JANAAGRAHA

A slow reversal of Karnataka's fiscal decentralisation

The state once led India in devolving money and power to local governments. Its recent decisions point the other way.

The 5th State Finance Commission (SFC) – the Constitutional Body set up every five years to recommend on how state resources should be devolved to rural and urban local governments – submitted its report in November of 2025 for the award period of FY 2026-27-2029-30.

The first financial year, 2026-27, following its submission has begun. This study focuses on the SFC's key recommendations and the state's response to it.

JULY 2026

Citizens need local self-governments to deliver basic services. But where is the money?

Karnataka's cities are reeling under the stress of rapid urbanisation. An average citizen faces severe challenges:

Photo Credit: Janaagraha File Photo and Jithendra M for India Today

- Karnataka's 327 Urban Local Governments (ULGs) rely heavily on the state for predictable grants to address these challenges.
- State Finance Commission (SFC) grants, itself, constitute over 75% of the revenues of smaller ULGs and around 40-50% in larger ULGs.
- This makes the state government's actions towards SFC recommendations critical.

For detailed explanation of how ULGs are funded, refer Slides 13, 14 and 15.

5th SFC recommends ~INR 34,052 cr (25%) as the urban share. Actual allocation to city governments is a meagre INR 4,972 cr.

The 5th SFC recommended a bold package but falls short of giving urban its due share:

- The Commission recommended 60% of state revenues to Local Governments (LGs). The highest so far.
- Of this, 25% allocated to urban, and 75% to rural. The urban share is significantly lower than the current urbanisation levels of 46%.
- Karnataka falls behind peer states.

On paper, the state government accepted:

- To devolve only 50% of state revenues to Local Governments.
- Of which 30% will be allocated to urban. This amounts to ~INR 34,052 crore.

What's accepted by the state government:	What ultimately reaches city governments:
INR 34,052 crore	**INR 4,972 crore**

This gap is largely explained by:

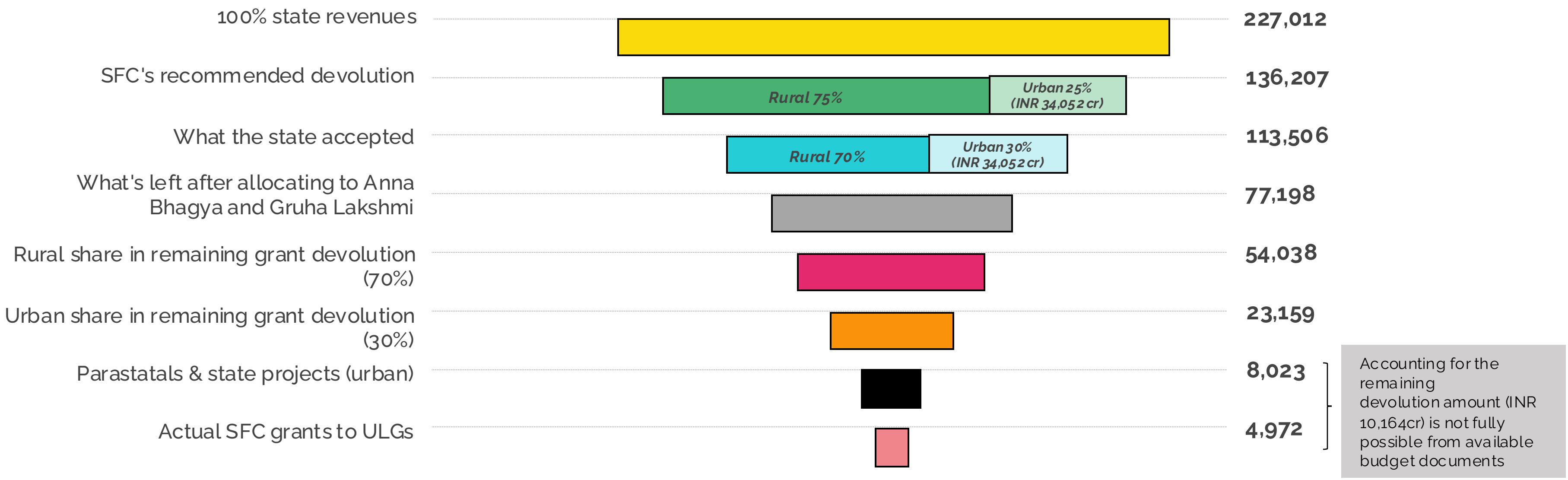
- Allocation of approximately one-third of funds meant for LGs to state welfare guarantee schemes - Anna Bhagya and Gruha Lakshmi
- Similarly, INR 8,023 crore allocated to parastatals from resources meant for ULGs, much against the advice of the CAG and previous SFCs.

For detailed explanation, refer Slides 21-28.

Actual allocation to city governments is a meagre INR 4,972 cr.

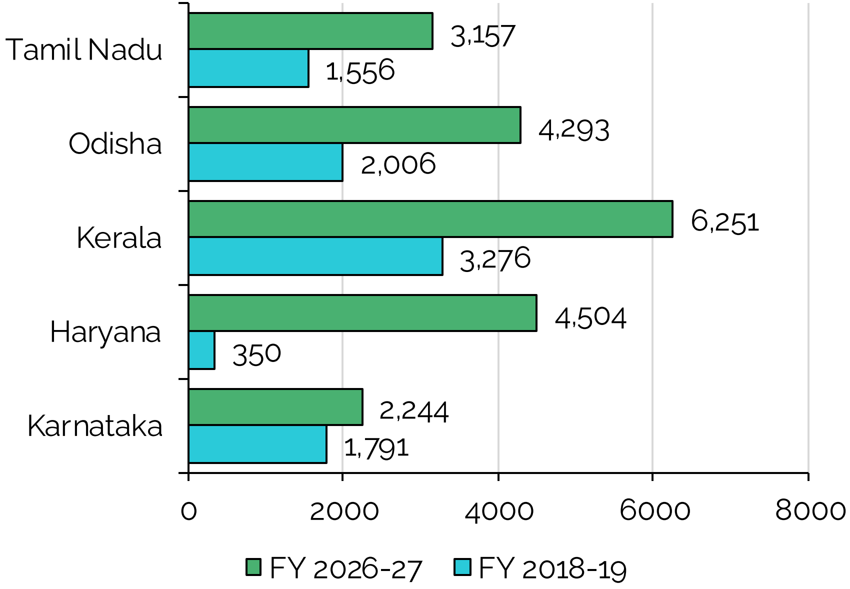
- Allocation to the two welfare guarantee schemes amounts to more than one-third of the accepted devolution (INR 36.308cr) to LGs.
- Allocation to parastatals is 1.6times the allocation to ULGs.

(Per annum figures in INR cr)



Source: Govt. Order FD 18 EXP-6 2025 (ATR) and Janaagraha's analysis from Karnataka State Budget Volumes for FY 2026-27
Note – State Revenues here refer to NLNORR or Non-Loan Net Own Revenue Receipts. It includes own tax and non-tax revenue receipts of the state government minus collection charges and cess deductions..

Karnataka now ranks last among comparable states in per-capita SFC grants to cities: INR 2,244, against Kerala's INR 6,251.

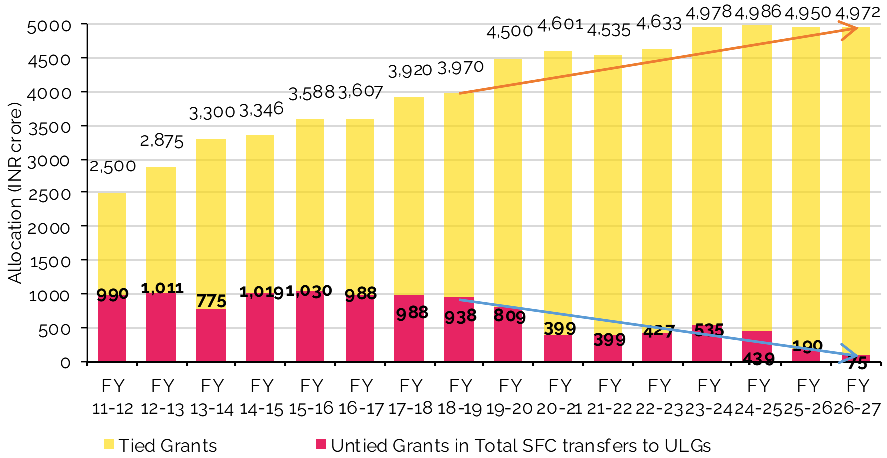


Source: Janaagraha's analysis from State Budget Volumes of respective states

Total allocation of SFC grants to ULGs has almost stagnated for the last 10 years. Even worse, untied grants have collapsed by 87% during the same period.

*Allocation to untied grants in **FY 2026-27 is INR 75 crore** vis-a-vis SFC's recommendation to **allocate ~INR 5,790 crore.***

- Cities and towns once used SFC grants to provide critical services – fix footpaths, install streetlights, or renovate a park.
- They can now barely scratch the surface, owing to steady decline in allocation by the state government,
- The impact is harsher for smaller towns that rely more heavily on grants.



For instance, Mysuru's untied grant has reduced from INR 43 crore in 2014-15, down to INR 3 crore in 2026-27.

For detailed explanation, refer Slide 33, 34, and 44.

The only other lifeline – Union Grants – are also at risk due to lack of ULG elections

- The XVI Union Finance Commission (UFC) has now put **INR 18,483 crore*** on the table for Karnataka's cities for the award period starting FY 2026-27 to FY 2030-31. This translates to INR 3,700 crore per annum, on average.
- But the lack of municipal elections – a pre-condition for a ULG to access all XVI FC grants – threatens even that lifeline.

Karnataka has already paid the price once.

Between FY 2021-22 and FY 2025-26:

~INR 964 crore lost

by BBMP in XV FC grants due to lack of elections.

The same trend might continue in the XVI FC period but at a much larger scale:

Roughly, two-thirds**

of Karnataka's 327 cities and towns are currently running without an election.

*Over five years **Approximate figure

For detailed explanation, refer Slide 36 and 37.

The Way Forward

The urban moment is now. ULGs need to be empowered if quality of life should improve.

01 Timely Constitution of SFCs:

State government should ensure timely constitution of SFCs at least two years before the start of the next award period, giving the SFC adequate and fixed tenure to function effectively,.

02 State schemes should not be included within the devolution package to local governments.

- Anna Bhagya and Gruha Lakshmi are important programmes — but they should be reported separately. Devolution should count what actually reaches city governments.
- The ATR (Action Taken Report) should separately report on allocation to all line items that the state counts as 'devolution to local governments'.

03 Restore Untied Grants while ensuring expenditure accountability:

- Accept the 5th SFC recommendation: at minimum, 25% of SFC grants to ULGs must be untied.
- ULG expenditure on SFC grants including project data, should be available in the public domain.

04 Improve accountability for implementation of SFC recommendations

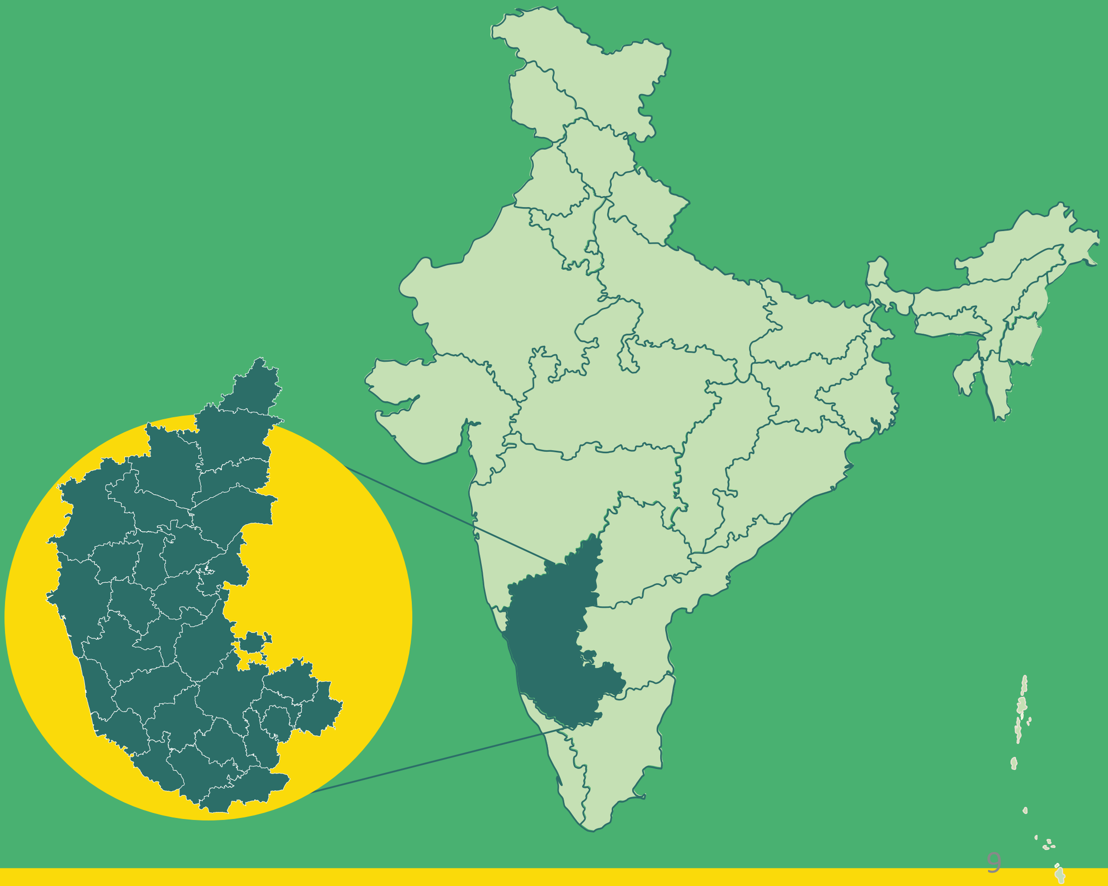
- The ATR should be tabled in the Assembly by the state government, along with justification for recommendations rejected
- Publication of an annual report on progress of implementation of SFC recommendations
- Publish ULG-wise details of grants allocated, released, and expenditures incurred

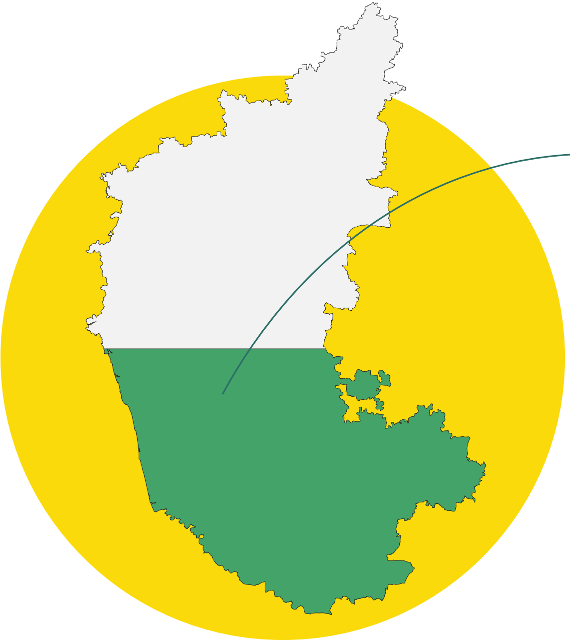
05 Hold Elections Now:

The state is constitutionally required to ensure elected local governments. Every month of delay has a measurable rupee cost. Disclose data on current election status of all ULGs.

Detailed Report

A slow reversal of Karnataka's fiscal decentralisation





46%

almost every second person in Karnataka now lives in a city

Number of cities are multiplying

Karnataka's Urban Local Governments (ULGs) have grown from 220 in 2011 to 327 today – a 49% jump.

*Source: FY 2026-27 Budget Book

As cities expand, service delivery gaps continue to increase

77%

of cities lack sewerage-network coverage — and only 7% have both a sewerage network and a treatment plant.

51%

of cities fall short of the 135-litres-per-capita-per-day water benchmark — with just ~5 hours of supply a day on average.

49%

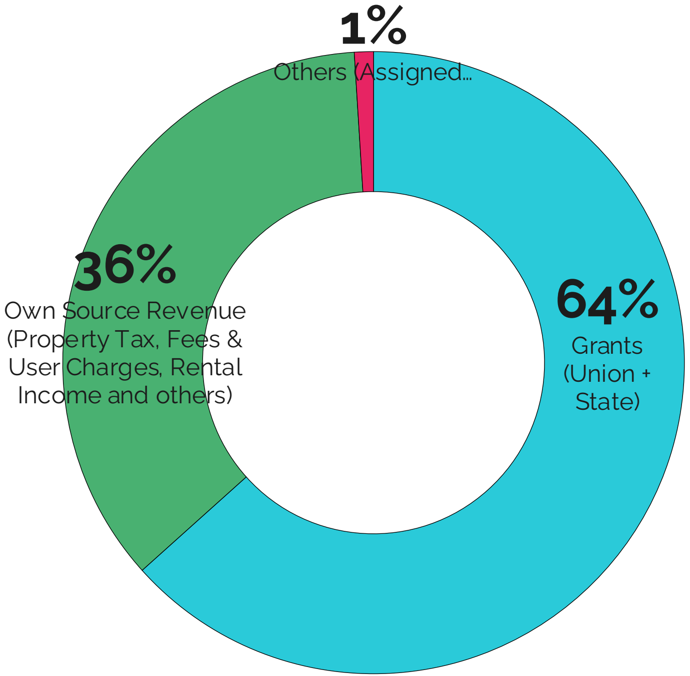
of cities have not achieved scientific disposal of solid waste.

Source: Janaagraha's analysis from 5th Karnataka SFC Report

Almost two-thirds of a city's service delivery costs is met from grants

- Although own revenue of ULGs is growing well at 10% CAGR (FY 18-19 to FY 23-24), dependence on grants has not reduced.

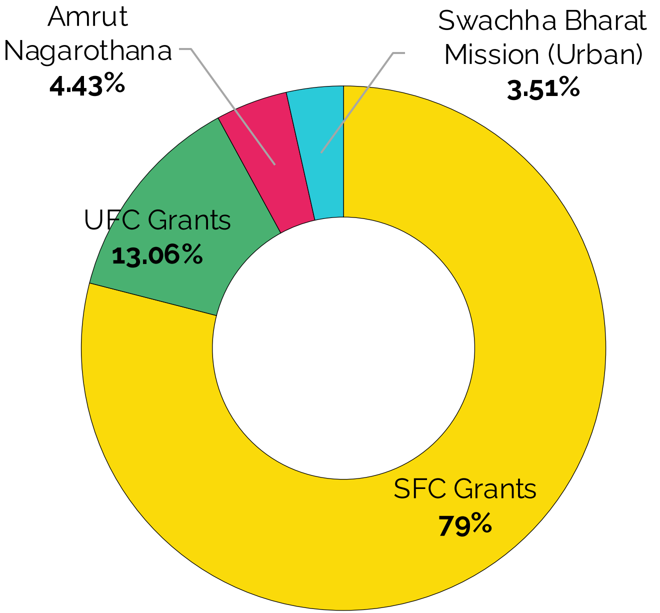
  If anything, grants remain critical to funding basic services such as solid waste management, roads, drains, streetlights, among others.



Source: Janaagraha's analysis of the 5th Karnataka SFC Report and Karnataka State Budget Volumes
Note – CAGR stands for Compound Annual Growth Rate
Note – SFC stands for State Finance Commission, while UFC stands for Union (or Central) Finance Commission

Of all grants to ULGs, 92% are State Finance Commission (SFC) and Union Finance Commission (UFC) grants

- In theory, their reliable and predictable nature is what makes them central to service delivery in ULGs.



Source: Janaagraha's analysis from Karnataka State Budget Volumes for FY 2021-22 to FY 2023-24
Note – (i) The chart above only includes allocations for major grants and schemes for which ULGs are solely responsible for planning and implementation.
(ii) The analysis excludes XVI Finance Commission grants, as they are yet to be released. The proportion of UFC grants is likely to increase once these funds are received.

SFC grants are the backbone of a ULG's daily essential services, while UFC grants contribute to asset creation

State Finance Commission (SFC) grants

Typically, SFC grants serve two core purposes:

~90%

goes to committed expenditures. I.e., municipal staff salaries and electricity bill payments for streetlights and water supply.

~10%

are for untied grants. Though meagre, they give ULGs the autonomy to spend on local needs

Note: The proportions mentioned are averages calculated for FY 2018-19 to FY 2026-27.

Union Finance Commission (UFC) grants

- UFC Grants, similar to SFC untied grants, are typically used for:
  - Creation and maintenance of capital assets
  - Service delivery by ULGs.
- This can include:
  - Purchase of garbage collection vehicles
  - Construction of a solid waste processing plant
  - Renovation of parks

SFC grants not only constitute the larger share, they are a lifeline for ULGs. Therefore, decisions around how these grants are allocated matter enormously.

If SFC grants matter this much, how reliably does Karnataka set up its SFCs?

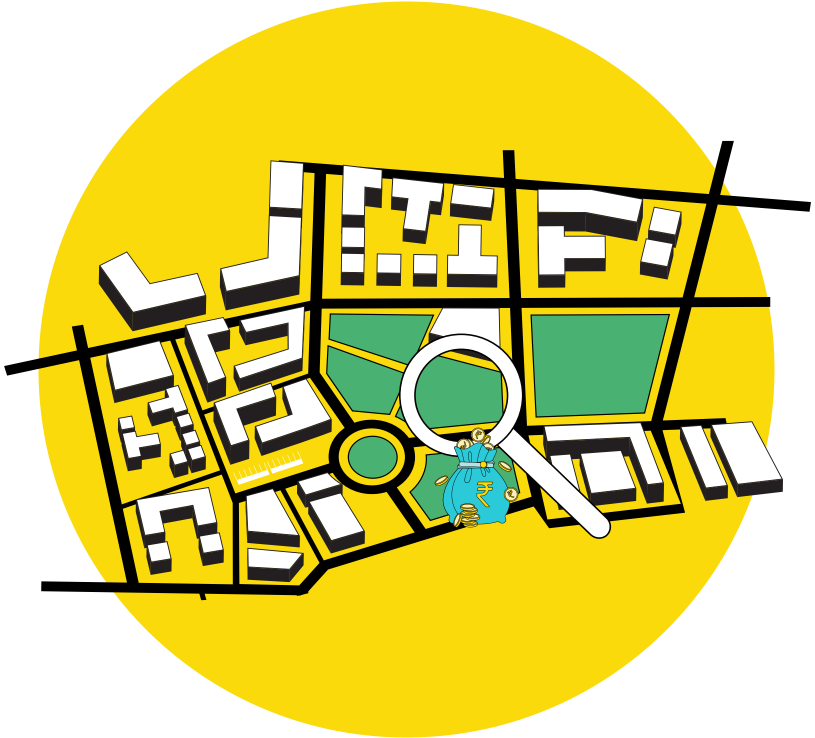
Karnataka is on its 5th State Finance Commission while peer states are on their 7th — its ULGs have been left at least ten years behind.

- The Constitution mandates that SFCs be set up every five years. I.e., their recommendations hold for five years.
- But every Karnataka SFC has arrived late, and the delay persists.
- Further, the state government has barely ever tabled its Action Taken Report in the Legislative Assembly, skipping accountability for its decisions on financial devolution to local governments

SFC	Date of constitution	Award period	Delay in start of award period* (years)
First	10 June 1994	1997-98 to 2001-02	-
Second	25 October 2000	2006-07 to 2010-11	**4** *(From 2002-03 to 2005-06, no SFC recommendations were in place)*
Third	28 August 2006	2011-12 to 2017-18* (**Extended for 2 years*)	0
Fourth	21 December 2015	2018-19 to 2023-24* (**Extended for 1 year*)	**2**
Fifth	11 October 2023	Interim Report for 2024-25 to 2025-26* (**Extended for 1 year*) Final Report for 2026-27 to 2029-30	**1**

Source: Janaagraha's analysis of the Respective Karnataka SFC Reports.

When new SFCs are not constituted on time, cities keep running on recommendations meant for what they were years ago - not what they have become.



With the 5th SFC, the state gave the SFC four six-month extensions instead of a stable two-year tenure

The uncertainty in tenure affects their mandate

Oct 2023 — 5th SFC Constituted

Feb 2024 — Interim SFC Report* for 2024-25 submitted to the Governor

Nov 2025 — SFC Final Report for 2026-27 to 2029-30 submitted to the Governor

Mar 2026 — SFC Report Tabled in the Assembly during the Budget Sessions

Mar 2026 — ATR Released in the public domain (not formally tabled)

Apr 2026 — SFC's award period commenced

Jun 2026 — The Constitutional timeline (6 months) to table the ATR in the Assembly has just passed.

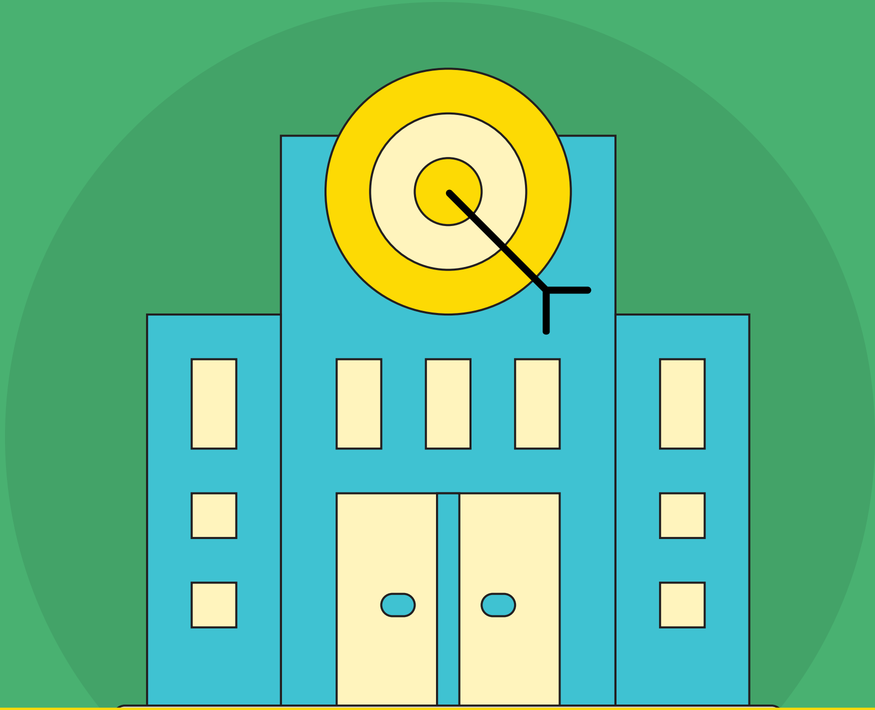
The SFC had to submit their first interim report in four months

Between this time period, they received 4 extensions of six months each.

Source: Govt. Order FD 18 EXP-6 2025 dated 31.03.2026; Constitution of India, Articles 243-I & 243-Y
**Note - The implementation period for the 5th SFC Interim Report recommendations was extended by one year, from FY 2024–25 to FY 2025–26.*

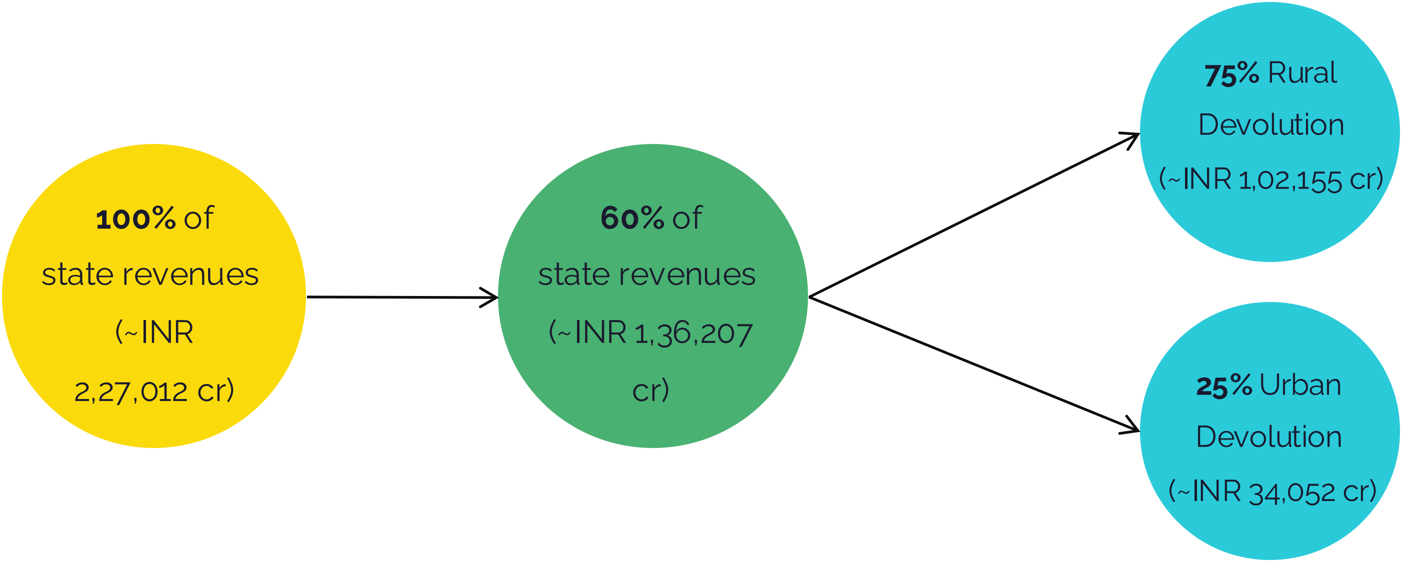
What did the 5th SFC actually recommend for cities?

The Commission has pushed forward on multiple frontiers



The 5th SFC recommended record devolution

*60% of state's revenue receipts, about INR 1,36,207 crore, allocated per year to rural and urban local governments. The highest so far**



Source: Janaagraha's analysis of the 5th Karnataka SFC Report
Note – State Revenues here refer to NLNORR or Non-Loan Net Own Revenue Receipts. It includes own tax and non-tax revenue receipts of the state government minus collection charges and cess deductions.
**Annexure 1 outlines how SFC recommendations have evolved in Karnataka.*

Five recommendations aimed at expanding cities' financial capacity and making their spending fairer

01 A share of city-generated taxes

At least 5% of local state GST and net professional-tax proceeds routed back to ULGs.

02 Flexibility restored

At least 50% of grants to be untied, reversing years of declining discretionary funds.

03 Maintenance, finally funded

New 'asset maintenance' grants, recognising chronic underinvestment in existing infrastructure.

04 Rewards for performance

Performance grants focused on improving decentralised governance.

05 Fairness within the city

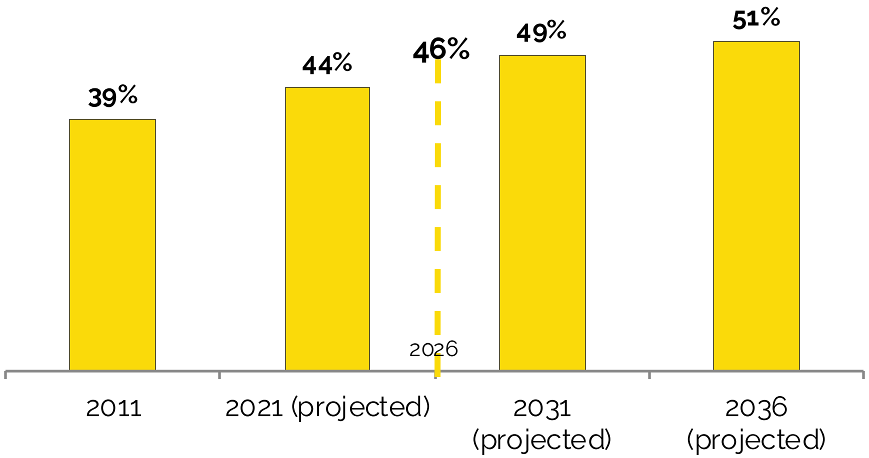
A push for inter-ward allocation to be based on population, area and slum population - a meaningful shift for poorer, denser wards.

Source: Janaagraha's analysis of the 5th Karnataka SFC Report

But this is undercut by two recommendations

(1) Karnataka is 46% urban, yet its cities and towns will receive only 25% of total SFC grants.

Projected Proportion of Urban Population in Karnataka



The 5th SFC kept the urban share at 25% - unchanged from the 4th SFC eight years ago - even as cities' population and their sheer number has surged.

This contrasts with its own submission to the XVI Finance Commission, where they proposed a 40%* urban share of Union grants.

Source: Janaagraha's analysis from the Report of the Technical Group on Population Projections, Ministry of Health and Family Welfare, 2019
**Source – [Proceedings of Finance Commissions' Conclave, Ministry of Panchayati Raj]*

(1) Unlike Karnataka, peer states allocate at least 40% share to urban, in tandem with their urbanisation trends.

Even the XVI Finance Commission now recommends a 45% urban share.

- Urban share in local government grants as determined by various State Finance Commissions

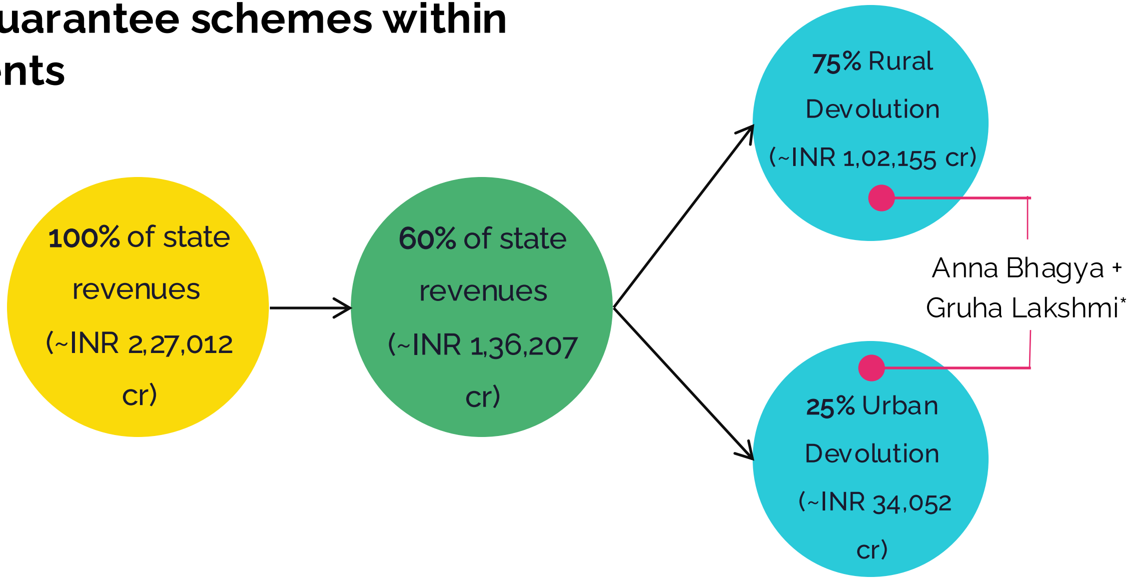
SFC	Karnataka	Haryana	Tamil Nadu	Rajasthan
I	15%	35%	40%	-
II	20%	38%	42%	-
III	30%	35%	42%	24%
IV	25%	35%	48%	25%
V	25%	45%	44%	30%
VI	NA	50%	51%	25%
Projected Urban Population, 2021	44%	41%	53%	26%

Source: Janaagraha's analysis of the respective reports of the different SFCs mentioned.

(2) For the first time, a Karnataka SFC has recommended to include two large state-run guarantee schemes within devolution to local governments

- Counting the two schemes - Anna Bhagya and Gruha Lakshmi – as devolution makes cities look better funded than they are.

- These are cash and food transfers paid straight to households, bypassing elected councils entirely. They should be kept separate from devolution to LGs.



Just as a state would not accept centrally-sponsored schemes being counted as "devolution" from the Union, state-run welfare schemes shouldn't count as devolution to cities.

Source: Janaagraha's analysis of the 5th Karnataka SFC Report
**Note – 5th SFC did not recommend specific amounts for Anna Bhagya or Gruhalakshmi, leaving allocations to the state government's discretion by default*
Note – State Revenues here refer to NLNORR or Non-Loan Net Own Revenue Receipts. It includes own tax and non-tax revenue receipts of the state government minus collection charges and cess deductions.

How did the State Government respond?

The State Government accepted less than the SFC recommended – and delivers even less than it accepted

The state government rejected critical elements of SFC recommendations

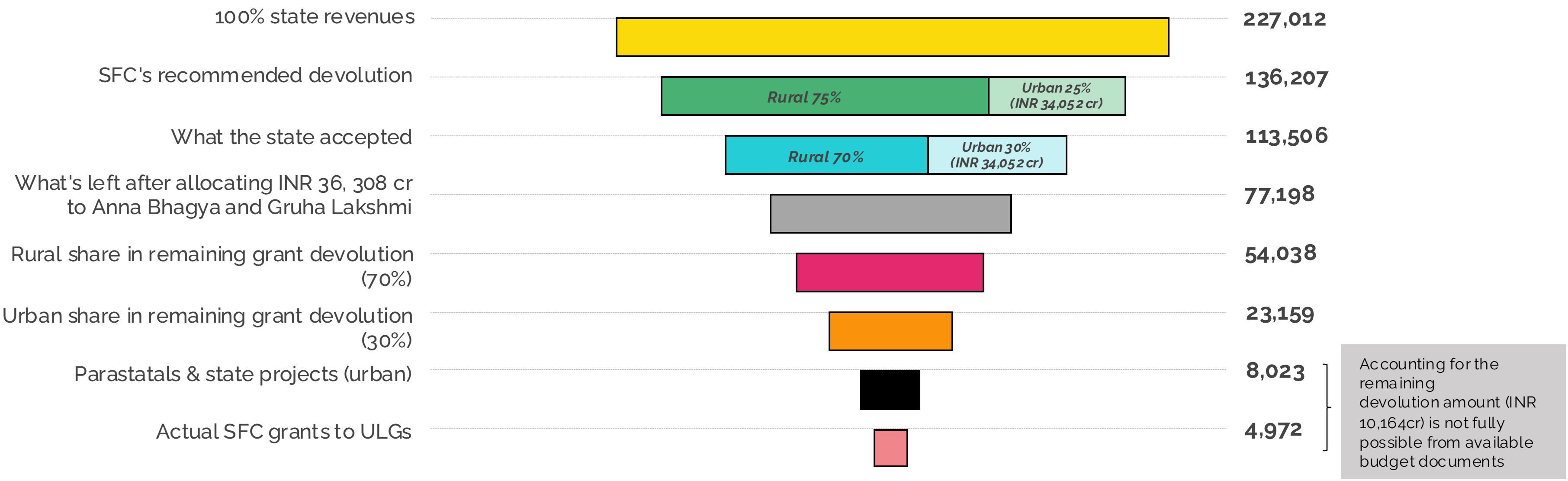
#	Theme	5th SFC Recommendation	State's Response	Analysis of responses in Action Taken Report
1	**Devolution of state revenues to LGs**	• 60% of state revenues to Local Governments (LGs) • Of this, 75% allocated to rural, and 25% (~INR 34,052 cr) to urban. The proportional share to urban remains unchanged from 4th SFC.	Accepted a lower proportion for LGs: • 50% of state revenues to LGs • Of this, 70% is allocated to rural and 30% (INR 34,052 cr) to urban. • The urban share will increase in a phased manner - 24% to 30% over four years	Since the welfare responsibilities of the state have increased more than that of local bodies and the state is facing grave fiscal challenges, state cannot devolve the higher share of 60%.
2	**A share of city-generated taxes**	At least 5% of city-generated state GST and net professional-tax proceeds routed back to ULGs.	**Rejected**	State government stated that these are already a part of the NLNORR considered for devolution of funds to local governments.
3	**Greater flexibility through untied grants**	50% of grants to ULGs should be untied. Minimum 25% should go to ULGs exclusively	**Rejected**	No alternative proportions provided.
4	**Additional specific-purpose grants**	Additional grants for asset maintenance and good performance	**Rejected**	No new grants proposed by the SFC were accepted.
5	**Ward-wise allocations**	Enabling fairness within the city through ward allocations in all the city corporations	Accepted.	Practically, this may not translate to any significant shift due to the small pool of untied grants for ULGs.
6	**Reform recommendations**	Recommendations for improving tax and non-tax revenues of ULGs, strengthening participatory governance	Left Vague	All reform-related recommendations referred to departments with no timelines or owners.

What reaches ULGs is a fraction of what the state government accepted

The gap is largely explained by:

- Allocation to two welfare guarantee schemes which amount to more than a third of the accepted devolution (INR 36.308cr) to LGs.
- Allocation to parastatals which is roughly 1.6 times the allocation to ULGs.

*(Per annum figures in INR cr)**



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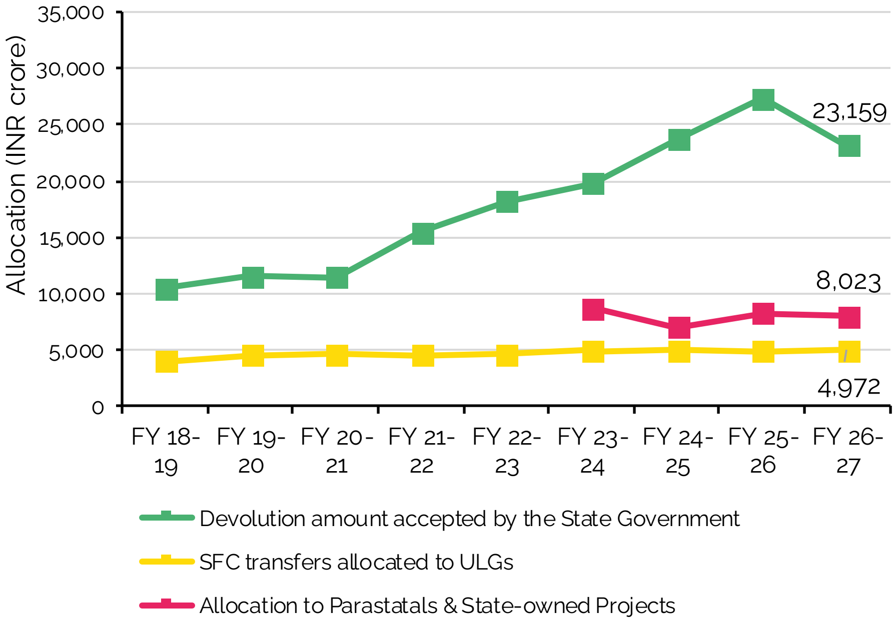
Note – State Revenues here refer to NLNORR or Non-Loan Net Own Revenue Receipts. It includes own tax and non-tax revenue receipts of the state government minus collection charges and cess deductions..
**Calculations here are estimates based on allocations provided in the FY 2026-27 budget book. The ATR does not provide this.*

What does this mean for city governments?

City Governments are squeezed in their efforts to provide basic urban services

The gap keeps widening: what the state claims to devolve climbs, while what reaches cities stays flat.

- Actual SFC grants to cities have flatlined near INR 4,972 cr, even as accepted devolution increases.
- Despite the advice of the CAG and previous SFCs, the state government continues to make allocations to state-run parastatal agencies out of SFC-recommended finances meant for ULGs



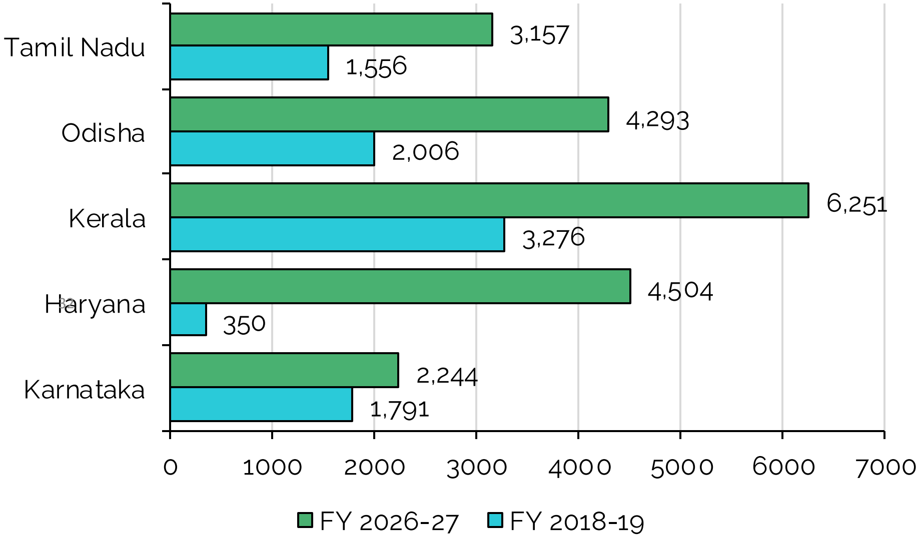
Source: (i) Respective Karnataka SFC Reports, (ii) Karnataka State Budget Volume of 'Budget Allocation for Urban Local Bodies' and 'Detailed Budget Estimates of Expenditure for Urban Development Department' of respective years,
Note – Allocations to parastatals only includes parastatals and state-owned projects budgeted in the Urban Development Department's budget.

Karnataka now ranks last among comparable states in per-capita SFC grants to cities: INR 2,244, against Kerala's INR 6,251.

Peer states more than doubled these grants over eight years.

- **+203%** Tamil Nadu
- **+214%** Odisha

Karnataka's per capita allocation just increased by 25%, with no growth in the last three years.

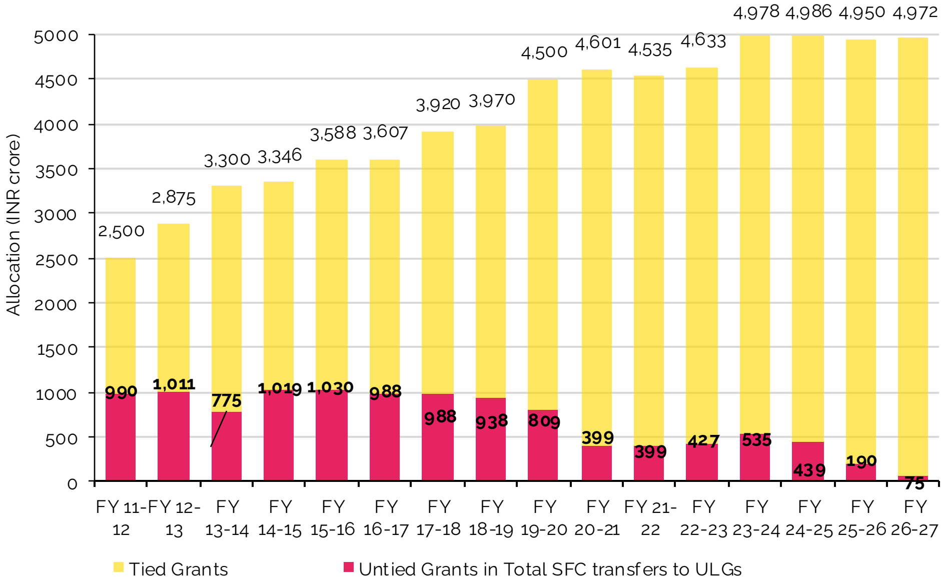


Source: Janaagraha's analysis from State Budget Volumes of respective states
Note – Per capita calculations are based on statutory town population from Census 2011.

Cities' only flexible money has collapsed.

The lowest in over a decade – down 87% from the 4th SFC period, now just 2% of all SFC grants to ULGs.

- INR 75 crore allocation to untied grants, against the INR 5,790* crore the 5th SFC recommended.
- By contrast, the XVI Finance Commission recommends that 52% of grants be untied.



To know more on trends in tied and untied grants in ULGs (i.e., salary and electricity grants), CLICK HERE – Annexure 3

Source: Karnataka SFC Reports; Karnataka State Budget Volumes; Janaagraha's calculations
**Note – Calculated as 25% of total SFC grants to urban recommended by the SFC*

Untied grants to major cities have fallen by more than 90% in 12 years.

For instance, Davanagere has gone from INR 22 crore to INR 2 crore.

City	Allocation for SFC Untied Grants (INR cr)					Decrease in Untied Grants (FY 2014-15 to FY 2026-27)
	2014-15	2017-18	2020-21	2023-24	2026-27	
Mysuru	**43**	48	19	25	**3**	-93%
Hubballi-Dharwad	**47**	36	15	19	**3**	-94%
Davanagere	**22**	24	10	12	**2**	-91%
Mangaluru	**22**	17	7	8	**1**	-95%
Kalaburagi	**27**	21	8	11	**2**	-93%

Source: Karnataka State Budget Volumes and Janaagraha's calculations

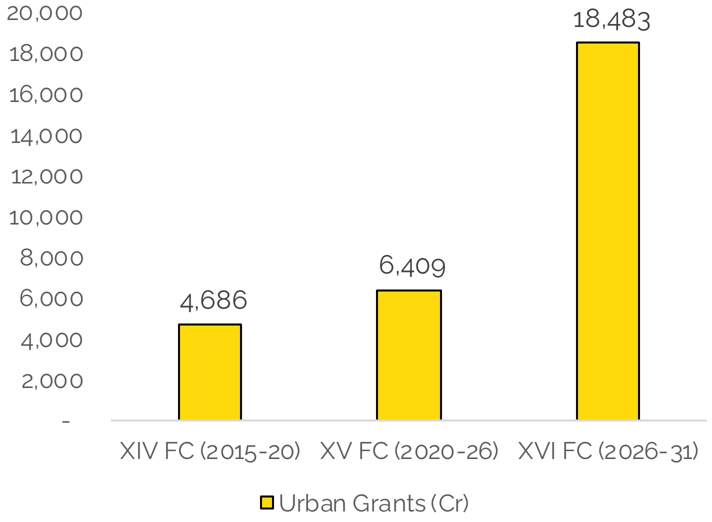
With SFC grants hollowed out, Karnataka's cities are critically dependent on XVI Finance Commission grants.

The XVI Finance Commission has just put INR 18,483 crore on the table for Karnataka's cities for the next 5 years.

But the lack of municipal elections threatens even that lifeline for some ULGs.

XV FC to XVI FC: 188% increase

More money than Karnataka's cities have ever had access to. But the access to money is at risk.



Three conditions to access XVI FC grants

Grant Condition	Karnataka's Performance
ULGs' Audited accounts publicly disclosed	**GOOD** Most Karnataka ULGs are disclosing Annual Financial Statements. This condition is being met.
SFC report + ATR tabled within 6 months	**UNCLEAR** SFC report submitted. ATR placed in public domain (Mar 2026). But it is not fully clear if ATR was tabled in the Assembly.
Duly elected local governments	**AT RISK** Elections are pending in many cities.

Source: XVI Finance Commission Report

No elected government, no grants. Karnataka has already paid this price once.

During XV FC (FY 2021-22 to FY 2025-26)

~INR 964 crore lost

by BBMP because elected local government was not in place.

In upcoming XVI FC (FY 2026-27 to FY 2030-31)

~INR 140 crore

in grants for 2026-27 hangs in limbo for just two cities — Mysuru and Mangaluru —as Karnataka delays civic elections.

Across Karnataka, 13 of 18 City Corporations, including all 5 under the new Greater Bengaluru Authority, are running without an elected council.

The constitutional obligation to hold elections is the state's responsibility. The cost of delay falls on cities.

For smaller cities (under 1 lakh population), UFC grants are the single largest source of untied infrastructure funding. Losing them is not a gap that SFC grants can fill.

Source: Janaagraha analysis

What next?

This report makes 5 core recommendations to the state government.

The Way Forward

The urban moment is now. ULGs need to be empowered if quality of life should improve

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State government should ensure timely constitution of SFCs at least two years before the start of the next award period, giving the SFC adequate and fixed tenure to function effectively,.

02 State schemes should not be included within the devolution package to local governments.

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- Publication of an annual report on progress of implementation of SFC recommendations
- Publish ULG-wise details of grants allocated, released, and expenditures incurred

05 Hold Elections Now:

The state is constitutionally required to ensure elected local governments. Every month of delay has a measurable rupee cost. Disclose data on current election status of all ULGs.

Annexures

40

The 5th SFC builds on two decades of recommendations

SFC	Award Period	Share of State's Own Revenue Recommended for Devolution to Local Governments	Share of Total Recommended Devolution going to:	
			PRIs	ULGs
First	1997-98 to 2001-02	36% of NLGORR to be devolved	30.6%	5.4%
Second	2006-07 to 2010-11	40% of NLGORR to be devolved	32%	8%
Third	2011-12 to 2017-18* (*Extended for 2 years)	33% of NLNORR to be devolved	23%	10%
Fourth	2018-19 to 2023-24* (*Extended for 1 year)	48% of NLNORR to be devolved	35%	12% + 1% separately to be devolved to BBMP
Fifth (Interim)	2024-25 to 2025-26	49% of NLNORR to be devolved	35%	13% + 1% separately to be devolved to BBMP
Fifth	**2026-27 to 2029-30**	**60% of NLNORR to be devolved, including, Gruhalakshmi and Anna Bhagya guarantee schemes**	**45%**	**15%**

Source: Respective Karnataka SFC Reports
**Note - Award period extended by one or two years due to delays in constitution of succeeding Commission.*
**Non-Loan Gross Own Revenue Receipts (NLGORR) includes – (i) All taxes levied, collected and appropriated by the state government, (ii) Interest receipts and, (iii) All duties, fees and other non-loan non-tax receipts levied and collected by the state government under the budget heads; General Services. Social Services and Economic Services.*
Non-Loan Net Own Revenue Receipts (NLNORR) stand for NLGORR – Total collection charges and cess deductions.

State's Response to 5th SFC's Recommendations, as per GO No. FD 18 EXP6-2025, dated 31 March 2026

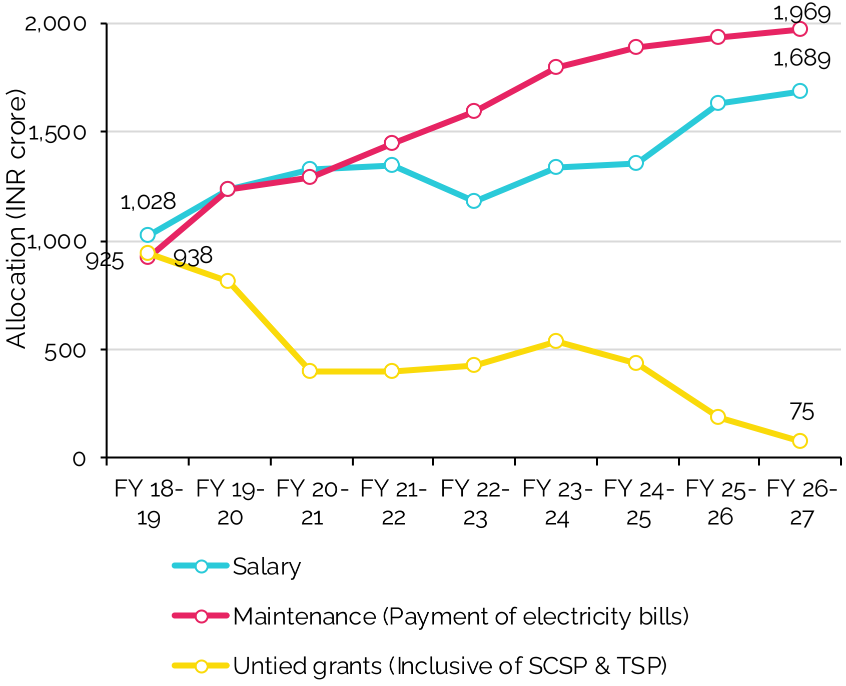
5th SFC's Recommendations	State's Response
State must devolve 60% of state's own revenue receipts (NLNORR) to local governments, inclusive of salaries, Gruhalakshmi and Anna Bhagya guarantee schemes	**Accepted Less:** State will devolve 50% of NLNORR to local governments, inclusive of salaries, Gruhalaksmi and Anna Bhagya guarantee schemes. This is because - • The state has been facing grave fiscal challenges including lesser allocations by the XV Finance Commission • The responsibilities of the state for welfare and development have significantly increased in recent years, compared to local governments. So, every increase in devolution to local governments will restrict the State in taking up these responsibilities.
Union Finance Commission grants must be kept outside the calculation of quantum of SFC grants to ULGs.	**Rejected:** Union Finance Commission grants will be considered part of state devolution as done earlier *Implication: by clubbing union transfers into the devolution figure, the state can appear to meet its SFC commitment while actually contributing less from its own resources.*
State government must allocate at least 5% of city-generated state GST and net proceeds of professional tax to ULGs.	**Rejected:** GST and Professional Tax are already included in the NLNORR.

State's Response to 5th SFC's Recommendations, as per GO No. FD 18 EXP6-2025, dated 31 March 2026

5th SFC's Recommendations	State's Response
SFC Grants to ULGs must include - • 50% untied grants • New grants for asset maintenance, capacity building of ULG functionaries, establishment costs for newly formed ULGs, and • Performance-based grants	**Rejected:** Due to the fiscal challenges being faced by the state, it would not be feasible to accept the Commission's recommendations *Implication: ULGs, especially the smaller ones, struggle to maintain existing infrastructure and lack basic operational funding. At a time when ULGs need more targeted support, the state's response offers no alternative mechanism to fill these gaps.*
In all the City Corporations (CC) of the state, 80% of the total funds devolved must be distributed to each ward, while the remaining 20% may be kept aside for inter-ward works	**Accepted:** Devolutions to wards may be allocated as per the indicators and weightages recommended. *Implication: this marks a shift from the typical practice of 'ad-hoc allocation' of resources across wards to a more need-responsive approach. But, with a fall in overall untied grants, this acceptance has limited practical impact.*
Various reform-related recommendations for improving tax and non-tax revenues of ULGs, strengthening participatory governance, ensuring ULG-consultation in all parastatal projects and extending the tenure of Mayors and Deputy Mayors	**Left vague:** Concerned departments must take action on 5th SFC's recommendations regarding fiscal, administrative, institutional, and governance reforms. *Implication: The Action Taken Report does not specify which department is responsible for implementation, by when it is expected to act, or how compliance will be monitored. Without these, there is little assurance that these recommendations will be meaningfully acted upon.*

Trends in SFC grants to ULGs

- Even as untied grants have dropped to almost nothing, we observe a related trend –
- **The rapid increase in allocation to electricity bills appears to have further crowded out any potential increases to untied grants**: Electricity bill payments, for water supply and streetlights in ULGs, have more than doubled from INR 925 cr (FY18-19) to INR 1,969 cr (FY26-27), now consuming 40% of all SFC grants to ULGs.
- A preliminary analysis and secondary sources indicate that this may not necessarily be linked to improved service delivery.
- The SFC report offers some recommendations to address this issue among rural areas but there is limited deliberation on the urban front.



Source: Karnataka State Budget Volume of 'Budget Allocation for Urban Local Bodies'
Note – The chart above only shows the key SFC grant components and excludes debt servicing and other components.

Role of the UFC and SFC.

Union Finance Commission (UFC)

- UFC's mandate is guided by Article 280.

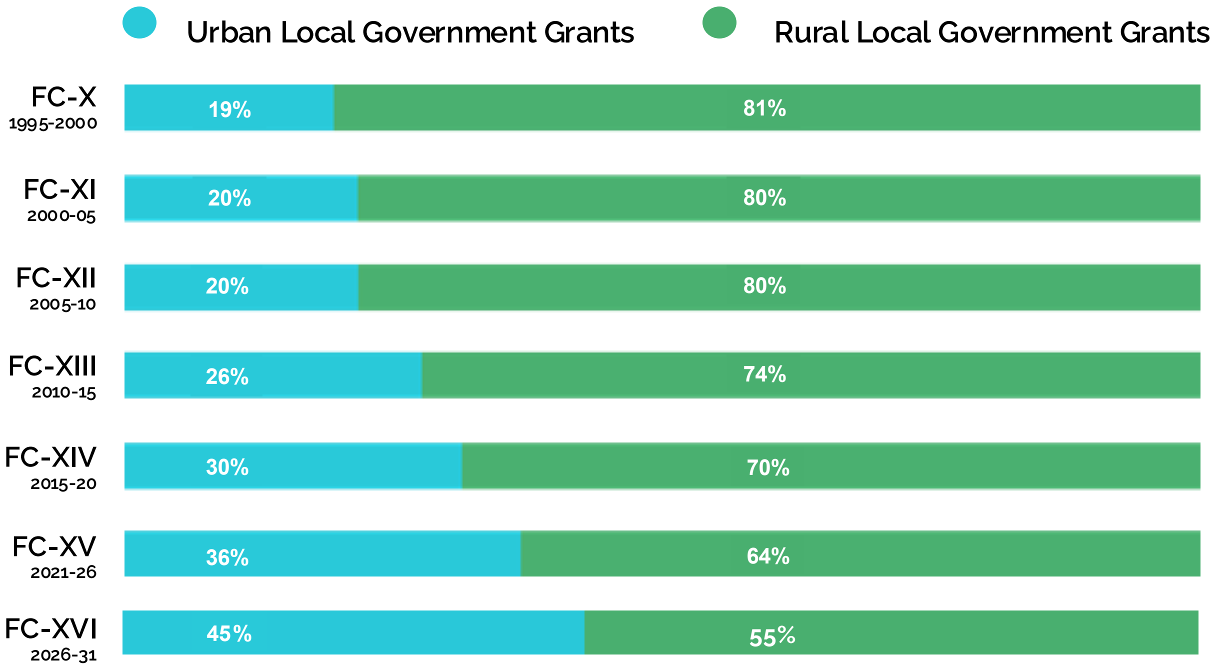
  Set up every five years, it recommends on devolution of union resources to all states
- For local governments specifically, the UFC recommends grants to Urban Local Governments (ULGs) and Panchayati Raj Institutions (PRIs).
- UFCs are constituted with predictable, five-yearly regularity. Government tables the Action Taken Report in the Parliament. There is relatively greater public scrutiny.

State Finance Commission (SFC)

- SFC's mandate is guided by Article 243Y and 243I.
- Set up every 5 years by each state government, SFCs recommend on devolution of state's revenues to LGs.
- In practice, SFCs across the country are often constituted late, leaving local governments in prolonged uncertainty. Further, there is very little accountability from the state government on how its recommendations are taken up,

Source: Constitution of India, XV & XVI Finance Commission Reports,

XVI FC raised ULG share to 45% of Local Government grants — up from 36% in XV FC



The increase in share to ULGs acknowledges the "projected urbanisation level of 40.73% by 2031, coupled with the elevated cost of service delivery in urban areas."

The 45% share includes two special grants: Urbanisation Premium and the Special Infrastructure Component

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