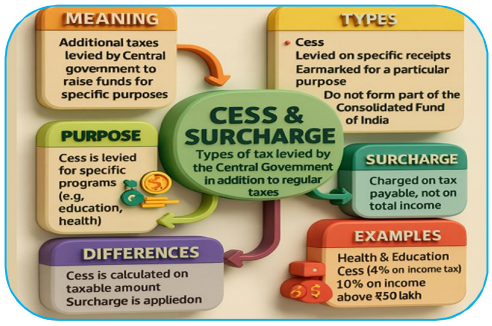
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CESS AND SURCHARGE IN INDIA: IMPACT ON FISCAL AUTONOMY OF STATES

Gurmeet Singh
Assistant Professor, Department of Political Science,
Punjabi University College, Ghudda, Bathinda, Punjab.

ABSTRACT :



The central government's increasing reliance on 'Cesses' and 'surcharges' has become a matter of serious concern regarding fiscal federalism and the fiscal autonomy of states in India. Although cesses and surcharges are constitutionally recognized instruments of taxation, their growing share in the central government's total tax revenue affects the equitable distribution of financial resources between the Centre and the states. Unlike the 'divisible pool' of central taxes, revenue generated from cesses and surcharges is generally excluded from the process of 'tax devolution' the mechanism through which funds are transferred to states based on the recommendations of the Finance Commission. Consequently, the excessive use of these instruments can reduce the share of resources available to states, potentially adversely affecting their fiscal capacity, expenditure priorities, and financial autonomy. This research paper examines the constitutional, fiscal, and institutional aspects of cesses and surcharges in India, with a particular focus on their impact on the principles of 'cooperative federalism' and fiscal autonomy. It analyzes how an increasing dependence on these instruments exacerbates the 'vertical fiscal imbalance' between the Centre and the states, creating challenges for the latter in financing essential public services and development programs. The study also explores the role of the Finance Commission, the need for greater transparency and accountability in the utilization of revenue derived from cesses and surcharges, and the possibilities for strengthening the existing fiscal transfer mechanism. Finally, this research paper suggests several reforms aimed at ensuring a more equitable distribution of financial resources, granting greater fiscal autonomy to the states, and establishing a robust framework for cooperative and competitive federalism in India.

KEYWORDS: *Cess, surcharge, fiscal federalism, autonomy, Centre-State financial relations, tax devolution, divisible pool, Finance Commission, vertical fiscal imbalance.*

INTRODUCTION

Fiscal federalism is an essential feature of the Indian constitutional system, governing the distribution of financial powers, taxation responsibilities, and revenue resources between the central and state governments. The effective functioning of a federal structure depends on a fair and balanced distribution of financial resources across different levels of government. The Constitution of India provides a framework for the allocation of taxation powers and financial responsibilities to ensure economic stability, administrative efficiency, and balanced regional development. However, a persistent 'vertical' fiscal imbalance exists due to an unequal distribution of revenue-raising powers and expenditure responsibilities between the Centre and the states.[1] In this context, the central government

possesses several constitutional mechanisms to mobilize financial resources, including taxes, duties, cesses, and surcharges. Cesses and surcharges have become significant components of India's taxation system and play a crucial role in augmenting government revenue. A cess is typically levied for a specific purpose—such as education, health, infrastructure, or social welfare—whereas a surcharge is an additional levy imposed on existing taxes, aimed at increasing the central government's revenue. Articles 270 and 271 of the Indian Constitution provide the constitutional framework for the distribution of central taxes and the imposition of surcharges. Notably, however, the proceeds from cesses and surcharges are generally excluded from the 'divisible pool' of central taxes that are shared with the states.[2]

The increasing reliance on cesses and surcharges has a profound impact on the fiscal autonomy and financial independence of state governments. State governments are primarily responsible for providing essential public services, including education, healthcare, agriculture, rural development, infrastructure, sanitation, and social welfare. These tasks require substantial and sustained financial resources. However, when a large portion of central tax revenue is collected through channels that cannot be shared with the states, the resources available for distribution among them diminish. This increases the states' reliance on transfers, grants, and centrally sponsored schemes provided by the central government. Such dependence can limit the flexibility of state governments to set their own spending priorities based on their specific regional requirements and developmental needs. The 'Finance Commission,' constituted under Article 280 of the Constitution, plays a crucial role in recommending the distribution of central tax revenue to be shared between the Centre and the states. Nevertheless, the exclusion of cesses and surcharges from the 'divisible pool' has raised concerns regarding the adequacy and fairness of the existing financial transfer mechanism. This has also intensified discussions surrounding the principles of cooperative and competitive federalism specifically concerning the financial rights and responsibilities of the states. While the central government argues that cesses and surcharges are necessary instruments for mobilizing additional resources for national development, state governments have expressed concern over their increasing use and the consequent reduction in their effective share of central tax revenue.[3]

STATEMENT OF PROBLEM

India has a federal financial system in which financial resources and the power to levy taxes are divided between the central government and state governments. Under the Constitution, and based on the recommendations of the Finance Commission, central tax revenue is shared with the states through a 'divisible pool.' However, 'cesses' and 'surcharges'—levied by the central government—are excluded from this divisible pool.[4] Consequently, states do not receive a direct share of these revenues through the process of tax devolution. The growing share of cesses and surcharges within the Centre's total tax revenue raises concerns regarding the availability of financial resources for the states. In 2011–12, cesses and surcharges accounted for approximately 6.4% of total tax revenue; by 2021–22, this figure had risen to 17.7%.[5] During the same period, the share of the divisible pool within total tax revenue declined. This situation has significant implications for 'fiscal federalism,' particularly concerning the distribution of financial resources between the Centre and the states. States rely on central tax devolution and grants-in-aid to fund expenditures on education, health, agriculture, infrastructure, and social welfare programs.

The increasing reliance on cesses and surcharges raises questions about the states' fiscal autonomy, their revenue-raising capacity, their financial independence, and their ability to plan development initiatives in alignment with regional priorities. Although cesses and surcharges are constitutionally valid tax instruments, their growing contribution to central revenue necessitates a thorough examination of their impact. This involves examining their impact on 'horizontal and vertical fiscal imbalances,' 'fiscal equalisation,' and Centre-State financial relations. Accordingly, the objective of this study is to examine trends in the collection of cesses and surcharges in India, analyse their impact on the divisible pool of central taxes, evaluate the system of intergovernmental fiscal transfers and fiscal equalisation, and assess their effects on the fiscal autonomy and financial position of state governments. The study also seeks to understand whether the existing system of revenue sharing

provides states with sufficient financial resources to foster balanced regional development and effectively implement public welfare programmes.[6]

The increasing use of cesses and surcharges raises questions regarding the fiscal autonomy of states, their capacity to mobilize revenue, their financial independence, and their ability to plan expenditure on development initiatives in alignment with regional priorities.[7] Although cesses and surcharges are constitutionally valid tax instruments, their growing share in central revenue necessitates an examination of their impact on horizontal and vertical fiscal imbalances, fiscal equalization, and the fiscal relations between the Centre and the states.[8] Consequently, this study aims to examine trends in the collection of cesses and surcharges in India, analyze their impact on the 'divisible pool' of central taxes, evaluate the system of fiscal transfers and fiscal equalization between governments, and assess the implications for the fiscal autonomy and financial position of state governments.[9] Furthermore, the study seeks to determine whether the existing framework for revenue distribution provides states with sufficient financial resources to foster balanced regional development and effectively implement public welfare programs.[10]

OBJECTIVES OF STUDY

- To examine the constitutional provisions and legal framework concerning cesses and surcharges in India.
- To analyze the nature of cesses and surcharges and their financial significance within the Central government's revenue collection.
- To study the Central government's increasing reliance on cesses and surcharges, and its impact on the 'divisible pool' of Central taxes.
- To analyze the implications of the growing use of cesses and surcharges for fiscal federalism and the fiscal autonomy of the states.
- To analyze the challenges arising from the states' dependence on Central financial transfers and grants, as influenced by the use of cesses and surcharges.

REVIEW OF LITERATURE

A literature review is an essential component of research, as it provides an understanding of existing knowledge, scholarly perspectives, research findings, and policy discussions relevant to the subject of study. In India, various economists, financial institutions, research organizations, and constitutional bodies have analyzed issues pertaining to fiscal federalism, Centre-State financial relations, tax transfers, and fiscal decentralization. Although 'cesses' and 'surcharges' are constitutionally valid instruments for revenue mobilization, their increasing use has sparked significant debate regarding their impact on the divisible pool of central taxes and the financial autonomy of state governments. The review presented here analyzes key reports and research studies pertinent to the current research topic.

M. Govinda Rao and Nirvikar Singh (2007), in their study, *"The Political Economy of India's Fiscal Federal System and its Reform"* examine the political and economic circumstances of India's fiscal federal system. The study discusses the division of taxation powers, fiscal transfers between the Centre and the states, and the role of the Finance Commission. It argues that a balanced distribution of financial resources between the Centre and the states is essential for making fiscal federalism effective in India.

Harikrishnan K. S. and Hiremath G. S. (2026) in their research article, "Fiscal Asymmetry and Subnational Social Spending: Decoding India's Federal Experience," examine the relationship between fiscal disparities among states and their social sector spending. The authors analyze how variations in revenue-raising capacity and reliance on intergovernmental transfers influence the ability of state governments to fund social sector programs. Their study highlights that states with limited fiscal resources may face greater challenges in fulfilling their expenditure responsibilities. It also explores how intergovernmental transfers shape the spending decisions of state governments. This study offers

significant insights into the connection between fiscal asymmetry and expenditure autonomy at the state level.[11]

Rao, M. Govinda and Singh, Nirvikar (1999) in their research paper, *'The Assignment of Taxes and Expenditures in India'*, analyze the division of taxing powers and expenditure responsibilities between the central and state governments. The authors argue that India's fiscal system exhibits a tendency toward centralization, as the central government possesses a greater capacity to mobilize revenue, while state governments bear significant responsibilities for the provision of public services. They identify this arrangement as a cause of 'vertical fiscal imbalance,' which necessitates financial transfers from the Centre to the states. The authors also discuss the shortcomings of the existing tax system and the need for reforms in tax assignment and the financial arrangements between the different levels of government. Their analysis provides an important theoretical foundation for understanding the fiscal relations between the Centre and the states. This is particularly relevant to the present research, as the exclusion of 'cesses' and 'surcharges' from the 'divisible pool' (distributable revenue) may further impact the allocation of financial resources between these two tiers of government.[12]

The Fifteenth Finance Commission (2021) in its report, *'Finance Commission in the Time of COVID: Report for 2021-26',* the Commission reviews the sharing of central tax revenue and the financial requirements of state governments. The Commission recommended that states should receive 41 percent of the 'divisible pool' of central taxes during this period. It also examined the composition of central tax revenue, specifically discussing the impact of cesses and surcharges on the divisible pool. The Commission observed that the share of cesses and surcharges within gross tax revenue has increased. Based on its projections, the Commission estimated that excluding the GST compensation cess these would account for an average of 18.4 percent of gross tax revenue between 2021-22 and 2025-26. The report clarifies that the percentage of tax devolution alone does not provide a complete picture of the resources reaching the states, as the overall size of the divisible pool is also a critical factor. This analysis is particularly relevant to the present research, as it directly links the growing reliance on cesses and surcharges to the availability of resources for state governments.[13]

Reserve Bank of India (2021), in its publication *'State Finances: A Study of Budgets'* analyzes the evolving fiscal relations between the central and state governments, including the nature of tax devolution and grants-in-aid. The report discusses the growing importance of central transfers in meeting the expenditure requirements of the states. It also highlights the impact of the increasing share of cesses and surcharges on the size of the 'divisible pool' (the pool of funds available for distribution). The analysis indicates that an increase in these levies can reduce the total tax revenue shared with the states even if the prescribed percentage for tax devolution remains unchanged. The report emphasizes the importance of 'predictable' fiscal transfers for sustaining the financial position of the states. This is relevant to the current research, as it provides an empirical basis for examining the relationship between cesses, surcharges, and the resources actually transferred to state governments.[14]

Kotha, Ashrita Prasad; Agarwal, Vinti; Sengupta, Arghya; and Singh, Ravi Pratap (2018) in their report titled *'Cesses and Surcharges: Concept, Practice and Reform', published by the Vidhi Centre for Legal Policy,* analyze the constitutional and legal framework governing cesses and surcharges in India. The authors clarify the distinction between these two forms of revenue: a cess is typically levied for a specific purpose, whereas a surcharge is an additional charge on an existing tax, which is not necessarily linked to any particular expenditure objective. The report highlights that the proceeds from cesses and surcharges do not form part of the 'divisible pool' the pool of revenue subject to sharing and are, therefore, not distributed to the states through the standard tax-sharing mechanism. It also draws attention to the growing significance of these levies within the central government's revenue collection. The report provides a vital legal foundation for examining the constitutional status, collection, and utilization of cesses and surcharges. It is directly relevant to the current research, as it addresses the core issue of how these levies impact the 'divisible pool' and the fiscal position of state governments.[15]

Varghese, Aswathy Rachel, Sumalatha, B. S., and Kumari, Anita L. (2026), in their research article titled "Intergovernmental Transfers and Fiscal Federalism in India*: A Critical Assessment of the Divisible Pool and Grants-in-Aid Framework*" analyze the system of fiscal transfers between the central

and state governments in India. The authors focus on the "divisible pool" of central taxes and the role of "grants-in-aid" in maintaining fiscal balance within the federal structure. Their study highlights the significance of the "divisible pool" in determining the share of financial resources transferred to state governments. They also express concern regarding the exclusion of "cesses" and "surcharges" from the "divisible pool," as this revenue is not shared with the states through the standard tax-transfer mechanism. The authors emphasize the need for a fair and transparent system of intergovernmental fiscal transfers to bridge the gap between the states' revenue-raising capacity and their expenditure obligations. This study is particularly relevant to the current research, as it provides a basis for examining how the increasing reliance on "cesses" and "surcharges" may affect the resources available to the states and, consequently, their fiscal autonomy.[16]

Organisation for Economic Co-operation and Development (2020) in its study *'Fiscal Federalism in India'* analyzes the framework of fiscal federalism in India and the distribution of financial responsibilities across various levels of government. The study examines the role of tax devolution and intergovernmental grants in addressing fiscal imbalances between the central and state governments. It emphasizes the importance of providing sub-national governments with adequate financial resources to enable them to effectively fulfill their expenditure responsibilities. The study also highlights the challenges associated with fiscal decentralization specifically, the difficulty of striking a balance between financial resources, expenditure responsibilities, and accountability. Its analysis is useful for understanding the institutional arrangements that govern fiscal transfers in India. In the context of current research, this study provides a comprehensive framework for examining how the centralization of revenue resources including the collection of cesses and surcharges—can impact the financial capacity and autonomy of state governments.[17]

World Bank (2025) in its research study *"Intergovernmental Transfers and Fiscal Equalization"* the World Bank examines the system of financial transfers between the Union and State governments in India. The study focuses on the role of tax devolution and grants-in-aid in addressing differences in the revenue-raising capacity and expenditure requirements of States. It draws attention to the significance of the divisible pool in determining the financial resources available to State governments. The study also provides a framework for understanding vertical fiscal imbalance and the importance of fiscal equalization in a federal system. Its discussion is relevant to the present research because the exclusion of cesses and surcharges from the divisible pool raises important questions about the distribution of Central tax revenues and the financial position of States. It helps establish the relationship between intergovernmental transfers, fiscal imbalance and the financial autonomy of State governments.[18]

RESEARCH METHODOLOGY

This study employs a theoretical, descriptive, and analytical research methodology to examine the constitutional, legal, and financial aspects of 'cess' and 'surcharge' in India. Furthermore, it analyzes their impact on 'fiscal federalism' and the 'fiscal autonomy' of state governments. The study is primarily based on secondary data, gathered from the Constitution of India, relevant central government legislation, Finance Commission reports, Union Budget documents, Reserve Bank of India (RBI) reports, publications by the Comptroller and Auditor General (CAG) of India, and research papers from recognized academic institutions and research organizations. Particular attention is given to Articles 265, 270, 271, 279, and 280 of the Constitution of India, alongside relevant judicial pronouncements and policy documents. The study adopts a qualitative approach, supported by quantitative and statistical analysis of Gross Tax Revenue, the collection of cesses and surcharges, the 'divisible pool,' and tax devolution to the states. It covers the period from 2011-12 to 2025-26 to investigate shifts in the collection of cesses and surcharges and their subsequent effects on Centre-State financial relations. A descriptive and comparative approach is utilized to analyze the share of 'non-shareable revenues' within the central government's Gross Tax Revenue, in order to assess its impact on the financial resources available to state governments. Furthermore, the recommendations of various Finance Commissions have also been examined to assess the adequacy of the existing tax-transfer mechanism.

Trends in Cess and Surcharge in India

Cess and surcharge have become increasingly important instruments of revenue mobilisation for the Central Government in India. Their growing contribution to government revenue has significant implications for taxation, fiscal federalism, Centre–State financial relations and public expenditure. Although both are additional levies imposed by the Central Government, they differ in their purpose and constitutional treatment.

Cess: A tax imposed for a specific purpose, such as health, education, infrastructure or agricultural development.

Surcharge: An additional charge on an existing tax, generally imposed to raise additional revenue. For example, surcharge on income tax.

An important feature is that neither cess nor surcharge forms part of the divisible pool of central taxes shared with states under the Finance Commission framework.

Historical trends in cess and surcharge collections

The broad trend has been a substantial increase in collections, particularly since 2014–15.

Selected indicators of the changing revenue structure

Financial year	Share in Centre's gross tax revenue
2014–15	9.6%
2017–18	11%
2018–19	15%
2019–20	13%
2020–21	20.5%
2021–22	18%
2022–23	15–16%
2023–24	14%
2024–25	13.94%
2025–26	16.4%

Note: Figures are drawn from different official and research sources and may differ slightly because of accounting coverage and revisions. The 2025–26 figure is reported in a July 2026 account of a Finance Ministry response. [19]

Major components and changing patterns

The increase in cess and surcharge collections is driven by several important levies.

Major levy	Purpose / area of application
Health and Education Cess	Financing health and education initiatives
Road and Infrastructure Cess	Roads and infrastructure development
GST Compensation Cess	Compensation to states for GST-related revenue losses
Agriculture Infrastructure and Development Cess	Agricultural infrastructure
Cess on Crude Oil	Petroleum sector-related revenue
Income-tax surcharge	Additional revenue from higher-income taxpayers
Corporation-tax surcharge	Additional revenue from companies
Social Welfare Surcharge	Customs-related revenue

Cess and Surcharge and the Divisible Pool

cess and surcharge have emerged as significant components of the Central Government's tax revenue in India, influencing the size of the divisible pool and the distribution of financial resources

between the Centre and States. Under Article 270 of the Constitution, the divisible pool comprises shareable central taxes, while cesses and surcharges are excluded from it. Article 271 empowers Parliament to impose surcharges for Union purposes. According to RBI data, the share of cess in gross tax revenue increased from approximately 6.4% in 2011–12 to 17.7% in 2021–22, while the divisible pool's share declined from 88.6% to 78.9% during the same period. This indicates a growing reliance on non-shareable revenue sources. Although the 15th Finance Commission recommended 41% devolution to States for 2021–26, the 16th Finance Commission has retained the same 41% share for 2026–31. However, this percentage applies only to the divisible pool and not to the Centre's entire gross tax revenue.

The increasing reliance on cess and surcharge has generated concerns regarding fiscal federalism and the financial autonomy of States. Since States do not receive a direct share of these collections, an increase in their proportion can reduce the effective resources available for tax devolution, even when the States' devolution percentage remains unchanged. For instance, if gross tax revenue is ₹ 100 and cess and surcharge account for ₹20, with collection costs of ▪ 1, the divisible pool would be ₹ 79. At 41% devolution, States would receive ₹32.39, equivalent to only 32.39% of gross tax revenue. States have therefore expressed concerns about fiscal centralisation, vertical fiscal imbalance and reduced financial flexibility. While cess and surcharge help the Union Government finance infrastructure, health, education and other national priorities, their excessive use may weaken cooperative federalism. Greater transparency in utilisation, rationalisation of non-shareable levies and a sufficiently large divisible pool are essential for ensuring equitable Centre–State financial relations.

Impact on Fiscal Federalism and State Fiscal Autonomy

Fiscal federalism in India has been significantly influenced by the increasing concentration of revenue-raising powers with the Union Government and the expenditure responsibilities of States. Under the constitutional framework, the Finance Commission recommends the distribution of central tax revenues between the Centre and States under Article 280. The 15th Finance Commission recommended 41% vertical tax devolution to States for 2021–26, and the 16th Finance Commission has retained the same share for 2026–31. However, the increasing reliance on cesses and surcharges, which are excluded from the divisible pool under Article 270, has raised concerns about the actual resources available to States. RBI data indicates that the share of cess in gross tax revenue increased from 6.4% in 2011–12 to 17.7% in 2021–22, while the divisible pool's share declined from 88.6% to 78.9%. This has implications for States' revenue receipts, particularly those heavily dependent on central tax devolution. The vertical fiscal imbalance is further intensified because States are responsible for major expenditure areas such as health, education, agriculture, rural development and public infrastructure, while their independent revenue-raising capacity remains relatively limited.

[1]The increasing use of centrally collected non-shareable revenues can reduce the effective fiscal autonomy of States and increase their dependence on Finance Commission transfers, grants-in-aid and centrally sponsored schemes. Differences in tax bases, economic development and revenue-generating capacities also create horizontal fiscal inequalities among States. States with lower per capita income and greater developmental requirements may face additional difficulties in financing public services and infrastructure. Conditional grants and centrally designed schemes can further restrict the flexibility of State Governments in determining expenditure priorities according to local needs. This has generated concerns regarding fiscal centralisation, transparency, accountability and the spirit of cooperative federalism. Although the Centre argues that cesses and surcharges finance important national priorities, States have demanded greater predictability in tax devolution and a wider shareable revenue base. Strengthening fiscal federalism requires rationalisation of cesses and surcharges, transparent utilisation of collections, timely transfer of funds and greater consultation with States. Ultimately, meaningful fiscal autonomy depends not merely on increasing the percentage of tax devolution but also on ensuring that States have adequate, predictable and flexible financial resources to fulfil their constitutional and developmental responsibilities.[20]

Cesses and Surcharges

The Fifteenth Finance Commission examines the constitutional, legal and fiscal aspects of cess and surcharge in India. The study critically analyses the increasing use of these additional tax instruments by the Central Government and their impact on the fiscal relationship between the Central and State Governments. It points out that cess is generally levied for a specific purpose, whereas surcharge is an additional levy imposed on existing taxes to augment the revenue of the Central Government. The report highlights that the revenue from cess and surcharge is generally kept out of the distributable pool of central taxes under the constitutional framework, resulting in greater concentration of fiscal resources at the Union level. It further examines how the increasing reliance on these non-shareable revenue instruments may reduce the proportion of central tax revenue available for distribution to the States, thereby affecting their fiscal capacity and fiscal autonomy. The study also identifies concerns related to utilization, transparency, accountability and continuation of cess collection beyond their intended purpose. It emphasizes the need for a more transparent and accountable tax structure to ensure that the revenue collected through cess is properly utilized for its intended purposes. The report argues that excessive reliance on surcharge may also affect the equitable distribution of fiscal resources between the Centre and the States. It concludes that appropriate reforms are necessary to rationalize the utilization of cess and surcharge, strengthen the tax devolution mechanism and maintain the right balance between the revenue needs of the Central Government and the fiscal interests of the State Governments. This research is highly relevant to the present study as it provides an important constitutional and economic foundation for understanding the impact of cess and surcharge on fiscal federalism in India and the fiscal autonomy of the States.

State Finances: A Study of Budgets

State finances refer to the income and expenditure of a state government. They include the collection of revenue, allocation of funds, public expenditure, borrowing and management of financial resources.

Sources of State Government Revenue

Source	Description
State GST (SGST)	Tax collected on goods and services
State Excise Duty	Tax on alcohol and related products
Stamp Duty	Revenue from property transactions
Registration Fees	Fees for registering property and documents
Motor Vehicle Tax	Tax collected from vehicles
Electricity Duty	Tax on electricity consumption
Land Revenue	Revenue collected from land
Non-Tax Revenue	Fees, fines, penalties and service charges
Central Tax Devolution	Share of central government taxes
Grants-in-Aid	Financial assistance from the central government

Components of a State Budget

Component	Meaning
Revenue Receipts	Income that does not create liabilities or reduce assets
Capital Receipts	Borrowings and receipts from asset sales or loan recovery
Revenue Expenditure	Regular government operating expenses
Capital Expenditure	Spending on infrastructure and asset creation
Fiscal Deficit	Total expenditure minus revenue receipts and non-debt capital receipts
Revenue Deficit	Revenue expenditure minus revenue receipts
Primary Deficit	Fiscal deficit minus interest payments

Intergovernmental Transfers and Fiscal Equalization

Cess and Surcharge in India: Impact on Fiscal Federalism and Fiscal Autonomy of States

Intergovernmental Transfers in India

Intergovernmental transfers refer to the financial resources transferred by the Central Government to State Governments through tax devolution, grants-in-aid and centrally sponsored schemes.

Type of transfer	Financial mechanism
Tax Devolution	Distribution of central taxes between Centre and States
Finance Commission Grants	Grants recommended by the Finance Commission
Revenue Deficit Grants	Financial support to states with post-devolution revenue deficits
Centrally Sponsored Schemes	Funds allocated for specific development programmes
Disaster Management Grants	Financial assistance for disaster preparedness and relief
Local Government Grants	Funds transferred to Panchayati Raj institutions and urban local bodies
GST Compensation	Compensation for revenue losses arising from GST implementation

States' Share in Central Taxes

Finance Commission	States' share in divisible pool
10th Finance Commission	29.0%
11th Finance Commission	29.5%
12th Finance Commission	30.5%
13th Finance Commission	32.0%
14th Finance Commission	42.0%
15th Finance Commission	41.0%
16th Finance Commission	41.0%

The 14th Finance Commission recommended 42%; the 15th and 16th Finance Commissions recommended 41%. The reduction reflects the creation of the Union Territories of Jammu and Kashmir and Ladakh.[21]

Cess and Surcharge as a Percentage of Centre's Gross Tax Revenue

Financial year	Cess and surcharge (% of GTR)
2011–12	6.4%
2012–13	6.8%
2013–14	6.7%
2014–15	6.8%
2015–16	9.1%
2016–17	9.9%
2017–18	11.2%
2018–19	12.9%
2019–20	14.6%
2020–21	19.7%
2021–22	17.7%

DISCCUSION

The increase in the collection of cess and surcharges by the Central Government and its collection has emerged as important features in the Indian structure. While the use of these financial instruments is recognised under Article 270 of the Constitution of India, their increasing contribution by the Central Government raises concerns about the equitable distribution of financial resources between the Centre and the States. The shareable parts of central taxes, and surcharges, are generally apportioned in a manner that limits the share of tax revenue that can be distributed to the States. 270 The division of Union-specific taxes between the Centre and the State Governments, 271 empowers Parliament to impose surcharges for the purposes of the Union. The increasing reliance on these instruments has created a gap between the proposed percentage and the actual resources of the states. Although the Fifteenth and Sixteenth Amendments had placed the share of states in the distributable pool, it does not mean that the increase in non-shared revenue sources to 41% has increased the fiscal imbalance, fiscal decentralization and the principles of cooperative federalism. Moreover, the implementation of GST has brought about a change in the national structure and the central GST compensation cess has also brought about the complexity involved in maintaining the federal revenue security and fiscal neutrality. Thus, the transparency, accountability, revenue-sharing in the form of cesses and surcharges raises important questions about the constitutional spirit of fiscal federalism.

Cess and surcharges have an impact on the states, which are responsible for a wide range of essential public services including education, health, agriculture, infrastructure, rural development and welfare. Less effective tax allocation may reduce the availability of untapped financial resources and increase the dependence of states on grants-in-aid and centrally sponsored schemes. This situation is likely to be exacerbated by elected state governments. States with limited spending capacity face significant challenges in managing their responsibilities. This issue is even more important in view of the fact that even financially strong states face challenges in delivering basic infrastructure and welfare programmes. Moreover, the increased burden of resources collected at the level of the central government, coupled with a large expenditure burden at the unit level, may exacerbate the existing fiscal imbalances. Thus, the Finance Commission, GAT Coal and other intergovernmental institutions should strengthen public accountability to maintain federal fiscal balance, including through greater transparency in expenditure, unspent balances and budget reporting. The current revenue sharing structure should also be reviewed to ensure that the fiscal independence of the states is compromised by the solid fiscal needs of the central government. A more equitable distribution system, better consultation, and predictability in tax distribution can promote cooperation and trust. Finally, the issue of cess and surcharge is a matter of revenue generation, with a view to ensuring checks and balances, democratic accountability, impartiality and the ability of state governments to perform their respective responsibilities.

CONCLUSION

In India, cesses and surcharges have become essential revenue-raising tools for the central government, but their increasing use has raised serious concerns about fiscal federalism and the financial autonomy of state governments. Although these revenue instruments are constitutionally permitted under Articles 270 and 271, their exclusion from the divisible pool reduces the share of gross tax revenue that can be distributed among the states. This situation poses challenges to equitable resource sharing, vertical fiscal balance, and cooperative federalism. The central government's reliance on non-share revenues has also raised questions about the effectiveness of the current tax devolution mechanism and the financial health of state governments. Since states are responsible for major development projects such as education, healthcare, agriculture, infrastructure, and welfare, sufficient and predictable financial resources are essential to fulfill their constitutional and administrative responsibilities. This study emphasizes the importance of maintaining a proper balance between the fiscal needs of the central government and the fiscal power of state governments. Strengthening India's federal financial system requires greater transparency in cess and surcharge collection, better revenue utilization, improved financial accountability, and a more equitable tax sharing system. The Finance Commission and the GST Council need to do a better job of addressing state concerns and promoting

effective financial decentralization. Furthermore, the central government should ensure that excessive reliance on cess and surcharge collection does not undermine the spirit of cooperative federalism or hinder states' development priorities. Frequent review of unallocated funds, greater coordination with state governments, and appropriate institutional reforms can contribute to a more balanced funding system. Finally, strengthening state financial autonomy is essential to ensuring democratic accountability, regional equity, inclusive economic development, and balanced national growth. A system of transparent, fair and coherent financial federalism will help maintain constitutional coordination between the Centre and the states, while also ensuring that both levels of government have adequate financial resources to fulfil their respective responsibilities.

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