipal Council (population between 20,000 and 49,999).
5. In Maharashtra, a Smaller Urban Area is further classified into Class A (population above 1,00,000), Class B (population between 40,001 and 1,00,000), and Class C (population of 40,000 or below). The state government may, by notification, declare a district headquarters or a taluk headquarters as a Transitional Area.
6. In Mizoram, a town with a population of less than 10,000 may still be designated as a Transitional Area and shall not be barred from such classification solely on the basis of population.
7. In Sikkim, for the purpose of classifying municipal areas located in eco-sensitive zones, tourist centres, pilgrim centres, or bazaars of any class, the governor may, by notification, prescribe separate population thresholds for each category of such municipal areas.
8. In West Bengal, municipal areas are further classified into Group A (population above 2,15,000), Group B (population between 1,70,001 and 2,15,000), Group C (population between 85,001 and 1,70,000), Group D (population between 35,001 and 85,000), and Group E (population of 35,000 or below). The state government may, by notification, prescribe separate conditions for classifying certain areas, including hilly regions, as a municipal area or municipal corporation.

Annexure 2.2: Areas Exempt from the 74th Constitutional Amendment Act

Sixth Schedule Areas	Cantonment Boards	Industrial Townships
Under the Sixth Schedule of the Constitution, tribal areas in Assam, Meghalaya, Mizoram, and Tripura have special autonomy. These regions are governed by Autonomous District Councils (ADCs), which possess extensive legislative, judicial, executive, and financial powers. ADCs can establish village or town committees, making them exceptions to the application of Part IX-A of the Constitution. Governance practices, however, vary: while the Karbi Anglong ADC in Assam conducts regular elections, the Dima Hasao ADC (also in Assam) does not. ADCs in Mizoram and Meghalaya have not held elections despite the presence of Town Committee Acts, whereas Tripura's ADCs conduct them regularly.	Cantonment Boards are local bodies established under the Cantonments Act, 2006, to oversee the governance of cantonment areas. Each cantonment is administered by the Ministry of Defence and governed by a Cantonment Board comprising elected members and ex-officio military officers. The Officer Commanding the station serves as the President of the Board, while other members include the District Magistrate or an Executive Magistrate, the Chief Executive Officer, Health Officer, Executive Engineer, military officers, and elected representatives. The number of elected members and military officers varies based on the category of the cantonment. Currently, there are 61 Cantonment Boards in the country.	Under Article 243Q, states can designate industrial areas as 'industrial townships', allowing industries to provide municipal services. Introduced late in the 74th Constitutional Amendment, this provision enables private local governance. These areas appear in the Census under different names: Industrial Notified Areas (26 in Gujarat); Industrial Townships (2 in Odisha, 5 in Uttar Pradesh, 2 in Uttarakhand, and 1 in West Bengal); and Notified Area Committees (2 in Jharkhand and 7 in Karnataka). Industry representatives and state officials are involved in the governance of these townships. Till 2009, Gujarat's industrial notified areas included panchayat representatives.

Annexure 2.3: State-wise Distribution of ULGs Constituted Since the 2011 Census

SL.No	States	Number of ULGs	Population as per 2011 Census
1	Andhra Pradesh	43	17,28,234
2	Arunachal Pradesh	7	48,887
3	Assam	16	1,80,408
4	Bihar	128	32,08,481
5	Chhattisgarh	5	1,49,018
6	Gujarat	3	81,095
7	Haryana	13	4,47,146
8	Himachal Pradesh	11	59,276
9	Jharkhand	10	3,34,974
10	Karnataka	98	18,88,839
11	Kerala	35	15,56,508
12	Madhya Pradesh	56	9,45,673
13	Maharashtra	172	29,81,550
14	Nagaland	20	94,978
15	Odisha	12	1,91,777
16	Punjab	26	2,91,604
17	Rajasthan	115	43,96,304
18	Tamil Nadu	1	16,784
19	Telangana	101	32,43,112
20	Tripura	4	63,253
21	Uttar Pradesh	137	31,48,172
22	Uttarakhand	39	4,05,909
23	West Bengal	5	2,11,242
	Total	1057	25,673,224

Source: CityFinance as on 30-06-2025.

Annexure 2.4: State Provisions for Transitional Areas

- i. The Gujarat Town Planning and Urban Development Act, 1976 identified 'Transitional Areas' as areas undergoing urbanisation, designated within development plans and Town Planning Schemes (TPS)¹⁶⁸.
- ii. In Maharashtra, specific regions transitioning to urban areas are designated as 'notified areas' under the Maharashtra Regional and Town Planning Act, 1966. Special Planning Authorities are established to manage development and infrastructure in these transitional zones.
- iii. Tamil Nadu was the first state to introduce the transitional classification of 'Town Panchayats' under the Tamil Nadu Urban Local Bodies Act, 1998, as an intermediary form between rural and urban local governments¹⁶⁹.
- iv. The Rajasthan Municipalities Act, 2009 classifies areas showing urban potential as transitional.
- v. The Andhra Pradesh Municipalities Act, 1965 defines a 'transitional area' or a 'smaller urban area nearing urban thresholds' as notified and brought under special urban planning regulations.
- vi. In Madhya Pradesh, transitional zones are managed as Nagar Panchayats, which combine rural and urban administrative features. Section 5 of the Madhya Pradesh Nagar Palika Act, 1961 and departmental notification No. 64-F-1-19-2009-Eighteen-3 dated 27 December 2011 outline the criteria for transition.

¹⁶⁸ Urban Development and Urban Housing Department, Government of Gujarat. (1976). The Gujarat Town Planning and Urban Development Act, 1976. https://townplanning.gujarat.gov.in/Documents/GTPUD/GTPUD_act_1976_English.pdf

¹⁶⁹ Government of Tamil Nadu. (n.d.). Department of Town and Country Planning: Introduction. <https://www.tn.gov.in/dtp/introduction.htm>

Annexure 2.5: Criteria for Declaring Transitional Areas in State Laws and Notifications

State	Legislations	Criteria
Madhya Pradesh	Section 5 of the Madhya Pradesh Nagar Palika Act, 1961 and departmental notification No. 64-F-1-19-2009-Eighteen-3 dated 27 December 2011 (refer Annexure 2.5.1)	i. Population of at least 20,000, with 60% of the area densely populated. ii. At least 50% of the population engaged in non-agricultural activities. iii. 30% of total buildings liable for property tax, with annual rental values of ₹4,800 or more. iv. Comprehensive water supply throughout the area. v. Higher revenue from markets and animal markets compared to nearby GPs. vi. A GP office building capable of accommodating 20 employees and 15 councillors. vii. At least 30% of roads and drains paved. viii. Adequate street lighting with electric poles installed in most areas.
Himachal Pradesh	Himachal Pradesh Municipal Act 1994	i. Population exceeding 2,000 ii. Annual revenue exceeding ₹5,00,000
Tamil Nadu	Tamil Nadu Urban Local Bodies Act, 1998	i. Population more than 10,000 ii. Density of the population iii. Percentage of employment in non-agriculture activities iv. Revenue generated more than ₹30,00,000 v. Economic importance

Annexure 2.5.1: Madhya Pradesh Government Notification No. 64-F-1-19-2009-eighteen-3 Dated 27 December 2011 to Identify Transitional Areas

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मध्यप्रदेश राजपत्र

(असाधारण)

प्राधिकार से प्रकाशित

पंचम, मंगलवार, दिनांक 27 दिसम्बर 2011—पृष्ठ 4, भाग 1933

क्रमांक 164)

नगरीय प्रशासन एवं विकास विभाग
मंत्रालय, बल्लभ धवन, भोपाल
भोपाल, दिनांक 27 दिसम्बर 2011

अभिप्रेत क्र. 64-एच-1-19-2009-आठवीं-3.—मध्यप्रदेश नगरपालिका अधिनियम, 1961 की धारा 5 में नगर परिषद् के लिए स्थापना योग्य क्षेत्र तथा नगरपालिका के लिए अनुसूचित नगरीय क्षेत्र एवं पंचायतों के लिए नगर पालिका अधिनियम, 1956 की धारा 2 में नगर पालिका के लिए नगरीय क्षेत्र के गठन का प्रावधान है।

2. उक्त अधिनियम द्वारा दिये गये निर्देश अनुसार नगर पालिका/नगरपालिका/नगर विभाग के गठन का मापदण्ड जनसंख्या के आधार पर निम्नप्रकार निर्धारित किया जाता है:—

नगर परिषद्	—	20,000 से अधिक 50,000 से कम जनसंख्या
नगरपालिका	—	50,000 से अधिक 3,00,000 से कम जनसंख्या
नगर पालिका विभाग	—	3,00,000 से अधिक जनसंख्या

इसके अतिरिक्त संक्रमणशील क्षेत्र के गठन हेतु निम्न मापदण्डों को ध्यान में रखा जाना है:—

- जनसंख्या 20 हजार से कम न हो, इसमें से जनसंख्या का 60 प्रतिशत अपने जनसंख्या हो।
- प्रशासनिक विकास में पूर्ण रूप पर निर्भरतापूर्ण संरक्षित हो तथा इन प्रतिबंधों में 50 प्रतिशत जनसंख्या शामिल हो।
- परिचित होने वाली विकास का स्तर का समान रूप से कम करने 10 लाख प्रतिवर्ष हो।
- प्रशासनिक विकास में निम्न कुल धन में से 30 प्रतिशत नगर पालिका की परिधि में आते हैं। अवधि 10 लाख प्रतिवर्ष प्रतिवर्ष 4000.00 रुपये से कम न हो।
- प्रशासनिक विकास के पूरे क्षेत्र में नगर प्रदाय किया जा रहा हो।
- प्रशासनिक विकास में लाने वाले आधार, पक्का बाजार, आवा-पान की अन्य साम संसाधनों की पूर्णता में अधिक उद्योग देने वाले हो।
- उक्त मापदण्ड का उल्लंघन का ध्यान होता यदि 10 वर्ग किलोमीटर क्षेत्र में अधिक 15 वर्ग किलोमीटर का क्षेत्र।
- प्रशासनिक विकास में कुल सड़कों की लंबाई की 30 प्रतिशत सड़क/परिधि पर सड़कें होना चाहिए।
- विशुद्ध जनसंख्या के अतिरिक्त विकास के अधिकतर क्षेत्र में विशुद्ध रूप से स्थापित हो।

मध्यप्रदेश के राज्यपाल के नाम से तथा अधीनस्थ,
सुभाष चंद्र बोस, प्रमुख अधिकारी, प्रमुख अधिकारी

1167

नियंत्रण, सार्वजनिक सुलभ एवं संयोजन, मध्यप्रदेश द्वारा नगरपालिका के लिए अनुसूचित, भोपाल में प्रतिष्ठित तथा प्रकाशित—2011

Annexure 2.6: Per Capita Revenue and Expenditure Comparison Between ULGs and RLGs in Tamil Nadu (2021–22)

Local Government	RLG	RLG - Per Capita (INR)	ULG	ULG - Per Capita (INR)
Name	Thathankuttai		Aalampalayam TP	
Population	24,708		20,286	
District	Namakkal		Namakkal	
Own Revenue Receipts (INR)	46,18,441	187	2,67,56,162	1,319
Central Finance Commission (INR)	1,66,23,774	673		
State Finance Commission (INR)	1,38,37,218	560		
Other Receipts (INR)	1,38,99,446	563	2,71,13,879	1,337
Total Receipts (INR)	4,89,78,879	1,982	5,38,70,041	2,656
Revenue Expenditure (INR)	1,90,42,649	771	6,17,61,760	3,045
Capital Expenditure (INR)	11,06,813	45	9,64,31,561	4,754
Total Expenditure (INR)	2,01,49,462	816	15,81,93,321	7,798

Source: Financial data for RLGs for the year 2021–22 was provided by the Ministry of Panchayati Raj (MoPR) to the XVI Finance Commission, as shared on 07-01-2025. Corresponding data for ULGs for the same year has been sourced from the CityFinance.

Annexure 2.7: Notification Declaring the Merger of Madhusudangarh

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से भी डाउन लोड किया जा सकता है.



मध्यप्रदेश राजपत्र

(असाधारण)

प्राधिकार से प्रकाशित

अंक 124] भोपाल, मंगलवार, दिनांक 20 फरवरी 2018—भाग 1, भाग 1999

नगरीय विकास एवं आवास विभाग
मंत्रालय, वस्तीय भवन, भोपाल
भोपाल, दिनांक 20 फरवरी 2018

सवि. अ. 7-एन-1-51-2017-अंश-3—मध्यप्रदेश नगरपालिका अधिनियम, 1961 (अंक 37 भा. 1961) की धारा 5 (1) (ख) में उक्त अधिनियम के प्रयोग में लाते हुए, ग्राम पंचायत, मधुसूदनगढ़ को निम्न खाली में निर्दिष्ट क्षेत्र को जोड़ कर पंचसद मधुसूदनगढ़ अधिसूचित किया जात है:—

क्र. (1)	जिला (2)	तहसील (3)	ग्राम पंचायत का नाम (4)	संश्लिष्ट क्षेत्र/क्षेत्रों का विवरण (5)
1.	रुम	मधुसूदनगढ़	1. मधुसूदनगढ़	1. मधुसूदनगढ़
			2. नलखेड़ा	2. नलखेड़ा
			3. कोल्लार	3. कोल्लार
			4. कौटेर	4. कौटेर
			5. पारसीय	5. पारसीय
				6. मिथौरिया
				7. गैर
			6. डोई	8. डोई
				9. राहीपुर

मध्यप्रदेश के राज्यपाल के नाम से तथा आदेशानुसार,
राजीव मिश्र, सचिव.

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निर्देश, आसानीय भुगतान एवं सेवाएं प्रदायी, आसानीय एवं आसानीय केटीय सुदृष्टताएं, भोपाल के मुद्रित एवं प्रकाशित - 2018.

Annexure 2.8: Gazette Notification of the Transition of Pedda Amberpet and Shamshabad in Telangana

4 TELANGANA GAZETTE EXTRAORDINARY [Part IV-B]

Short title and commencement.	1. (1) This Ordinance may be called the Telangana Municipalities (Amendment) Ordinance, 2024. (2) It shall come into force at once.
Amendment of Schedule-I	2. In the Telangana Municipalities Act, 2019, in Schedule-I,
(Act No. 11 of 2019).	(1) under the Heading "XV RANGA REDDY", against the Sl.Nos.43, 47, 50 and 53 the following shall be substituted in the respective columns, namely,-

Sl. No.	Name of the District	Name of the Municipality	Number of Wards
(1)	(2)	(3)	(4)
*43		Pedda Amberpet (including Bacharam, Gowrelly, Quthbullapur and Tharamathipet Grampanchayats)	24
47		Shamshabad (including Bahadurguda, Peddagolkonda, Chinnagolkonda, Hamidullanagar, Rasheedguda and Ghansimiyaguda Grampanchayats)	25
50		Narsingi (including Mirjaguda Grampanchayat)	18
53		Thukkuguda (including the Harshaguda Grampanchayat)	15"

Annexure 2.9: Percentage Share of Urbanisation Premium to States under Methods 1, 2 and 3

State	Method 1 (i)	Method 1 (ii)	Method 2	Method 3
	Projected urban population 2021 (MoHFW) minus current statutory towns (2011 Census)	Projected urban population 2021 (MoHFW) minus projected statutory towns, 2021	Population of census towns 2011	State's population and area (2011)
Andhra Pradesh	4.81%	5.46%	4.37%	4.32%
Arunachal Pradesh	0.05%	-0.32%	0.01%	0.38%
Assam	1.48%	2.32%	1.99%	2.64%
Bihar	2.65%	0.39%	1.01%	8.26%
Chhattisgarh	1.53%	-0.61%	0.28%	2.39%
Goa	0.54%	1.02%	0.97%	0.12%
Gujarat	7.30%	4.49%	3.63%	5.26%
Haryana	3.03%	1.96%	1.88%	2.08%
Himachal Pradesh	0.07%	0.03%	0.04%	0.71%
Jharkhand	3.34%	3.40%	5.31%	2.78%
Karnataka	4.96%	1.41%	2.52%	5.29%
Kerala	14.38%	27.82%	21.18%	2.68%
Madhya Pradesh	4.00%	2.06%	2.27%	6.56%
Maharashtra	9.32%	5.58%	8.27%	9.59%
Manipur	0.27%	0.36%	0.38%	0.29%
Meghalaya	0.22%	0.32%	0.45%	0.30%
Mizoram	0.07%	-0.11%	0.00%	0.15%
Nagaland	0.31%	0.21%	0.13%	0.21%
Odisha	1.57%	1.84%	1.70%	3.72%
Punjab	2.10%	1.61%	1.41%	2.28%
Rajasthan	3.72%	2.17%	2.55%	6.36%
Sikkim	0.11%	-0.24%	0.01%	0.07%
Tamil Nadu	7.56%	8.36%	10.26%	5.94%
Telangana	4.56%	4.95%	4.10%	3.04%
Tripura	0.60%	0.39%	0.60%	0.31%
Uttar Pradesh	10.18%	7.05%	7.32%	16.05%
Uttarakhand	1.08%	1.29%	1.01%	0.95%
West Bengal	10.22%	16.80%	16.34%	7.26%

Annexure 3.1: Parastatals Involved in Urban Functions in Karnataka

Sl. No.	Parastatal	Department	Function(s)
State-level Parastatals			
1.	Karnataka Urban Water Supply and Drainage Board (KUWSDB)	UDD	- Construction of water works for bulk water supply - Capacity creation and augmentation of Water Supply Schemes (WSS) and Under Ground Drainage (UGD) schemes - Operation and Maintenance (O&M) of the WSS and UGD projects in some ULGs on the direction of the state government
2.	Karnataka Urban Infrastructure Development and Finance Corporation (KUIDFC)	UDD	- Prepare, formulate and implement projects, schemes and programmes relating to urban infrastructure development - Provide technical and financial consultancy - Construction of water works and their O&M in some ULGs.
3.	Karnataka Rail Infrastructure Development Company (KRIDE)	UDD	- Boost rail infrastructure projects in the state - Execution of the Bengaluru Suburban Rail Project (BSRP) and two large doubling projects - Enrich rural-urban connectivity - Synergise multiple modes of public transport
4.	State Road Corporations (KSRTC, NWKRTC, NEKRTC)	Transport	Providing quality public transport services to residents across the state and its ULGs
5.	Karnataka Slum Development Board (KSDB)	Housing	- Boost rail infrastructure projects in the state - Execution of the Bengaluru Suburban Rail Project (BSRP) and two large doubling projects - Enrich rural-urban connectivity - Synergise multiple modes of public transport
6.	Rajiv Gandhi Housing Corporation Limited (RGHCL)	Housing	- Provide housing to the socially and economically weaker sections of society - Implementation of union and state housing schemes
7.	Karnataka Industrial Area Development Board	Industries and Commerce	- Promoting rapid and orderly establishment and development of industries - Providing industrial infrastructural facilities and other amenities in industrial areas
8.	Bangalore Water Supply and Sewerage Board (BWSSB)	UDD	Responsible for water supply and sewage disposal within the jurisdiction of the BBMP
9.	Bangalore Metro Rail Corporation Limited (BMRCL)	UDD	Implementing and operating the Bangalore Metro Rail Project

Sl. No.	Parastatal	Department	Function(s)
State-level Parastatals			
10.	Bengaluru Metropolitan Transport Corporation (BMTCL)	Transport	• Provide safe, clean, and affordable public bus transport in Bengaluru • Serve surrounding urban, sub-urban and rural areas
11.	Bangalore Development Authority (BDA)	UDD	• Preparation of a Comprehensive Development Plan for Bengaluru metropolitan region • Development of infrastructure • Provision of development-related sites and services • Provision of housing for underprivileged citizens
12.	Bangalore Metropolitan Region Development Authority (BMRDA)	UDD	• Planning and supervising the development of the areas within the Bangalore Metropolitan Region (BMR) • Raising finances for development projects or schemes • Coordinating the activities of BBMP, parastatals, and other bodies connected with development activities in the BMR
13.	Urban Development Authorities (31 in number for each district)	UDD	• Planning, promoting, and securing the development of urban areas in the district • Execution of construction, engineering, and other operations necessary for development
14.	Town Planning Authorities (52 in number)	UDD	• Preparation of master plans • Land use zoning and preparation of zoning regulations • Providing technical assistance to various government departments/local bodies for orderly urban development
15.	Special Purpose Vehicles (SPVs) created under the Smart Cities Mission (7 in number)	UDD	• Execution of the Smart City Proposal under the guidance of the state government • Mobilisation of resources • Incorporation of joint ventures and formation of Public-Private Partnerships with Indian or foreign firms

Annexure 3.2: Budget Allocations by Karnataka's Urban Development Department (UDD) to Parastatals and ULGs

Sl. No.	Particulars	FY 2020-21		FY 2021-22		FY 2022-23		FY 2023-24		FY 2024-25	
		INR crore	% of UDD Budget	INR crore	% of UDD Budget	INR crore	% of UDD Budget	INR crore	% of UDD Budget	INR crore	% of UDD Budget
1.	Total UDD budget	15,973	-	14,238	-	14,399	-	15,702	-	14,922	-
2.	Allocations to parastatals	6,205	39.85%	5,429	38.13%	5,812	40.37%	6,735	42.89%	3,490	23.39%
2.1	Allocations to Bengaluru city-based parastatals	4,187	26.21%	3,019	21.20%	3,062	21.27%	3,535	22.51%	2,087	13.99%
2.2	Allocations to state-level parastatals	1,618	10.13%	2,010	14.12%	1,750	12.15%	2,050	13.06%	1,200	8.04%
2.3	Allocations to state-level parastatals under Smart Cities Mission	400	2.50%	400	2.81%	1,000	6.94%	1,150	7.32%	203	1.36%
3.	Allocations to ULGs	6,150	38.50%	5,706	40.08%	5,845	40.60%	6,260	39.87%	6,479	43.42%
3.1	Allocation to ULGs under SFC grants	4,601	28.80%	4,535	31.86%	4,632	32.17%	4,978	31.70%	4,985	33.41%
3.2	Allocations to ULGs under CFC grants	1,549	9.70%	1,171	8.22%	1,213	8.42%	1,282	8.16%	1,493	10.01%
4.	Allocations to state or district-level implementing authorities,* under state and central schemes ⁵	1,298	8.13%	585	4.11%	588	4.08%	1,709	10.88%	1,673	11.21%
5.	Total allocations to parastatals, ULGs, and other implementing authorities (2 + 3 + 4)	13,653	85.47%	11,720	82.32%	12,246	85.05%	14,705	93.64%	11,642	78.02%

Annexure 3.3: Parastatals Involved in Urban Functions in Odisha

Sl. No.	Parastatals	Type	Function
1	Bhubaneswar Smart City Limited (BSCL)	City	Executes Smart City projects
2	Rourkela Smart City Limited (RSCL)	City	Executes Smart City projects
3	Bhubaneswar Development Authority (BDA)	City	Urban planning and infrastructure
4	Cuttack Development Authority (CDA)	City	Urban planning and infrastructure
5	Brahmapur Development Authority	City	Urban planning and infrastructure
6	State Urban Development Agency (SUDA)	State	Implements urban poverty and infrastructure schemes
7	Water Corporation of Odisha (WATCO)	State	Manages urban water supply and sewerage
8	Odisha State Road Transport Corporation (OSRTC)	State	Operates state-level public bus services
9	Odisha Water Supply and Sewerage Board (OWSSB)	State	Designs water and sewerage systems
10	Capital Region Urban Transport (CRUT)	City	Manages bus transport in Bhubaneswar-Cuttack
11	Bhubaneswar Metro Rail Corporation Limited (BMRCL)	City	Implements metro rail project

Annexure 3.4: Budget Allocations by the Government of Odisha to Parastatal Agencies (2018–19 Actuals to 2025–26 Budget Estimates)

HUDD Budget Distribution by Allocation Type from 2018-19 (A) to 2025-26 (BE)

	2018-19 (A)	2019-20 (A)	2020-21 (A)	2021-22 (A)	2022-23 (A)	2023-24 (A)	2024-25 (RE)	2025-26 (BE)
Parastatals (INR Crore)	816	1,037	397	617	1,520	1,320	2,474	1,532
ULG (INR Crore)	2,101	2,752	2,278	2,508	2,465	3,743	4,184	4,347
Unknown (INR Crore)	785	627	779	996	1,588	1,271	1,704	2,139
ULG (XV FC Tied) (INR Crore)	0	0	544	493	511	508	572	583
Direct Benefit Transfer (DBT) (INR Crore)	310	290	269	408	402	393	616	683
Total	4,012	4,707	4,267	5,023	6,485	7,235	9,551	9,285

Note: 'Unknown' refers to budget heads that could not be verified by us as being transferred to parastatals or ULGs. These include budget heads like Samruddha Sahara, SUJALA, Town Planning Scheme, etc.

Percentage Share of Budget Distribution by Allocation Type from 2018-19 (A) to 2025-26 (BE)

	2018-19 (A)	2019-20 (A)	2020-21 (A)	2021-22 (A)	2022-23 (A)	2023-24 (A)	2024-25 (RE)	2025-26 (BE)	Average
Parastatals	20%	22%	9%	12%	23%	18%	26%	17%	19%
ULG	52%	58%	53%	50%	38%	52%	44%	47%	49%
Unknown	20%	13%	18%	20%	24%	18%	18%	23%	19%
ULG (XV FC Tied)	0%	0%	13%	10%	8%	7%	6%	6%	6%
Direct Benefit Transfer (DBT)	8%	6%	6%	8%	6%	5%	6%	7%	7%

Distribution of State Scheme Expenditure by Implementing Agency (2018–19 to 2025–26)

	2018-19 (A)	2019-20 (A)	2020-21 (A)	2021-22 (A)	2022-23 (A)	2023-24 (A)	2024-25 (RE)	2025-26 (BE)	Average
Parastatals	22%	23%	27%	37%	34%	24%	37%	15%	27%
ULG	30%	52%	32%	23%	22%	46%	28%	39%	34%
Unknown	48%	25%	41%	40%	44%	31%	35%	47%	39%

Note: Approximately 61% of the total state scheme budget was tagged to implementing agencies.

Distribution of Centrally Sponsored Scheme (CSS) Expenditure by Recipient Type (2018–19 to 2025–26)

	2018-19 (A)	2019-20 (A)	2020-21 (A)	2021-22 (A)	2022-23 (A)	2023-24 (A)	2024-25 (RE)	2025-26 (BE)	Average
Parastatals	55%	50%	5%	1%	41%	38%	34%	39%	33%
ULG	5%	12%	4%	26%	2%	17%	36%	26%	16%
Unknown	4%	17%	41%	34%	28%	10%	4%	5%	18%
Direct Benefit Transfer (DBT)	36%	21%	50%	39%	28%	34%	27%	30%	33%

Note: Approximately 82% of the total CSS budget was tagged to recipient type.

Annexure 3.5: Revenue Composition and Own Revenue Share by ULG Population Category

ULG Population Category	Total Own Revenue (INR crore)	% Share of Total Revenue	Total Assigned Revenues (INR crore)	% Share of Total Revenue	Revenue Grants and Subsidies (INR crore)	% Share of Total Revenue	Other Income (INR crore)	% Share of Total Revenue	Total Revenue (INR crore)	Revenue Expenditure (INR crore)	% Share of Total Revenue
>4 million	51,425	71%	2,362	3%	16,989	23%	1,970	3%	72,747	36,748	140%
1-4 million	27,156	65%	3,335	8%	10,447	25%	909	2%	41,847	25,786	105%
500K-1 million	4,431	40%	887	8%	5,638	50%	216	2%	11,172	7,911	56%
100K-500K	7,786	37%	2,580	12%	9,835	47%	589	3%	20,782	14,512	54%
<100K	7,834	29%	2,963	11%	15,459	57%	705	3%	26,962	19,214	41%

Source: Audited accounts of 3,803 ULGs for the financial year 2021-22 from CityFinance.

Annexure 3.6: Composition of Municipal Revenues and Expenditures at the National Level (2021–22)

2021-22	Own Revenue	Assigned Revenue	Revenue Grants & Subsidies	Borrowings	Total Revenue	Revenue	Total Revenue (INR crore)
Amount (INR crore)	1,03,241	13,443	64,847	27,028.30	208,559	1,12,988	55,941
% of GDP	0.38%	0.05%	0.24%	0.10%	0.77%	0.42%	0.21%

Source: Data has been extrapolated from audited accounts of 3,803 ULGs for the financial year 2021–22, as reported on the CityFinance. The percentage share of GDP has been calculated using the national GDP figure of INR 2,69,49,646 crore for 2021–22.

Annexure 3.8: Components of Gross Domestic Product at Current Prices

Year	PFCE (INR crore)	GFCE (INR crore)	GFCE (INR crore)	CIS (INR crore)	Valu- ables (INR crore)	Export of goods and services (INR crore)	Import of goods and services (INR crore)	Discrep- ancies (INR crore)	GDP (INR crore)
2011-12 Series									
2014-15	72,47,340	13,01,762	37,50,392	3,12,698	2,09,407	28,63,636	32,35,962	18,687	1,24,67,959
2015-16	81,26,408	14,36,171	39,57,092	2,62,477	2,03,506	27,28,647	30,44,923	1,02,495	1,37,71,874
2016-17	91,26,533	15,86,658	43,38,671	1,38,083	1,67,326	29,48,772	32,20,591	3,06,216	1,53,91,669
2017-18	1,00,36,153	18,40,119	48,15,600	2,37,581	2,41,685	32,11,521	37,51,389	4,58,773	1,70,90,042
2018-19	1,12,05,296	20,45,552	55,68,422	3,18,234	2,26,104	37,66,294	44,77,169	2,46,934	1,88,99,668
2019-20	1,22,45,357	22,11,933	57,20,386	1,35,231	1,94,800	37,52,188	42,70,232	1,13,930	2,01,03,593
2020-21	1,21,30,481	23,05,547	54,24,997	38,460	2,78,821	37,09,237	37,87,294	-2,46,154	1,98,54,096
2021-22	1,43,82,704	24,72,153	69,79,647	2,13,837	3,85,015	50,49,645	56,69,023	-2,16,579	2,35,97,399
2022-23 (1st RE)	1,64,22,535	28,83,649	82,86,979	2,77,120	3,35,730	62,52,449	72,13,027	-2,95,789	2,69,49,646
2023-24 (PE)	1,78,22,526	30,68,970	91,07,021	2,95,198	4,39,024	64,53,015	71,10,310	-5,39,778	2,95,35,667
2024-25 (1st AE)	2,00,29,580	33,30,598	97,63,363	3,19,249	5,13,009	69,66,331	78,15,050	-6,95,674	3,24,11,406

Source: Ministry of Finance, Government of India. (2024-25). Economic Survey.
<https://www.indiabudget.gov.in/economicsurvey/index.php>

Annexure 4.1: Share of Local Government Grants in Gross Tax Revenue Based on Finance Commission Projections and Actuals (2015–16 to 2025–26)

Indicator	2015–16	2016–17	2017–18	2018–19	2019–20	2020–21	2021–22	2022–23	2023–24	2024–25 (RE)	2025–26 (BE)
Projected by the Finance Commission (INR lakh crore)											
(a) Gross Tax Revenue (GTR)	15.67	18.03	20.76	23.94	27.63	18.76	21.35	23.62	26.43	29.86	34.01
(b) Divisible Pool (DP)	13.79	15.91	18.39	21.27	24.64	14.00	16.06	17.87	20.11	22.84	26.16
(c) Tax Share to States	5.79	6.68	7.72	8.93	10.35	5.74	6.59	7.33	8.24	9.37	10.72
(d) LG Grants	0.30	0.49	0.56	0.65	0.87	1.00	0.80	0.85	0.87	0.92	.92
Percentage (%)											
(e) DP/GTR	88%	88%	89%	89%	89%	75%	75%	76%	76%	76%	77%
(f) Tax Share/DP	42%	42%	42%	42%	42%	41%	41%	41%	41%	41%	41%
(g) LG/DP (Proposed)	2.17%	3.07%	3.06%	3.05%	3.55%	7.14%	5.00%	4.74%	4.34%	4.03%	3.52%
Actual											
(h) GTR (INR lakh crore)	14.56	17.16	19.19	20.80	20.10	20.27	27.09	30.54	34.65	38.53	42.70
(i) GR of GTR (%)	–	18%	12%	8%	–3%	1%	34%	13%	13%	11%	11%
(j) DP (INR lakh crore)	12.81	15.15	17.00	18.49	17.92	15.13	20.38	23.10	26.15	29.38	32.88
(k) LG/DP (%)	2.34%	3.23%	3.31%	3.51%	4.87%	6.61%	3.94%	3.67%	3.33%	3.13%	2.80%

Source: XIV and XV Finance Commission reports; Economic Survey 2024–25.

Annexure 4.2: Local Government Grants as a Percentage of Estimated GDP by XIV & XV FC and Actual GDP During the Award Period

	Estimated	Actual
2015-16		
LG Grants (INR crore)	29,988	29,988
GDP (INR crore)	1,46,15,001	1,37,71,874
%	0.21%	0.22%
2016-17		
LG Grants (INR crore)	48,868	48,868
GDP (INR crore)	1,65,88,026	1,53,91,669
%	0.29%	0.32%
2017-18		
LG Grants (INR crore)	56,288	56,288
GDP (INR crore)	1,88,27,410	1,70,90,042
%	0.30%	0.33%
2018-19		
LG Grants (INR crore)	64,939	64,939
GDP (INR crore)	2,13,69,110	1,88,99,668
%	0.30%	0.34%
2019-20		
LG Grants (INR crore)	87,352	87,352
GDP (INR crore)	2,42,53,940	2,01,03,593
%	0.36%	0.43%
2020-21		
LG Grants (INR crore)	90,000	90,000
GDP (INR crore)	1,91,19,458	1,98,54,096
%	0.47%	0.45%
2021-2022		
LG Grants (INR crore)	80,297	80,297
GDP (INR crore)	2,17,00,585	2,35,97,399
%	0.37%	0.34%
2022-23		
LG Grants (INR crore)	84,703	84,703
GDP (INR crore)	2.17%	2,69,49,646
%	2,69,49,646	0.31%
2023-24		
LG Grants (INR crore)	87,181	84,703
GDP (INR crore)	2,62,57,165	2,95,35,667
%	0.33%	0.30%

Source: XIV and XV Finance Commission reports; Economic Survey 2024-25.

Annexure 4.3: Gross Domestic Product (GDP) in Nominal Terms (2015–16 to 2024–25)

Actual	Nominal GDP (INR crore)
2015-16	1,37,71,874
2016-17	1,53,91,669
2017-18	1,70,90,042
2018-19	1,88,99,668
2019-20	2,01,03,593
2020-21	1,98,54,096
2021-22	2,35,97,399
2022-23	2,69,49,646
2023-24	2,95,35,667
2024-25	3,24,11,406

Source: Ministry of Finance, Government of India. (2024-25). Economic Survey.
<https://www.indiabudget.gov.in/economicsurvey/index.php>

Annexure 4.4: Per Capita LG Grants Allocation by FCs

Indicator	X FC (1995– 2000)	XI FC (2000– 05)	XII FC (2005– 10)	XIII FC (2010– 15)	XIV FC (2015– 20)	XV FC (2021– 26)	XVI FC (Proposed) 2026–31
Census Year	1971	1991	2001	2011	2017	2023	2028
Rural Population (Crore)	43.89	62.40	74.07	82.17	86.14	89.00	90.39
Rural Grants (INR crore)	4,381	8,000	20,000	64,407	2,00,292	2,80,733	5,70,000
Per Capita Rural Grants (INR crore)	100	128	270	784	2,325	3,158	6,306
Urban Population (Crore)	10.91	20.70	27.15	35.74	40.68	45.73	49.72
Urban Grants (INR crore)	1,000	2,000	5,000	23,111	87,144	1,55,628	3,80,000
Per Capita Urban Grants (INR)	92	97	184	647	2,142	3,403	7,642
Total LG Grants (INR crore)	5,381	10,000	25,000	87,518	2,87,436	4,36,361	9,50,000 ¹⁷⁰
Growth Rate of LG Grant Allocation (%)	-	86%	150%	250%	228%	52%	118%
Per Capita LG Grants (INR)	98	120	247	742	2,266	3,241	6,780
Growth Rate of Per Capita LG Grants (%)	-	23%	105%	201%	205%	43%	109%

■ Population as per Census ■ Population as per MoHFW 2019 projections

Source: Population figures for Census years (1971 to 2011) are sourced from censusindia.gov.in. Population projections (excludes UTs) for 2017, 2023, and 2028 are based on estimates by the Ministry of Health and Family Welfare's Technical Group Report (2019). Grant allocations are drawn from the XV Finance Commission report.

¹⁷⁰ To estimate LG grants for the XVI FC, we analysed the nominal GDP trend from the post-COVID period (2021-22 to 2023-24), deriving a CAGR of 11.9%. Additionally, we considered the NSO's projected growth rate of 9.7% for 2023-24 to 2024-25. Adopting a conservative approach, we assumed a 9% growth rate for the FC award period (2026-31), estimating the nominal GDP for this period at ₹23,04,56,298 Cr. LG grants were calculated as 0.35% of GDP, with a 60:40 rural-urban split.

4.5: Local Government Grant Allocations under the XIV and XV Finance Commissions (Actuals) and XVI Finance Commission (Projections)

Year	LG Grants (INR crore)	Total Population (crore)	Per Capita LG Grants (INR)	Per Capita LG Grant Growth Rate (%)
2015-16	29,988	124	242	–
2016-17	48,868	125	390	61%
2017-18	56,288	127	444	14%
2018-19	64,939	128	507	14%
2019-20	87,352	130	674	33%
2020-21	99,925	131	763	–
2021-22	80,297	132	607	-20%
2022-23	84,703	133	635	5%
2023-24	87,181	135	648	2%
2024-25	92,087	136	678	5%
2025-26	92,093	137	672	-1%
2026-27	1,50,363	138	1,088	62%
2027-28	1,67,991	139	1,207	11%
2028-29	1,87,685	140	1,340	11%
2029-30	2,09,688	141	1,486	11%
2030-31	2,34,271	142	1,649	11%

Source: XV Commission Report and Ministry of Health and Family Welfare, Technical Group Report (2019)¹⁷¹

¹⁷¹ The per capita of LG grants and urban grants are calculated based on the year-on-year population projections for the respective year from MoHFW 2019 technical report. The total and urban population excludes UTs.

Annexure 4.6: Local Government Grants as a Percentage of GDP During XIV FC Period

	2014-15 (BE)	2014-15 (Reassessed)	2015-16	2016-17	2017-18	2018-19	2019-20
Gross Revenue Receipts	12.25	12.14	12.25	12.39	12.55	12.73	12.92
Gross Tax Revenues	10.60	10.60	10.72	10.87	11.03	11.20	11.39
Corporation Tax	3.50	3.50	3.61	3.73	3.85	3.97	4.10
Income Tax	2.21	2.21	2.27	2.34	2.40	2.47	2.54
Customs	1.57	1.57	1.55	1.54	1.52	1.51	1.49
Union Excise Duties	1.61	1.61	1.50	1.40	1.31	1.23	1.15
Service Tax	1.68	1.68	1.75	1.83	1.91	2.00	2.09
Other Taxes	0.03	0.03	0.03	0.03	0.03	0.02	0.02
Non-Tax Revenues	1.65	1.54	1.53	1.52	1.52	1.52	1.53
Interest Receipts	0.15	0.15	0.13	0.10	0.09	0.07	0.06
Dividends and Profits	0.34	0.34	0.34	0.34	0.34	0.34	0.34
Dividend/Surplus from RBI	0.36	0.41	0.41	0.42	0.42	0.42	0.43
Petroleum	0.11	0.11	0.11	0.11	0.11	0.11	0.11
Telecommunication	0.35	0.19	0.19	0.19	0.19	0.19	0.19
Other Non-Tax Revenues	0.34	0.34	0.35	0.36	0.38	0.39	0.41
Tax Share to States	2.97	2.97	3.96	4.03	4.10	4.18	4.27
NCCD Transfer to NCCF/NDRF	0.04	0.04	0.04	0.04	0.04	0.04	0.04
Net Revenues to Centre	9.24	9.13	8.25	8.32	8.41	8.51	8.62
Revenue Expenditure	12.18	12.18	10.81	10.57	10.20	9.87	9.55
General Service	5.57	5.57	5.45	5.30	5.12	4.96	4.81
Interest Payment	3.32	3.32	3.23	3.10	2.95	2.81	2.69
Defence	1.04	1.04	1.04	1.04	1.04	1.04	1.04
Pension	0.64	0.64	0.61	0.59	0.57	0.55	0.53
Police	0.36	0.36	0.36	0.36	0.36	0.36	0.36
Fiscal Services	0.08	0.08	0.08	0.08	0.07	0.07	0.07
External Affairs	0.04	0.04	0.04	0.03	0.03	0.03	0.03
Other General Service	0.09	0.09	0.09	0.09	0.09	0.09	0.09
Social Service	0.46	0.46	0.41	0.37	0.33	0.30	0.27
Economic Service	1.11	1.11	1.09	1.07	1.06	1.04	1.03
Transport (Including Divided relief to Railways)	0.21	0.21	0.22	0.23	0.24	0.25	0.26
Communication	0.03	0.03	0.03	0.03	0.03	0.03	0.02
Science, Technology & Environment	0.15	0.15	0.15	0.15	0.15	0.15	0.15
Export Promotion	0.02	0.02	0.02	0.02	0.02	0.02	0.02
Other Economic Service	0.70	0.70	0.67	0.65	0.62	0.60	0.58
Subsidy	2.02	2.02	1.70	1.60	1.40	1.20	1.00
Food	0.89	0.89	0.67	0.67	0.67	0.67	0.67
Other	1.13	1.13	1.03	0.93	0.73	0.53	0.33
Grants-in-Aid to State Government Recommended by Finance Commission	0.50*	0.50	0.61	0.61	0.55	0.52	0.55
Revenue Deficit Grants	0.06	0.06	0.33	0.25	0.19	0.16	0.14
Disaster Relief Grant to States	0.04	0.04	0.07	0.06	0.06	0.05	0.05
Grants to Local Bodies to States	0.17	0.17	0.21	0.29	0.30	0.30	0.36
Provision for other transfers (expected) to States	0.04	0.04	1.35	1.42	1.54	1.64	1.67
Grants-in-Aid to Union Territory	0.04	0.04	0.04	0.04	0.04	0.04	0.04
Other Revenue Exp.	0.16	0.16	0.16	0.17	0.17	0.17	0.18
Capital Expenditure	1.76	1.76	1.64	1.40	1.90	2.40	2.90
Non-Debt Capital Receipts	0.57	0.57	0.61	0.65	0.70	0.76	0.82
Recovery of Loans and Advances	0.08	0.08	0.06	0.05	0.04	0.03	0.03
Other Capital Receipts	0.49	0.49	0.54	0.60	0.66	0.72	0.80
Revenue Deficit/Surplus(-)	2.94	3.05	2.56	2.25	1.79	1.36	0.93
Fiscal Deficit/Surplus(-)	4.13	4.24	3.60	3.00	3.00	3.00	3.00
Adjusted Outstanding Debt	45.40	45.40	43.60	41.41	39.49	37.79	36.30

Source: XIV Finance Commission report, p. 436. The table presents estimated year-on-year Gross Tax Revenue (GTR) and corresponding grants to local governments for the award period.

Annexure 4.7: Divisible Pool as a Percentage of GDP During XV FC Period

	2020-21 (BE)	2020-21 (Reassessed)	2021-22	2022-23	2023-24	2024-25	2025-26
Gross Revenue Receipts	12.49	11.17	11.20	11.30	11.42	11.60	11.82
Gross Tax Revenue	10.77	9.81	9.84	9.94	10.07	10.25	10.47
Corporation Tax	3.03	2.56	2.58	2.62	2.67	2.74	2.82
Income Tax	2.84	2.32	2.35	2.39	2.44	2.53	2.63
Customs Duties	0.61	0.53	0.54	0.54	0.55	0.56	0.57
Union Excise Duties	1.19	1.55	1.49	1.45	1.41	1.37	1.33
Service tax	0.00	-	-	-	-	-	-
Goods and Services Tax	3.07	2.83	2.86	2.91	2.97	3.03	3.09
Other Taxes	0.03	0.02	0.02	0.02	0.02	0.02	0.02
Non-Tax Revenues	1.71	1.35	1.35	1.35	1.35	1.35	1.35
Interest Receipts	0.05	0.06	0.05	0.05	0.04	0.04	0.03
Dividends and Profits	0.29	0.17	0.17	0.17	0.17	0.17	0.17
Dividend/Surplus from RBI	0.40	0.47	0.47	0.47	0.47	0.47	0.47
Petroleum	0.06	0.06	0.06	0.06	0.06	0.06	0.06
Telecommunication	0.59	0.37	0.32	0.29	0.25	0.21	0.18
Other Non Tax Revenues	0.32	0.23	0.28	0.31	0.36	0.41	0.43
Divisible Pool	8.51	7.32	7.40	7.52	7.66	7.84	8.05
Tax Share to States	3.49	3.00	3.03	3.08	3.14	3.21	3.30
NCCD Transfer to NCCF/NDRF	0.01	0.02	0.01	0.01	0.01	0.01	0.01
Net Revenues to the Centre	8.99	8.15	8.15	8.20	8.27	8.38	8.51
Revenue Expenditure	11.70	14.07	13.08	12.67	12.16	11.69	11.32
General services	5.65	6.36	6.05	5.99	5.86	5.68	5.47
Interest Payments	3.15	3.55	3.50	3.53	3.49	3.42	3.31
Defence revenue expenditure	0.93	1.09	1.02	0.99	0.96	0.93	0.90
Pensions	0.94	0.97	0.87	0.84	0.80	0.76	0.72
Police	0.42	0.49	0.43	0.42	0.40	0.38	0.36
Fiscal Services	0.08	0.10	0.09	0.08	0.08	0.07	0.07
External Affairs	0.04	0.05	0.04	0.04	0.04	0.04	0.04
Other general services	0.09	0.11	0.10	0.09	0.09	0.08	0.07
Social Services	0.56	0.82	0.76	0.77	0.78	0.78	0.78
Health	0.14	0.32	0.33	0.35	0.37	0.38	0.40
Other Social Services	0.42	0.49	0.44	0.42	0.41	0.40	0.39

Source: XV Finance Commission report, Annexure 4.2, p. 705. The table presents estimated year-on-year Gross Tax Revenue (GTR) and corresponding divisible pool for the award period

Annexure 4.8: Local Government Grants as a Percentage of GDP During XV FC Period

	2020-21 (BE)	2020-21 (Reassessed)	2021-22	2022-23	2023-24	2024-25	2025-26
Economic Services (excluding subsidy)	1.02	1.50	1.27	1.19	1.15	1.10	1.04
Transport and Communication	0.16	0.19	0.17	0.17	0.16	0.16	0.15
Science, Technology & Environment	0.14	0.16	0.14	0.14	0.13	0.13	0.13
Export Promotion	0.01	0.01	0.01	0.01	0.01	0.01	0.01
Power	0.06	0.07	0.06	0.06	0.06	0.06	0.06
Other economic services	0.65	1.07	0.88	0.82	0.78	0.74	0.70
Subsidy	1.17	1.63	1.45	1.36	1.27	1.18	1.09
Food	0.51	0.87	0.86	0.82	0.77	0.72	0.67
Others	0.65	0.77	0.59	0.54	0.50	0.46	0.42
Grants-in-Aid to State Governments Recommended by Finance Commission	0.67	1.03	1.07	0.96	0.75	0.65	0.57
Revenue Deficit Grants	0.13	0.39	0.55	0.36	0.20	0.08	0.04
Disaster Relief Grants to States	0.09	0.12	0.10	0.10	0.09	0.09	0.08
Grants to local government to States	0.44	0.52	0.37	0.36	0.33	0.32	0.28
Sector-specific grant	-	-	0.06	0.10	0.09	0.11	0.11
State-specific grant	-	-	-	0.04	0.04	0.05	0.05
Provision for other transfers (expected) to States**, of which	2.27	2.30	2.05	1.97	1.92	1.86	1.92
GST compensation to States	0.57	0.49	0.42	0.42	0.43	0.44	0.57
Grants-in-Aid to Union Territories	0.21	0.25	0.25	0.25	0.26	0.26	0.27
Other revenue expenditure	0.16	0.18	0.18	0.18	0.18	0.18	0.17
Capital Expenditure	1.83	1.84	1.70	1.51	1.53	1.54	1.49
Non-Debt Capital Receipts	1.00	0.36	0.64	0.48	0.41	0.36	0.30
Revenue Deficit/Surplus(-)	2.71	5.92	4.94	4.47	3.88	3.31	2.81
Fiscal Deficit/Surplus(-)	3.54	7.40	6.00	5.50	5.00	4.50	4.00
Adjusted Outstanding Debt*	47.47	59.63	58.40	59.03	58.68	57.56	55.72

Source: XV Finance Commission report, Annexure 4.2, p. 706. The table presents year-on-year local government grants for the award period.

Annexure 4.9: Trends in Total and Per Capita Outlays to the Rural Sector under MoPR, MoRD, and DDWS (2019–20 to 2025–26)

Year	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26
Centrally Sponsored Schemes (CSS)	Actuals (INR crore)	Actuals (INR crore)	Actuals (INR crore)	Actuals (INR crore)	RE (INR crore)	RE (INR crore)	BE (INR crore)
National Social Assistance Programme	8,692	42,443	8,152	9,651	9,476	9,652	9,652
Mahatma Gandhi National Rural Employment Guarantee Programme	71,687	1,11,170	98,468	90,806	89,154	86,000	86,000
Pradhan Mantri Gram Sadak Yojna	14,017	13,688	13,992	18,783	15,380	14,500	19,000
Deendayal Antyodaya Yojana - National Rural Livelihoods Mission (DAY-NRLM)	9,022	9,208	9,383	11,536	13,934	15,047	19,005
Shyama Prasad Mukherjee Rurban Mission	304	369	150	821			
Pradhan Mantri Awas Yojna (PMAY)	18,116	19,269	30,057	44,962	21,770	32,426	54,832
Additional transfer to Agriculture Infrastructure and Development Fund	-	-	-	-	12,002	-	
Pradhan Mantri Krishi Sinchayee Yojna (Department Land Resources)	1,467	938	941	743	1,565	1,800	2,505
Rashtriya Gram Swaraj Abhiyan (MoPR)	465	686	690	762	887	765	1,064
Jal Jeevan Mission (DDWS)	10,030	10,998	63,126	54,700	69,992	22,694	67,000
Swachh Bharat Mission (DDWS)	8,213	4,945	3,099	4,925	6,546	7,192	7,192
A. Total CSS	1,42,014	2,13,714	2,28,058	2,37,688	2,40,706	1,90,076	2,66,250
B. Projected Population (MoHFW)	88,17,24,000	88,66,14,000	89,14,16,000	89,49,47,000	89,83,95,000	90,17,59,000	90,50,40,000
Per Capita of CSS Allocation to MoPR, MoRD, and DDWS (A/B)	1,611	2,410	2,558	2,656	2,679	2,108	2,942

Source: The total expenditure attributed to the Ministry of Panchayati Raj (MoPR), the Ministry of Rural Development (MoRD), and the Department of Drinking Water Supply (DDWS) has been considered as the rural outlay. For per capita estimates, we used population projections for the respective years from the Ministry of Health and Family Welfare's Technical Group Report (2019).

Annexure 4.10: Trend in Total and Per Capita Outlays to the Urban Sector under MoHUA (2019–20 to 2025–26)

Year							
Centrally Sponsored Schemes (CSS)	2019-20 Actuals (INR crore)	2020-21 Actuals (INR crore)	2021-22 Actuals (INR crore)	2022-23 Actuals (INR crore)	2023-24 RE (INR crore)	2024-25 RE (INR crore)	2025-26 BE (INR crore)
PMAY-U	6,848	20,991	59,963	28,653	21,684	15,170	23,294
AMRUT	6,392	6,448	7,280	6,500	5,591	6,000	10,000
Smart Cities	3,207	3,305	6,588	8,653	7,982	2,000	
SBM (Urban)	1,256	995	1,952	1,926	2,392	2,159	5,000
DAY-NULM	732	817	794	547	501	210	
PM-eBus Sewa Scheme	-	-	-	-	1	500	1,310
CITIIS 2.0	-	-	-	-	-	225	250
National Urban Digital Mission (NUDM)	-	-	-	-	-	109	1,250
Urban Challenge Fund							10,000
MTRS & Metro	18,908	8,998	23,473	23,603	23,102	28,546	34,807
A. Total CSS	37,342	41,554	1,00,050	69,882	61,254	54,920	85,911
B. Projected Population (MoHFW)	45,11,76,000	46,05,07,000	46,99,27,000	47,88,14,000	48,77,85,000	49,68,39,000	50,59,76,000
Per Capita of CSS (A/B)	828	902	2,129	1,459	1,256	1,105	1,698

Source: Total expenditure by the Ministry of Housing and Urban Affairs (MoHUA) has been considered as the urban outlay. Per capita estimates are based on population projections (includes states and UTs) for the respective years from the Ministry of Health and Family Welfare's Technical Group Report (2019)

Annexure 4.11: Percentage of Rural and Urban Allocations as per SFC Devolutions

State	Urbanisation Rate (2011 Census)	Urbanisation Rate (2026 MoHFW)	% Share to Urban by Latest SFC
Andhra Pradesh	30%	38%	33%
Assam	14%	16%	40%
Bihar	11%	13%	35%
Haryana	35%	44%	50%
Himachal Pradesh	10%	10%	34%
Karnataka	39%	46%	29%
Kerala	48%	81%	20%
Odisha	17%	19%	33%
Punjab	37%	43%	48%
Rajasthan	25%	27%	25%
Sikkim	25%	55%	24%
Tamil Nadu	48%	55%	51%
Uttar Pradesh	22%	24%	55%
Uttarakhand	30%	37%	60%
West Bengal	32%	38%	32%

Source: Census 2011.

Urbanisation rates for states are calculated using population projections for the respective years from the Ministry of Health and Family Welfare's 2019 Technical Report. Urban share under the State Finance Commissions (SFCs) is based on the latest available SFC reports of the respective states.¹⁷²

¹⁷² The latest SFC inter se allocation between urban and rural are unavailable for 13 states—Arunachal Pradesh, Chhattisgarh, Goa, Gujarat, Jharkhand, Madhya Pradesh, Maharashtra, Manipur, Meghalaya, Mizoram, Nagaland, Tripura, and Telangana.

Annexure 4.12: Per Capita Allocation Differences Between Rural and Urban Local Governments Under the XV Finance Commission

States	Level of Urbanisation (as per 2011 Census)	Per Capita ULG Share as per FC Allocation (INR)	Per Capita ULG Share as per Census Urbanisation Rate (INR)	Per Capita Loss/Gain (INR)
Andhra Pradesh	30%	3,526	3,119	407
Arunachal Pradesh	23%	14,479	9,821	4,658
Assam	14%	7,268	3,028	4,239
Bihar	11%	8,504	2,840	5,664
Chhattisgarh	23%	4,885	3,354	1,530
Goa	62%	1,643	3,030	(1,388)
Gujarat	43%	2,473	3,114	(641)
Haryana	35%	2,850	2,938	(88)
Himachal Pradesh	10%	12,409	3,683	8,727
Jharkhand	24%	4,244	3,017	1,227
Karnataka	39%	2,713	3,101	(389)
Kerala	48%	2,035	2,870	(835)
Madhya Pradesh	28%	3,955	3,231	724
Maharashtra	45%	2,285	3,054	(770)
Manipur	29%	4,233	3,652	580
Meghalaya	20%	6,101	3,620	2,481
Mizoram	52%	3,234	4,985	(1,751)
Nagaland	29%	4,361	3,715	646
Odisha	17%	6,422	3,168	3,254
Punjab	37%	2,658	2,946	(288)
Rajasthan	25%	4,514	3,319	1,196
Sikkim	25%	5,455	4,078	1,376
Tamil Nadu	48%	2,058	2,945	(887)
Telangana	39%	2,664	3,109	(445)
Tripura	26%	3,965	3,068	897
Uttar Pradesh	22%	4,367	2,875	1,492
Uttarakhand	30%	3,785	3,364	421
West Bengal	32%	3,022	2,848	175

Source: Authors' compilation using data from Census 2011 and XV FC Report

Annexure 4.13: State-wise Urban and Rural Grant Shares Based on a Total Local Government Grant Pool of INR 9.50 Lakh Crore

	XIV FC		XV FC		Proposed Method	
State	Urban Share (INR crore)	Rural Share (INR crore)	Urban Share (INR crore)	Rural Share (INR crore)	Urban Share (INR crore)	Rural Share (INR crore)
Andhra Pradesh	12,016	28,605	16,366	24,549	15,644	24,760
Arunachal Pradesh	815	2,699	1,443	2,164	340	2,296
Assam	3,205	17,904	10,037	15,055	4,710	18,211
Bihar	8,847	69,464	31,394	47,090	12,590	59,340
Chhattisgarh	5,250	17,333	9,100	13,649	6,357	14,226
Goa	729	441	470	705	971	400
Gujarat	21,181	28,535	19,988	29,983	27,567	25,302
Haryana	6,873	12,836	7,910	11,864	9,468	11,112
Himachal Pradesh	668	5,977	2,684	4,026	737	4,928
Jammu & Kashmir	4,311	11,451	-	-	-	-
Jharkhand	6,325	19,989	10,569	15,854	8,494	17,125
Karnataka	19,361	30,700	20,125	30,187	25,298	26,972
Kerala	12,107	13,285	10,183	15,274	17,062	11,498
Madhya Pradesh	17,109	44,807	24,921	37,381	21,489	38,610
Maharashtra	41,027	49,689	36,451	54,677	54,414	44,182
Manipur	567	682	1,108	1,662	893	1,691
Meghalaya	102	-	1,141	1,712	638	1,909
Mizoram	400	-	582	872	612	727
Nagaland	421	-	781	1,172	611	1,195
Odisha	5,855	29,251	14,122	21,183	7,499	24,763
Punjab	8,108	13,518	8,680	13,020	11,135	11,742
Rajasthan	14,918	45,060	24,159	36,239	18,254	38,635
Sikkim	161	494	265	398	164	422
Tamil Nadu	27,210	29,010	22,565	33,847	37,388	25,471
Telangana	11,202	17,762	11,556	17,334	14,573	15,453
Tripura	736	1,112	1,196	1,794	1,029	1,887
Uttar Pradesh	33,878	1,18,239	61,006	91,509	47,643	1,01,347
Uttarakhand	2,697	6,225	3,595	5,392	3,265	5,410
West Bengal	21,943	46,910	27,604	41,407	31,152	40,385
Total	2,88,023	6,61,977	3,80,000	5,70,000	3,80,000	5,70,000
	30%	70%	40%	60%	40%	60%

Source: Calculations by the authors based on data from Census 2011, XIV Finance Commission Report, and XV Finance Commission Report. For details on the methodology, refer to Section 4.3.1.

Annexure 4.14: States' Share of Local Government Grants — Comparison of XIV and XV Finance Commissions and Proposed Method

State	XIV FC	XV FC	Proposed Method	Proposed Method (minus) XIV FC	Proposed Method (minus) XV FC
Andhra Pradesh	4.28%	4.31%	4.25%	-0.02%	-0.05%
Arunachal Pradesh	0.37%	0.38%	0.28%	-0.09%	-0.10%
Assam	2.22%	2.64%	2.41%	0.19%	-0.23%
Bihar	8.24%	8.26%	7.57%	-0.67%	-0.69%
Chhattisgarh	2.38%	2.39%	2.17%	-0.21%	-0.23%
Goa	0.12%	0.12%	0.14%	0.02%	0.02%
Gujarat	5.23%	5.26%	5.57%	0.33%	0.31%
Haryana	2.07%	2.08%	2.17%	0.09%	0.08%
Himachal Pradesh	0.70%	0.71%	0.60%	-0.10%	-0.11%
Jammu & Kashmir	1.66%	-	0.00%	-1.66%	0.00%
Jharkhand	2.77%	2.78%	2.70%	-0.07%	-0.08%
Karnataka	5.27%	5.30%	5.50%	0.23%	0.21%
Kerala	2.67%	2.68%	3.01%	0.33%	0.33%
Madhya Pradesh	6.52%	6.56%	6.33%	-0.19%	-0.23%
Maharashtra	9.55%	9.59%	10.38%	0.83%	0.79%
Manipur	0.13%	0.29%	0.27%	0.14%	-0.02%
Meghalaya	0.01%	0.30%	0.27%	0.26%	-0.03%
Mizoram	0.04%	0.15%	0.14%	0.10%	-0.01%
Nagaland	0.04%	0.21%	0.19%	0.15%	-0.02%
Odisha	3.70%	3.72%	3.40%	-0.30%	-0.32%
Punjab	2.28%	2.28%	2.41%	0.13%	0.12%
Rajasthan	6.31%	6.36%	5.99%	-0.33%	-0.37%
Sikkim	0.07%	0.07%	0.06%	-0.01%	-0.01%
Tamil Nadu	5.92%	5.94%	6.62%	0.70%	0.68%
Telangana	3.05%	3.04%	3.16%	0.11%	0.12%
Tripura	0.19%	0.31%	0.31%	0.11%	-0.01%
Uttar Pradesh	16.01%	16.05%	15.68%	-0.33%	-0.37%
Uttarakhand	0.94%	0.95%	0.91%	-0.03%	-0.03%
West Bengal	7.25%	7.26%	7.53%	0.28%	0.27%

Source: XIV Finance Commission Report; XV Finance Commission Report; rural area data sourced from IndiaStat. Proposed method is based on authors' calculations.

Note: In the proposed method, the urban grant share for each state was calculated based on its proportion of India's total urban population, including statutory towns (ST), census towns (CT), and outgrowths (OG) as per the 2011 Census. The rural grant share was calculated using a 90% weightage to rural population (total population minus urban population from 2011 Census) and 10% to rural area. Each state's total share of local government grants was derived by combining its urban and rural components.

For Arunachal Pradesh, the rural area is assumed to be the total geographical area of the state due to the absence of publicly available disaggregated data. Please note that rural area figures are not sourced from official government publications and may contain variations.

Annexure 4.15: Performance Conditions Prescribed by the XIII Finance Commission

Sl. No.	XIII FC Performance Conditions
1	In all ULGs, states should implement an accounting framework consistent with the format and codification pattern suggested in the National Municipal Accounts Manual and must put in place a supplement to the budget documents for ULGs.
2	The C&AG of India must be given Technical Guidance and Support (TG&S) over the audit of all the local bodies in a state at every tier/category and the Annual Technical Inspection Report as well as the Annual Report of the Director of Local Fund Audit must be placed before the state legislature.
3	The state government must put in place a system of independent local government ombudsmen who will look into complaints of corruption and maladministration against the functionaries of local governments, both elected members and officials, and recommend suitable action.
4	The state governments must put in place a system to electronically transfer local government grants provided by this Commission to the respective local governments within five days of their receipt from the union government. Self-certification by state governments with a description of the arrangements in place will demonstrate compliance with this condition.
5	State governments must prescribe, through an Act, the qualifications of persons eligible for appointment as members of the SFC consistent with Article 243l (2) of the Constitution.
6	All local government should be fully enabled to levy property tax (including tax for all types of residential and commercial properties) and any hindrances in this regard must be removed.
7	State governments must put in place a state-level Property Tax Board, which will assist all municipalities and municipal corporations in the state to put in place an independent and transparent procedure for assessing property tax.
8	State governments must notify or cause all the municipal corporations and municipalities to notify by the end of a fiscal year (31 March) the service standards for four service sectors — water supply, sewerage, stormwater drainage, and solid waste management — proposed to be achieved by them by the end of the succeeding fiscal year.
9	All municipal corporations with a population of more than 1 million (2001 Census) must put in place a fire hazard response and mitigation plan for their respective jurisdictions.

Annexure 4.16: Analysis of Air Quality Grant Performance and Implementation Challenges¹⁷³

1. Performance against PM10 targets

An analysis of Continuous Ambient Air Quality Monitoring Stations (CAAQMS) data from 42 million-plus cities reveals a wide gap between actual PM10 levels and performance targets for 2024–25 (based on a 15% annual reduction from 2019–20 baseline levels):

- **Only two ULGs (Varanasi and Prayagraj)** are on track to meet the PM10 targets for 2024–25.
- Of the 38 ULGs with available data for 2024–25, **36 exceeded the targeted PM10 concentrations.**
- **28 ULGs recorded PM10 levels more than twice** their target concentration.
- **7 ULGs recorded levels more than three times** their target.

This pattern suggests systemic challenges in aligning ground-level outcomes with performance-based grant conditions.

2. Design factors affecting pollution levels

Air quality in urban centres is shaped by a complex interplay of factors, including:

- **Local emissions** from construction, transport, waste burning, and road dust within the city
- **Regional emissions** from surrounding areas that lie outside the ULG's jurisdiction
- **Meteorological conditions** such as wind speed, temperature inversions, and humidity levels, which affect pollutant dispersion.

While local sources contribute significantly to exposure levels within city boundaries, ULGs have limited jurisdiction or control over regional air-shed emissions or meteorological influences. As a result, even where ULGs implement localised emission-reduction efforts, unfavourable weather conditions or high regional pollution can negate progress and result in underperformance against grant targets.

Moreover, across the larger air-shed, the absence of sectoral emission reduction indicators leads to underutilisation of funds. This results in misallocation of funds, which are often used for physical infrastructure rather than emission reduction in urban centres and larger air-sheds.

¹⁷³ Based on conducted qualitative consultations with CPCB consultants in Varanasi, Patna, and Bengaluru; officials from SPCB and UDHD Patna; and staff across these ULGs to identify bottlenecks and opportunities for better utilisation of Finance Commission funds. We also met with officials at Commission for Air Quality Management in National Capital Region and Adjoining Areas to understand governance challenges, though inputs from ULGs under CAQM remain pending for validation.

3. Institutional and implementation bottlenecks

In addition to structural and design challenges, implementation capacity at the ULG level also hampers effectiveness. Despite functioning District-Level Implementation Committees (DLICs), key departments remain disengaged or inconsistent in follow-through, leading to implementation breakdowns. Air quality often remains a peripheral responsibility for them, rather than a core mandate. The lack of clearly assigned roles and accountability mechanisms results in weak inter-agency coordination and fragmented responses.

Further, late release of funds to ULGs has emerged as another significant operational barrier. Late disbursements create bottlenecks in contractor work due to funding discontinuity, undermining sustained efforts to curb pollution levels.

The lack of skilled manpower in ULGs was highlighted in stakeholder interviews. While individual Central Pollution Control Board (CPCB) consultants have been deployed for each ULG, they are often not integrated into municipal systems and have limited to no authority. This results in underutilisation of skilled manpower, fragmented planning, and weak implementation continuity.

Annexure 4.17: Recommendations for Strengthening Air Quality Management Through Finance Commission Grants

1. Create a dedicated sector-specific air quality grant

The XVI Finance Commission (FC) should create a separate performance-based grant category for 'Air Pollution', distinct from the existing Million-Plus Challenge Fund (MCF). This grant should be designed as a sector-specific performance grant, in line with other FC grants to states. Under this model:

- i. The overall responsibility for planning, monitoring, and delivering outcomes should rest with state governments, which can coordinate among relevant stakeholders across jurisdictions.
- ii. Monitoring and performance assessment should apply only to those interventions falling within the mandate of the respective entities, with flexibility for states to determine internal coordination and accountability mechanisms.

Key features of this new sector-specific air pollution grant include:

- a. **Expand eligibility beyond population thresholds:** Prioritise regions with significant population growth, covering both million-plus ULGs and other ULGs with poor air quality, based on monitoring data, including those with less than 5 years of data to ensure newly monitored pollution hotspots are not excluded.
- b. **Address emissions outside city limits:** Target pollution sources in surrounding areas such as industrial clusters, brick kilns, and construction sites.
- c. **Manage periphery and agglomeration areas independently:** Direct funds to eligible ULGs instead of routing them through larger metropolitan entities. This eliminates administrative bottlenecks and ensures smaller ULGs are not dependent on larger bodies for funding or approvals.
- d. **Avoid conflating air pollution work with developmental and service delivery work:** Interventions for air pollution must leverage specialised knowledge from broader urban development programmes, allowing for targeted technological interventions instead of being diluted within wider municipal services.

2. Establish a sub-grant for institutional capacity

The XVI FC should establish specific sub-grants under the air quality grant framework to address the fundamental capacity that have hampered effective air quality management.

Challenges with air quality management often stem from insufficient institutional capacity at the ULG and state levels, rather than a lack of intent. A specific percentage of the air quality grants should be dedicated to capacity building and institutional strengthening in state and other responsible agencies to achieve the targets set in 2020-21, during early implementation.

Key Components of this sub-grant include:

- i. **Technical expertise development:** Recruitment of full-time technical experts, including environmental engineers, data managers, and urban planners dedicated to air quality management.
- ii. **Establishment of Clean Air Cell:** To serve as the institutional backbone for proactive clean air governance within ULGs. These Cells must consist of permanent technical personnel, representatives of key line departments, and independent experts, and must facilitate multi-departmental coordination through:
 - a. Regular training programmes on air quality planning, monitoring, and data systems management
 - b. Public grievance redressal systems
 - c. Establishment and maintenance of CAAQM stations
 - d. Use of emission inventories and source apportionment data for planning, action and reporting on emission-load reduction indicators.
- iii. **Self-sustainability of Clean Air Cells:** Annual self-sustainability indicators and milestones should be linked to sub-grant allocation to build financial and institutional sustainability, for example:
 - a. Creation and retention of trained staff
 - b. Timely preparation and third-party validation of annual Clean Air Action Plans
 - c. Integration of air quality into urban planning documents like master plans and transport strategies
 - d. Inclusion of public health co-benefits into pollution management planning
 - e. Rethinking framework for demonstrated convergence between SBM, AMRUT, STPs, and NCAP funds.
- iv. **Data infrastructure development:** To facilitate transparent implementation, public reporting, and real-time monitoring.

This would address the governance vacuum and encourage ULGs to invest in administrative continuity, staff capacity, and planning systems.

3. Continue support for target-achieving ULGs

ULGs that have successfully achieved their air quality targets should continue to receive performance-linked funds, as they require sustained support to maintain progress and avoid reversal.

The goal should be to level the playing field, ensuring smaller ULGs with genuine intent and plans are not handicapped by lack of upfront funding.

4. Address delayed grant disbursement through process reforms

Grants to several ULGs were disbursed towards the end of the financial year, resulting in insufficient time for ULGs to plan work, issue tenders, and complete implementation. Late receipt of funds leads ULGs to prioritise large expenditures to project higher utilisation, rather than systematic action to reduce emissions.

Disbursement to ULGs should be completed within 2 months of the beginning of a financial year to ensure sufficient time for planning and executing systematic pollution reduction actions.

5. Develop additional performance parameters and indicators

The XVI FC should revamp the current performance-linked grant framework for air quality, moving beyond outcome-only indicators that have proven inadequate, such as PM₁₀ reduction or increase in good air quality days. The XVI FC should encourage the nodal ministry to develop a composite performance framework that evaluates ULGs on a mix of input, process, and output indicators, aligned with their contextual constraints.

i. Sectoral and departmental performance indicators

Allocate a portion of urban air quality grants to specific departmental contributions through mandatory MoUs between ULGs and key line departments within cities and at the state level. These MoUs should specify:

- a. Clear responsibilities and deliverables linked to emission load reduction
- b. Specific actions under City Clean Air Action Plans (CAAP) and State Action Plans (SAP)
- c. Performance targets informed by emission inventories and source apportionment studies
- d. Direct fiscal penalties for departments that fail to fulfil obligations.

ii. Institutional capacity indicators

- a. Inter-agency coordination mechanisms between ULGs, state departments, and regulatory bodies such as the Clean Air Cells.
- b. Install and maintain minimum 85% uptime of Continuous Ambient Air Quality Monitoring (CAAQM) stations.
- c. Actively use emission inventories and emission source analysis for action planning and resource allocation.
- d. Develop trained technical personnel and conduct regular capacity building programmes.

iii. Process indicators

- a. **Establish and maintain transparency on budget utilisation** through financial tracking systems that monitor fund allocation across air quality interventions, department-wise expenditure against MoUs, and quarterly cost variance analysis.

- b. **Establish integrated reporting** through regular data updates on the PRANA portal, linking performance measurement to systematic reporting of indicators as per action plans and MoUs to ensure accuracy and regularity.
- c. **Enable transparency and accountability** by quarterly publication of performance data on ULG websites, including inter-departmental meeting minutes, departmental performance against MoU targets, budget utilisation reports, and air quality trend analysis with action taken.

iv. Output indicators

- a. Restore focus on directly measuring both PM_{2.5} and PM₁₀ concentrations, while increasing the number of days with air quality within permissible limits, recognising that PM_{2.5} poses greater health risks.
- b. Define sectoral emission reduction targets aligned with city-specific emission source analysis.

By rewarding structural and systemic progress, ULGs laying strong institutional foundations or tackling governance bottlenecks will remain incentivised, even if pollution concentration reductions take time to materialise. This will shift focus from optics to operational depth and will ensure that performance-linked grants drive meaningful change.

Annexure 4.18: Analysis of Tied Grant Utilisation Across 2020–21 to 2023–24 — Trends by Year, Population Category, and State

Year-wise Tied Grant Utilisation Summary (2020–21 to 2023–24)					
Financial Year	Tied Grants Disbursed (INR crore)	Total Expenditure (INR crore)	Total Expenditure as % of Tied Grants Disbursed	Unutilised Tied Grants (INR crore)	Unutilised Grants as % of Tied Grants Disbursed
2020-21	6,256	1,198	19%	5,058	81%
2021-22	4,493	3,014	67%	1,478	33%
2022-23	5,824	3,848	66%	1,976	34%
2023-24	6,578	4,489	68%	2,089	32%
Total	16,573	8,060	49%	8,513	51%

Findings: The utilisation rate has increased significantly from 19% in 2020-21 to 68% in 2023-24, showing better fund management and execution over the years.

Tied Grant Utilisation (%) by Population Category (2020–21 to 2023–24)				
Population Category	2020-21	2021-22	2022-23	2023-24
>4 million	91%	98%	98%	98%
1-4 million	7%	30%	29%	37%
500K-1 million	18%	26%	28%	27%
100K - 500K	9%	27%	26%	19%
<100K	18%	29%	31%	31%
Total	19%	32%	31%	59%

Findings: Larger ULGs (population above 4 million) show higher utilisation rates, with an overall improving trend. While utilisation rates among smaller ULGs varied, the smallest category (population below 100,000) demonstrated a steady upward trend, reaching 31% in both 2022–23 and 2023–24.

Cumulative Tied Grant Utilisation by State (2020–21 to 2022–23)			
State name	Total tied grant (INR crore)	Total expenditure (INR crore)	% Tied grant utilisation
Andhra Pradesh	3,274	156	5%
Assam	1,499	185	12%
Bihar	7,100	1,487	21%
Chhattisgarh	573	18	3%
Gujarat	334	57	17%
Himachal Pradesh	419	116	28%
Karnataka	995	260	26%
Kerala	461	146	32%
Maharashtra	3,196	1,180	37%
Odisha	2,185	718	33%
Punjab	1,409	510	36%
Rajasthan	4,663	1,170	25%
Tamil Nadu	2,620	1,692	65%
Telangana	2,100	1,233	59%
Tripura	62	34	54%
Uttar Pradesh	11,830	3,414	29%
Uttarakhand	547	176	32%
Findings: States like Tripura, Tamil Nadu, and Telangana have higher utilisation rates (>50%), with Tamil Nadu achieving the highest utilisation (65%). While states like Andhra Pradesh, Chhattisgarh, Assam, Bihar & Gujarat show lower utilisation rates(<25%), indicating potential issues in absorptive capacities and project execution.			

Source: Based on the DUR data sourced from CityFinance as on 10-06-2024.

Annexure 4.19.1: Sector-wise Utilisation of Tied Grants by Year and Population Category (2020–21 to 2023–24)

Year-wise Sectoral Utilisation of Tied Grants (2020–21 to 2023–24)				
Financial Year	Expenditure on Water Management (WM) (INR crore)	Expenditure on Sanitation (INR crore)	% Share of Water Management in Total Expenditure	% Share of Sanitation in Total Expenditure
2020-21	310	888	26%	74%
2021-22	936	2,078	31%	69%
2022-23	1,270	2,578	33%	67%
2023-24	3,259	1,230	73%	27%
Total	5,775	6,775	46%	54%
Findings: Sanitation accounts for a significant share of expenditure, although its proportion declined from 74% in 2020–21 to 27% in 2023–24. In contrast, expenditure on water management increased significantly year-on-year, rising from ₹310 crore in 2020–21 to ₹3,259 crore in 2023–24.				

Cumulative Sector-wise Utilisation of Tied Grants by Population Category (2020–21 to 2023–24)				
Population Category	Water Management (INR crore)	Sanitation (INR crore)	% Share of Water Management in Total Expenditure	% Share of Sanitation in Total Expenditure
>4 million	450	1,204	27%	73%
1-4 million	1,046	1,027	50%	50%
500K-1 million	647	657	50%	50%
100K - 500K	1,201	1,277	48%	52%
<100K	2,432	2,609	48%	52%
Total	5,775	6,775	46%	54%
Findings: ULGs with populations above 4 million have utilised 73% of their funds on sanitation. ULGs with populations between 1 million and 4 million show an even split, with 50% of funds allocated to sanitation. This may be due to the fact that water supply is typically managed by parastatal agencies in larger urban centres.				
Smaller ULGs (population below 500k) exhibit a more balanced distribution between water management and sanitation, with 48–50% of funds directed toward water management.				

Source: Based on the DUR data sourced from CityFinance as on 10-06-2024.

Annexure 4.19.2: Sector-wise Utilisation of Tied Grants by State (2020–21 to 2023–24)

Cumulative Sector-wise Utilisation of Tied Grants by State (2020–21 to 2023–24)				
State	Water Management (INR crore)	Sanitation (INR crore)	% Share of Water Management in Total Expenditure	% Share of Sanitation in Total Expenditure
Andhra Pradesh	70	85	45%	55%
Assam	101	85	54%	46%
Bihar	647	840	43%	57%
Chhattisgarh	8	10	44%	56%
Gujarat	36	21	64%	36%
Himachal Pradesh	56	59	49%	51%
Karnataka	133	127	51%	49%
Kerala	69	77	47%	53%
Maharashtra	556	624	47%	53%
Odisha	392	325	55%	45%
Punjab	261	249	51%	49%
Rajasthan	433	737	37%	63%
Tamil Nadu	717	975	42%	58%
Telangana	369	864	30%	70%
Tripura	13	21	39%	61%
Uttar Pradesh	1,832	1,582	54%	46%
Uttarakhand	81	95	46%	54%
Total	3,948	7,390	35%	65%

Findings:

High Water Management Expenditure: States such as Uttar Pradesh, Odisha, Assam, and Gujarat have allocated a higher share of funds to water management, each exceeding 53% of total tied grant expenditure.

Balanced Allocation: States like Punjab, Karnataka, and Madhya Pradesh show a relatively even distribution between water management and sanitation.

Sanitation-Focused States: Tripura, Rajasthan, and Telangana have a marked skew towards sanitation, with over 60% of their funds utilised in this sector.

Source: Based on the DUR data sourced from CityFinance as on 10-06-2024.

Annexure 4.20: Grant Utilisation in 141 ULGs of Telangana (2021–22 to 2023–24)

Population Category	Tied Grants Released under XV FC (INR crore)	Tied Grants Utilised (INR crore)	Tied Grant Utilisation Rate (%)	Untied Grants Released under XV FC (INR crore)	Untied Grants Utilised (INR crore)	Untied Grant Utilisation Rate (%)
500K-1 million	50	33	66%	33	25	76%
100K-500K	121	69	57%	80	64	80%
<100K	299	153	51%	198	152	77%
Total	470	254	54%	311	241	77%

Source: Received from Telangana CDMA in October 2024.

Note: The analysis of tied and untied utilisation includes only NMPC grants. Therefore, grants allocated and released to Hyderabad UA have not been considered in this analysis.

Annexure 4.21: Grant Utilisation in 444 ULGs of Maharashtra (2020–21 to 2024–25)

Total Grants Released, Expenditure Incurred, and Utilisation Rate (2020–21 to 2024–25)			
	Grant Released (INR crore)	Total Expenditure (INR crore)	Utilisation Rate
Tied grant	4,452	1,812	41%
Untied grant	1,559	928	60%

Cumulative Sector-wise Expenditure from Tied and Untied Grants (2020–21 to 2024–25)				
Sector	Tied Grants (INR crore)	% Share of Tied Grants	Untied Grants (INR crore)	% Share of Untied Grants
Drinking water supply	447	25%	56	6%
Sanitation (including septic management)	136	7%	7	1%
Sewage and solid waste management	1,063	59%	97	10%
Stormwater drainage	3	0%	3	0%
Maintenance of community assets	3	0%	7	1%
Maintenance of roads and footpaths	16	1%	10	1%
Electricity	68	4%	536	58%
Burial grounds	0	0%	0	0%
Cremation grounds	0	0%	0	0%
Women and child development-related issues	0	0%	0	0%
Others	76	4%	213	23%

Source: Data collected from UDD Maharashtra, as on date 27-01-2025

Annexure 5.1: Service Level Benchmarks and Targets as per MoHUA's Handbook (2008)

Indicators	Benchmark
Water Supply	
Coverage of water supply connections	100%
Per capita supply of water	135 lpcd
Extent of metering of water connections	100%
Extent of non-revenue water (NRW)	20%
Continuity of water supply	24 hours
Quality of water supplied	100%
Efficiency in redressal of customer complaints	80%
Cost recovery in water supply services	100%
Efficiency in collection of water supply-related charges	90%
Sewage Management	
Coverage of toilets	100%
Coverage of sewage network services	100%
Collection efficiency of the sewage network	100%
Adequacy of sewage treatment capacity	100%
Quality of sewage treatment	100%
Extent of reuse and recycling of sewage	20%
Efficiency in redressal of customer complaints	80%
Extent of cost recovery in sewage management	100%
Efficiency in collection of sewage charges	90%
Solid Waste Management (SWM)	
Household level coverage of solid waste management services	100%
Efficiency of collection of municipal solid waste	100%
Extent of segregation of municipal solid waste	100%
Extent of municipal solid waste recovered	80%
Extent of scientific disposal of municipal solid waste	100%
Efficiency in redressal of customer complaints	80%
Extent of cost recovery in SWM services	100%
Stormwater Drainage	
Coverage of stormwater drainage network	100%
Incidence of water logging/flooding	0

Annexure 5.2: Service Level Benchmarks (SLBs) Mandated by the XV Finance Commission for Measuring Urban Service Delivery Performance

Indicators
Water Supply
Households covered with piped water supply
Water supplied (litre per capita per day)
Reduction in non-revenue water
Water Conservation Measures
Rainwater harvesting
Reuse/recycling of water
Rejuvenation of water bodies
Solid Waste Management and Sustaining Outcomes of Swachh Bharat Mission
Garbage-free star rating of cities
Coverage of water supply for public/community toilets

Source: XV Finance Commission Report, Annexure 79, p. 750

Annexure 5.3: Number of ULGs Submitting SLB

	ULGs with Data in 2020-21		ULGs with Data in 2021-22		ULGs with Data in 2022-23		ULGs with Data in 2023-24	
Population Category	Number	%	Number	%	Number	%	Number	%
>4 million	7	100%	7	100%	7	100%	6	86%
1-4 million	35	97%	35	97%	36	100%	35	97%
500K-1 million	44	100%	42	95%	41	93%	35	80%
100K-500K	374	99%	351	93%	343	91%	284	75%
<100K	4,051	93%	3,853	88%	3,802	87%	3,197	73%
Total	4,511	94%	4,288	89%	4,228	88%	3,557	74%

Source: CityFinance as on July 2025

Note: The number of ULGs with SLB data includes those that have accessed the portal and initiated data entry, including entries currently under review. Percentages are calculated based on the total number of ULGs active in the respective year.

Annexure 5.4: Performance of 43 Municipal Performance Committees (MPCs) on SLBs Linked to the Million-Plus Challenge Fund

Indicators	No. of ULGs (43 MPCs with available data considered)		
	Number	%	Number
Coverage of water supply connections	35 (81%)	3 (7%)	5 (12%)
Per capita supply of water	25 (58%)	10 (23%)	8 (19%)
Extent of non-revenue water	42 (98%)	0	1 (2%)
Coverage of waste-water network services	29 (67%)	10 (23%)	4 (9%)
ODF Rating	5 (12%)	37 (86%)	1 (2%)
GFC Rating	5 (12%)	38 (88%)	0

Source: CityFinance as on March 2025. Performance data pertains to the financial year 2022–23.

Annexure 5.5.1: State-wise Allocation (A) and Release (R) of XV FC MPC and NPMC Grants for 2020–21 (as on 31 March 2025)

2020-21									
Sl. No.	State Name	MPC (INR crore)		NMPC-Tied (INR crore)		NMPC-Untied (INR crore)		Total (INR crore)	
		A	R	A	R	A	R	A	R
1	Andhra Pradesh	135	135	497	497	497	497	1,129	1,129
2	Arunachal Pradesh	-	-	56	56	56	56	111	111
3	Assam	-	-	386	386	386	386	772	772
4	Bihar	204	204	1,004	1,004	1,004	1,004	2,212	2,212
5	Chhattisgarh	107	107	243	243	243	243	593	593
6	Goa	-	-	18	18	18	18	36	36
7	Gujarat	405	405	364	364	364	364	1,133	1,133
8	Haryana	48	48	257	257	257	257	561	561
9	Himachal Pradesh	-	-	104	104	104	104	207	207
10	Jharkhand	159	159	248	248	248	248	654	654
11	Karnataka	279	279	496	496	496	496	1,270	1,270
12	Kerala	339	339	223	223	223	223	784	784
13	Madhya Pradesh	299	299	660	660	660	660	1,619	1,619
14	Maharashtra	793	793	610	610	610	610	2,013	2,013
15	Manipur	-	-	43	43	43	43	85	85
16	Meghalaya	-	-	44	44	44	44	88	88
17	Mizoram	-	-	23	23	23	23	45	45
18	Nagaland	-	-	30	30	30	30	60	60
19	Odisha	-	-	544	544	544	544	1,087	1,087
20	Punjab	90	90	244	244	244	244	578	578
21	Rajasthan	281	281	649	649	649	649	1,578	1,578
22	Sikkim	-	-	10	10	10	10	20	20
23	Tamil Nadu	323	323	591	591	591	591	1,504	1,504
24	Telangana	234	234	211	211	211	211	655	655
25	Tripura	-	-	46	46	46	46	92	92
26	Uttar Pradesh	714	714	1,634	1,634	1,634	1,634	3,981	3,981
27	Uttarakhand	-	-	139	139	139	139	278	278
28	West Bengal	419	419	643	643	643	643	1,705	1,705
	Total	4,829	4,829	10,011	10,011	10,011	10,011	24,850	24,850

Source: Information based on CityFinance data as on 31-03-2025.

Note: The MPC grants excludes the excludes the air quality allocation.

Annexure 5.5.2: State-wise Allocation (A) and Release (R) of XV FC MPC and NPMC Grants for 2021-22 (as on 31 March 2025)

2021-22									
Sl. No.	State Name	MPC (INR crore)		NMPC-Tied (INR crore)		NMPC-Untied (INR crore)		Total (INR crore)	
		A	R	A	R	A	R	A	R
1	Andhra Pradesh	136	136	451	451	301	301	888	888
2	Arunachal Pradesh	-	-	50	0	34	0	84	0
3	Assam	-	-	350	350	234	234	584	584
4	Bihar	206	206	911	911	607	607	1,724	1,724
5	Chhattisgarh	109	109	220	220	147	147	476	476
6	Goa	-	-	16	16	11	11	27	27
7	Gujarat	408	408	331	331	220	220	959	959
8	Haryana	49	49	232	232	155	155	436	436
9	Himachal Pradesh	-	-	94	94	62	62	156	156
10	Jharkhand	161	161	224	224	150	150	535	535
11	Karnataka	281	281	450	450	300	300	1,031	1,031
12	Kerala	256	256	202	202	134	134	592	592
13	Madhya Pradesh	301	301	599	599	399	399	1,299	1,299
14	Maharashtra	799	799	553	553	369	369	1,721	1,721
15	Manipur	-	-	38	0	26	0	64	0
16	Meghalaya	-	-	40	40	26	26	66	66
17	Mizoram	-	-	20	20	14	14	34	34
18	Nagaland	-	-	27	14	18	15	45	28
19	Odisha	-	-	493	493	329	329	822	822
20	Punjab	90	90	222	222	148	148	460	460
21	Rajasthan	284	284	589	589	392	392	1,265	1,265
22	Sikkim	-	0	9	9	6	6	15	15
23	Tamil Nadu	303	303	536	536	357	357	1,196	1,196
24	Telangana	236	236	191	191	127	127	554	554
25	Tripura	-	-	42	42	28	28	70	70
26	Uttar Pradesh	720	720	1,482	1,482	988	988	3,190	3,190
27	Uttarakhand	-	-	125	125	84	84	209	209
28	West Bengal	422	422	584	584	389	389	1,395	1,395
	Total	4,761	4,761	9,082	8,979	6,054	5,992	19,897	19,732

Source: Information based on CityFinance data as on 31-03-2025.

Note: The MPC grants excludes the excludes the air quality allocation.

Annexure 5.5.3: State-wise Allocation (A) and Release (R) of XV FC MPC and NPMC Grants for 2022–23 (as on 31 March 2025)

2022-23									
Sl. No.	State Name	MPC (INR crore)		NPMC-Tied (INR crore)		NPMC-Untied (INR crore)		Total (INR crore)	
		A	R	A	R	A	R	A	R
1	Andhra Pradesh	141	141	467	467	312	312	920	920
2	Arunachal Pradesh	-	-	52	0	35		87	0
3	Assam	-	-	363	363	242	242	605	605
4	Bihar	213	213	943	943	629	629	1,785	1,785
5	Chhattisgarh	113	108	228	228	152	152	493	488
6	Goa	-	-	17	17	11	11	28	28
7	Gujarat	422	422	343	343	228	228	993	993
8	Haryana	51	51	241	240	160	160	452	451
9	Himachal Pradesh	-	-	97	97	65	65	162	162
10	Jharkhand	166	166	233	233	155	155	554	554
11	Karnataka	291	291	466	466	311	311	1,068	1,068
12	Kerala	265	265	209	209	139	139	613	613
13	Madhya Pradesh	311	311	620	620	414	414	1,345	1,345
14	Maharashtra	827	827	573	573	382	382	1,782	1,782
15	Manipur	-	-	40	0	27	0	67	0
16	Meghalaya	-	-	41	0	28	0	69	0
17	Mizoram	-	-	21	21	14	14	35	35
18	Nagaland	-	-	28	0	19	0	47	0
19	Odisha	-	-	511	511	340	340	851	851
20	Punjab	93	93	230	230	153	153	476	476
21	Rajasthan	294	294	610	610	406	406	1,310	1,310
22	Sikkim	-	-	10	5	6	3	16	8
23	Tamil Nadu	313	313	555	555	370	370	1,238	1,238
24	Telangana	245	245	198	198	132	132	575	575
25	Tripura	-	-	43	43	29	29	72	72
26	Uttar Pradesh	746	746	1,535	1,535	1,023	1,023	3,304	3,304
27	Uttarakhand	-	-	130	130	87	87	217	217
28	West Bengal	437	437	605	605	403	403	1,445	1,445
	Total	4,928	4,923	9,409	9,241	6,272	6,161	20,609	20,325

Source: Information based on CityFinance data as on 31-03-2025.

Note: The MPC grants excludes the excludes the air quality allocation.

Annexure 5.5.4: State-wise Allocation (A) and Release (R) of XV FC MPC and NPMC Grants for 2023-24 (as on 31 March 2025)

2023-24									
Sl. No.	State Name	MPC (INR crore)		NPMC-Tied (INR crore)		NPMC-Untied (INR crore)		Total (INR crore)	
		A	R	A	R	A	R	A	R
1	Andhra Pradesh	149	149	494	366	329	244	972	759
2	Arunachal Pradesh	-	-	55	0	37	0	92	0
3	Assam	-	-	384	384	256	255	640	639
4	Bihar	225	225	998	992	665	661	1,888	1,878
5	Chhattisgarh	118	0	241	72	161	48	520	120
6	Goa	-	-	18	0	12	0	30	0
7	Gujarat	448	366	362	181	241	121	1,051	668
8	Haryana	54	0	254	127	169	104	477	231
9	Himachal Pradesh	-	-	103	95	68	63	171	158
10	Jharkhand	176	0	246	-	164	-	586	-
11	Karnataka	307	0	493	384	328	256	1,128	640
12	Kerala	281	155	221	214	147	143	649	513
13	Madhya Pradesh	330	330	656	326	437	217	1,423	873
14	Maharashtra	875	0	606	297	404	198	1,885	495
15	Manipur	-	-	43	0	28	0	71	0
16	Meghalaya	-	-	44	0	29	0	73	0
17	Mizoram	-	-	22	11	15	15	37	26
18	Nagaland	-	-	30	0	20	0	50	0
19	Odisha	-	-	540	508	360	339	900	847
20	Punjab	98	92	243	226	162	149	503	467
21	Rajasthan	311	311	644	449	430	300	1,385	1,060
22	Sikkim	-	-	10	0	7	0	17	0
23	Tamil Nadu	331	325	587	576	391	384	1,309	1,286
24	Telangana	259	259	209	186	140	121	608	566
25	Tripura	-	-	46	46	30	30	76	76
26	Uttar Pradesh	788	715	1,623	1,511	1,082	1,008	3,493	3,234
27	Uttarakhand	-	-	137	132	92	87	229	219
28	West Bengal	462	462	640	214	426	143	1,528	819
	Total	5,212	3,391	9,947	7,297	6,632	4,886	21,791	15,573

Source: Information based on CityFinance data as on 31-03-2025.

Note: The MPC grants excludes the excludes the air quality allocation.

Annexure 5.5.5: State-wise Allocation (A) and Release (R) of XV FC MPC and NPMC Grants for 2024-25 (as on 31 March 2025)

2024-25									
Sl. No.	State Name	MPC (INR crore)		NPMC-Tied (INR crore)		NPMC-Untied (INR crore)		Total (INR crore)	
		A	R	A	R	A	R	A	R
1	Andhra Pradesh	158	0	523	4	349	3	1,030	7
2	Arunachal Pradesh	-	-	58	0	39	0	97	0
3	Assam	-	-	406	69	271	46	677	114
4	Bihar	239	239	1,057	833	704	555	2,000	1,627
5	Chhattisgarh	126	126	255	0	170	0	551	126
6	Goa	-	-	19	0	13	0	32	0
7	Gujarat	474	433	383	0	256	0	1,113	433
8	Haryana	57	0	269	0	180	0	506	0
9	Himachal Pradesh	0	-	109	104	72	69	181	173
10	Jharkhand	186	0	260	0	174	0	620	0
11	Karnataka	325	0	522	217	348	145	1,195	362
12	Kerala	297	0	234	0	156	78	687	78
13	Madhya Pradesh	350	290	695	0	463	0	1,508	290
14	Maharashtra	928	0	642	0	428	0	1,998	0
15	Manipur	-	-	45	0	30	0	75	0
16	Meghalaya	-	-	46	0	31	0	77	0
17	Mizoram	-	-	23	0	16	0	39	0
18	Nagaland	-	-	32	0	21	0	53	0
19	Odisha	-	-	572	480	381	320	953	801
20	Punjab	105	85	257	196	172	131	534	412
21	Rajasthan	328	328	683	325	455	216	1,466	869
22	Sikkim	-	-	11	0	7	0	18	0
23	Tamil Nadu	350	350	622	584	414	389	1,386	1,323
24	Telangana	274	274	221	69	148	92	643	434
25	Tripura	-	-	49	49	32	32	81	81
26	Uttar Pradesh	836	710	1,719	1,490	1,146	993	3,701	3,193
27	Uttarakhand	-	-	146	0	97	0	243	0
28	West Bengal	489	0	677	0	452	0	1,618	0
	Total	5,522	2,836	10,536	4,418	7,024	3,069	23,082	10,322

Source: Information based on CityFinance data as on 31-03-2025.

Note: The MPC grants excludes the excludes the air quality allocation.

Annexure 5.6: Grant Release Percentage Based on Fulfilment of Eligibility Conditions in FY 2023–24 (as on 31 March 2025)

State	Total No. of ULGs	% ULGs Meeting AFS Conditions	Estimated AFS Grant (INR crore)	% ULGs Meeting AFS + Property Tax (GR) Conditions	Estimated AFS + Property Tax (GR) Grant (INR crore)	% ULGs Meeting AFS + Property Tax (GR) + Duly Elected Conditions	Estimated AFS + Property Tax GR + Duly Elected Grant (INR crore)	% ULGs Meeting AFS + Property Tax (GR) + Duly Elected + DUR Conditions	Estimated AFS + Property Tax (GR) + Duly Elected + DUR Grant (INR crore)
Andhra Pradesh	121	100%	823	94%	803	76%	610	75%	601
Arunachal Pradesh	31	0%	0	0%	0	0%	0	0%	0
Assam	104	100%	640	78%	566	78%	566	78%	566
Bihar	261	100%	1663	54%	1,316	54%	1,316	54%	1,316
Chhattisgarh	167	100%	364	90%	343	89%	341	83%	322
Goa	14	100%	6	0%	0	0%	0	0%	0
Gujarat	162	100%	600	44%	327	23%	239	23%	239
Haryana	88	100%	0	84%	0	0%	0	0%	0
Himachal Pradesh	66	100%	171	82%	159	82%	159	82%	159
Jharkhand	47	100%	410	96%	394	96%	394	96%	394
Karnataka	315	100%	821	93%	782	66%	580	66%	580
Kerala	87	100%	209	94%	195	94%	195	94%	195
Madhya Pradesh	414	100%	993	52%	545	52%	545	52%	545
Maharashtra	421	100%	1,094	98%	963	31%	163	31%	163
Manipur	27	0%	0	0%	0	0%	0	0%	0
Meghalaya	7	0%	0	0%	0	0%	0	0%	0
Mizoram	2	100%	37	50%	31	50%	31	50%	31
Nagaland	39	0%	0	0%	0	0%	0	0%	0
Odisha	115	100%	900	91%	826	90%	745	89%	743
Punjab	167	100%	1,050	93%	386	92%	384	91%	382
Rajasthan	209	100%	911	57%	586	57%	586	57%	586
Sikkim	7	0%	0	0%	0	0%	0	0%	0
Tamil Nadu	647	100%	1,092	100%	978	100%	976	100%	976
Telangana	142	100%	349	87%	315	85%	303	85%	303

State	Total No. of ULGs	% ULGs Meeting AFS Conditions	Estimated AFS Grant (INR crore)	% ULGs Meeting AFS + Property Tax (GR) Conditions	Estimated AFS + Property Tax (GR) Grant (INR crore)	% ULGs Meeting AFS + Property Tax (GR) + Duly Elected Conditions	Estimated AFS + Property Tax GR + Duly Elected Grant (INR crore)	% ULGs Meeting AFS + Property Tax (GR) + Duly Elected + DUR Conditions	Estimated AFS + Property Tax (GR) + Duly Elected + DUR Grant (INR crore)
Tripura	20	100%	76	100%	76	100%	76	100%	76
Uttar Pradesh	768	100%	2,705	52%	1,733	52%	1,733	52%	1,733
Uttarakhand	111	100%	288	77%	206	77%	206	77%	206
West Bengal	126	100%	1039	75%	753	68%	706	68%	706
Total	4,685	97%	15,416	74%	12,282	63%	10,857	63%	10,825

Source: CityFinance as on 31-03-2025.

Note: For the year 2023–24, the analysis assessed Urban Local Governments (ULGs) against four eligibility conditions mandated for grant disbursement: (i) publication of Audited Financial Statements (AFS), (ii) demonstration of property tax growth rate in line with the state's GSDP growth rate, and (iii) presence of a duly elected municipal body (iv) publish Detailed Utilisation Report (DUR). ULGs were grouped by the number of conditions met (one, two, three or all four) to identify which specific conditions most affected eligibility and disbursement outcomes.

Annexure 6.1: Total Revenue (TR), Own Source Revenue (OSR), and Property Tax by Population Category

Population Category	Number of ULGs	Population	Total Own Revenue (INR crore)	Total Revenue (INR crore)	% Share of OSR to TR	Property Tax (INR crore)	Property Tax Per Capita (INR)
>4 million	7	4,68,07,001	51,425	72,747	71%	9,642	2,060
500K-4 million	76	8,06,65,428	31,587	53,019	60%	11,154	1383
<500K	3,720	15,34,13,171	15,620	47,744	33%	5,365	350

Source: Analysis based on audited financial statements of 3,803 ULGs for 2021-22 from CityFinance.

Annexure 6.2: ULGs with Population above 4 Million as per the 2011 Census

Sl. No.	ULG	State	Population as per Census 2011
1	Kolkata Municipal Corporation	West Bengal	44,96,694
2	Brihanmumbai Municipal Corporation	Maharashtra	1,24,42,373
3	Bruhat Bengaluru Mahanagara Palike	Karnataka	84,43,675
4	Amdavad Municipal Corporation	Gujarat	55,77,940
5	Greater Chennai Corporation	Tamil Nadu	46,46,732
6	Greater Hyderabad Municipal Corporation	Telangana	67,31,790
7	Surat Municipal Corporation	Gujarat	44,67,797

Annexure 6.3: ULGs with 500k–4 Million Population as per CityFinance

Sl. No.	ULG	State	Population as per Census 2011
1	Pune Municipal Corporation	Maharashtra	31,24,458
2	Lucknow Nagar Nigam	Uttar Pradesh	28,17,105
3	Kanpur Municipal Corporation	Uttar Pradesh	27,65,348
4	Nagpur Municipal Corporation	Maharashtra	24,05,665
5	Indore Municipal Corporation	Madhya Pradesh	19,64,086
6	Thane Municipal Corporation	Maharashtra	18,41,488
7	Bhopal Municipal Corporation	Madhya Pradesh	17,98,218
8	Greater Visakhapatnam Municipal Corporation	Andhra Pradesh	17,28,128
9	Pimpri-Chinchwad Municipal Corporation	Maharashtra	17,27,692
10	Patna Municipal Corporation	Bihar	16,84,222
11	Vadodara Municipal Corporation	Gujarat	16,70,806
12	Ghaziabad Municipal Corporation	Uttar Pradesh	16,48,643
13	Municipal Corporation Ludhiana	Punjab	16,18,879
14	Agra Municipal Corporation	Uttar Pradesh	15,85,704
15	Jaipur Municipal Corporation Greater	Rajasthan	15,23,081
16	Municipal Corporation Jaipur Heritage	Rajasthan	15,23,081
17	Nashik Municipal Corporation	Maharashtra	14,86,053
18	Municipal Corporation Faridabad	Haryana	14,14,050
19	Meerut Municipal Corporation	Uttar Pradesh	13,05,429
20	Rajkot Municipal Corporation	Gujarat	12,86,678
21	Kalyan-Dombivli Municipal Corporation	Maharashtra	12,47,327
22	Vasai-Virar City Municipal Corporation	Maharashtra	12,22,390
23	Varanasi Nagar Nigam	Uttar Pradesh	11,98,491
24	Aurangabad Municipal Corporation	Maharashtra	11,75,116
25	Dhanbad Municipal Corporation	Jharkhand	11,62,472
26	Amritsar Municipal Corporation	Punjab	11,32,383
27	Navi Mumbai Municipal Corporation	Maharashtra	11,20,547
28	Prayagraj Municipal Corporation	Uttar Pradesh	11,12,544
29	Howrah Municipal Corporation	West Bengal	10,77,075

Sl. No.	ULG	State	Population as per Census 2011
30	Ranchi Municipal Corporation	Jharkhand	10,73,427
31	Jabalpur Municipal Corporation	Madhya Pradesh	10,55,525
32	Gwalior Municipal Corporation	Madhya Pradesh	10,54,420
33	Coimbatore City Municipal Corporation	Tamil Nadu	10,50,721
34	Vijayawada Municipal Corporation	Andhra Pradesh	10,34,358
35	Corporation of Madurai	Tamil Nadu	10,17,865
36	Raipur Municipal Corporation	Chhattisgarh	10,10,433
37	Guwahati Municipal Corporation	Assam	9,57,352
38	Solapur Municipal Corporation	Maharashtra	9,51,558
39	Hubballi-Dharwad Municipal Corporation	Karnataka	9,43,788
40	Bareilly Municipal Corporation	Uttar Pradesh	90,36,68
41	Mysore City Corporation	Karnataka	8,93,062
42	Moradabad Nagar Nigam	Uttar Pradesh	8,87,871
43	Gurugram Municipal Corporation	Haryana	8,76,969
44	Aligarh Municipal Corporation	Uttar Pradesh	8,74,408
45	Jalandhar Municipal Corporation	Punjab	8,62,886
46	Tiruchirappalli City Municipal Corporation	Tamil Nadu	8,47,387
47	Bhubaneswar Municipal Corporation	Odisha	8,43,402
48	Salem City Municipal Corporation	Tamil Nadu	8,29,267
49	Mira Bhayandar Municipal Corporation	Maharashtra	8,09,378
50	Thiruvananthapuram Municipal Corporation	Kerala	7,43,691
51	Bhiwandi Municipal Corporation	Maharashtra	7,09,665
52	Saharanpur Municipal Corporation	Uttar Pradesh	7,05,478
53	Gorakhpur Municipal Corporation	Uttar Pradesh	6,73,446
54	Guntur Municipal Corporation	Andhra Pradesh	6,47,508
55	Amravati Municipal Corporation	Maharashtra	6,47,057
56	Bikaner Municipal Corporation	Rajasthan	6,44,406
57	Jamshedpur Notified Area Council	Jharkhand	6,31,364
58	Bhilai Municipal Corporation	Chhattisgarh	6,25,700
59	Warangal Municipal Corporation	Telangana	6,15,998
60	Cuttack Municipal Corporation	Odisha	6,10,189

Sl. No.	ULG	State	Population as per Census 2011
61	Firozabad Municipal Corporation	Uttar Pradesh	6,04,214
62	Kochi Municipal Corporation	Kerala	6,02,046
63	Bhavnagar Municipal Corporation	Gujarat	5,93,368
64	Dehradun Nagar Nigam	Uttarakhand	5,69,578
65	Durgapur Municipal Corporation	West Bengal	5,66,517
66	Asansol Municipal Corporation	West Bengal	5,63,917
67	Nanded-Waghala City Municipal Corporation	Maharashtra	5,50,439
68	Kolhapur Municipal Corporation	Maharashtra	5,49,236
69	Ajmer Municipal Corporation	Rajasthan	5,42,321
70	Kalaburagi City Corporation	Karnataka	5,33,587
71	Jodhpur North Municipal Corporation	Rajasthan	5,16,878
72	Jodhpur South Municipal Corporation	Rajasthan	5,16,878
73	Loni Nagar Palika Parishad	Uttar Pradesh	5,16,082
74	Ujjain Municipal Corporation	Madhya Pradesh	5,15,215
75	Siliguri Municipal Corporation	West Bengal	5,13,264
76	Ulhasnagar Municipal Corporation	Maharashtra	5,06,098
77	Jhansi Municipal Corporation	Uttar Pradesh	5,05,693
78	Sangli-Miraj-Kupwad Municipal Corporation	Maharashtra	5,02,793
79	Kota North Municipal Corporation	Rajasthan	5,00,847
80	Kota South Municipal Corporation	Rajasthan	5,00,847

Annexure 6.4: Growth Rate of Property Tax Collection for ULGs with 500k–4 Million Population

	Growth Rate Category (FY 2019-20)					Growth Rate Category (FY 2020-21)					Growth Rate Category (FY 2021-22)				
States	0 to 5%	5% to 10%	Greater than 10%	Negative Growth Rate	Grand Total	0 to 5%	5% to 10%	Greater than 10%	Negative Growth Rate	Grand Total	0 to 5%	5% to 10%	Greater than 10%	Negative Growth Rate	Grand Total
Andhra Pradesh				3	3	1		2		3			1	2	3
Assam				1	1			1		1				1	1
Chhattisgarh	1		1		2			1	1	2			2		2
Gujarat	1		1	3	5	1		1	3	5	1		4		5
Jharkhand			2		2				2	2		1	1		2
Karnataka				1	1				1	1			1		1
Kerala				1	1				1	1				1	1
Madhya Pradesh		1	2	2	5			3	2	5			4	1	5
Maharashtra	2	2	1	3	8		2	3	3	8	1		6	1	8
Odisha			2		2		1		1	2			1	1	2
Rajasthan				2	2				2	2			1	1	2
Tamil Nadu			2	1	3			1	2	3	1		1	1	3
Telangana		1	1		2		1		1	2			1	1	2
Uttar Pradesh		1	4	4	9	2	1	5	1	9	1	1	4	3	9
Grand Total	4	5	16	21	46	4	5	17	20	46	4	2	27	13	46

Source: Analysis based on city budgets sourced from CityFinance Rankings, as on August 2024.

Annexure 6.5: Percentage Share of XVI FC Grant Allocation in Relation to the Budget Size of ULGs with 500K–4 Million Population

ULG	Grant Allocation 2026-31 (INR crore)	Per Year (INR crore)	Budget Size 2021-22 (INR crore)	Grant as a Share of Budget Size (%)
Pune Municipal Corporation	3,451	690	6,807	3%
Lucknow Nagar Nigam	3,112	622	964	19%
Kanpur Municipal Corporation	3,054	611	1,068	17%
Nagpur Municipal Corporation	2,657	531	2,290	7%
Indore Municipal Corporation	2,169	434	1,762	7%
Thane Municipal Corporation	2,034	407	3,505	3%
Bhopal Municipal Corporation	1,986	397	1,626	7%
Greater Visakhapatnam Municipal Corporation	1,909	382	1,164	10%
Pimpri-Chinchwad Municipal Corporation	1,908	382	3,867	3%
Vadodara Municipal Corporation	1,845	369	1,846	6%
Ghaziabad Municipal Corporation	1,821	364	683	16%
Rajkot Municipal Corporation	1,421	284	613	14%
Vasai-Virar City Municipal Corporation	1,350	270	1,365	6%
Varanasi Nagar Nigam	1,324	265	337	24%
Dhanbad Municipal Corporation	1,284	257	189	41%
Navi Mumbai Municipal Corporation	1,238	248	2,557	3%
Prayagraj Municipal Corporation	1,229	246	483	15%
Ranchi Municipal Corporation	1,186	237	236	30%
Jabalpur Municipal Corporation	1,166	233	524	13%
Gwalior Municipal Corporation	1,165	233	778	9%
Coimbatore City Municipal Corporation	1,161	232	1,393	5%
Vijayawada Municipal Corporation	1,142	228	578	12%
Raipur Municipal Corporation	1,116	223	742	9%
Guwahati Municipal Corporation	1,057	211	369	17%
Hubballi-Dharwad Municipal Corporation	1,042	208	452	14%
Bareilly Municipal Corporation	998	200	261	23%

ULG	Grant Allocation 2026-31 (INR crore)	Per Year (INR crore)	Budget Size 2021-22 (INR crore)	Grant as a Share of Budget Size (%)
Moradabad Nagar Nigam	981	196	223	26%
Bhubaneswar Municipal Corporation	932	186	583	10%
Salem City Municipal Corporation	916	183	497	11%
Mira Bhayandar Municipal Corporation	894	179	1,333	4%
Saharanpur Municipal Corporation	779	156	170	27%
Guntur Municipal Corporation	715	143	498	9%
Cuttack Municipal Corporation	674	135	484	8%
Bhilai Municipal Corporation	691	138	236	18%
Warangal Municipal Corporation	680	136	247	17%
Firozabad Municipal Corporation	667	133	167	24%
Kochi Municipal Corporation	665	133	659	6%
Bhavnagar Municipal Corporation	655	131	574	7%
Kolhapur Municipal Corporation	607	121	398	9%
Ajmer Municipal Corporation	599	120	197	18%
Jodhpur North Municipal Corporation	571	114	163	21%
Ujjain Municipal Corporation	569	114	387	9%

Note: The table lists only 42 ULGs as the budget documents for the remaining 38 ULGs were not publicly available.

