Subject Name: Constitution Law
Topic Name: Financial relationship between Centre and State

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The Indian Constitution provides distinct revenue streams for both the Centre and the States, establishing a clear demarcation of taxing powers between them. The Union holds specific taxation authority encompassing income tax, corporate taxes, customs duties, excise duties, estate and wealth taxes, and fees pertaining to matters listed under the Union List.

State's Taxation Authority

Conversely, the States wield primary taxation powers over land revenue, stamp duties, agricultural income tax, passenger tax, entry taxes, and notably, sales taxes and duties on alcohol and other intoxicants as outlined in the State List.

Revenue Sharing Between Union and States

Recognizing that States might not achieve financial self-reliance autonomously, the Constitution mandates the sharing of certain revenue items between the Union and the States. Key aspects of this arrangement include duties levied by the Union but collected and utilised by the States (such as stamp duties and excise duties on medicinal and toilet preparations), and duties and taxes levied and collected by the Union but assigned to the States (such as railways passenger fares tax or grants in lieu of it).

Service Tax and Revenue Sharing

Additionally, Article 268A, introduced by the Constitution 88th Amendment Act, 2003, empowers the Union to levy service taxes, with collection and appropriation by both Union and States guided by principles formulated by Parliament.

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Income Tax and Excise Duties Sharing

Income tax and Union excise duties, though levied and collected by the Union, are shared with the States according to the recommendations of the Finance Commission. However, surcharges on duties and taxes, as well as income tax paid by corporate enterprises, are not shareable.

Constitutional Amendments and Financial Allocation

The Tenth Finance Commission recommended that 29 percent of the total income obtained from certain Central taxes and duties be allocated to the States, a recommendation enacted into law through the Constitution (80th Amendment) Act, 2000.

Allocation of Taxes and Duties

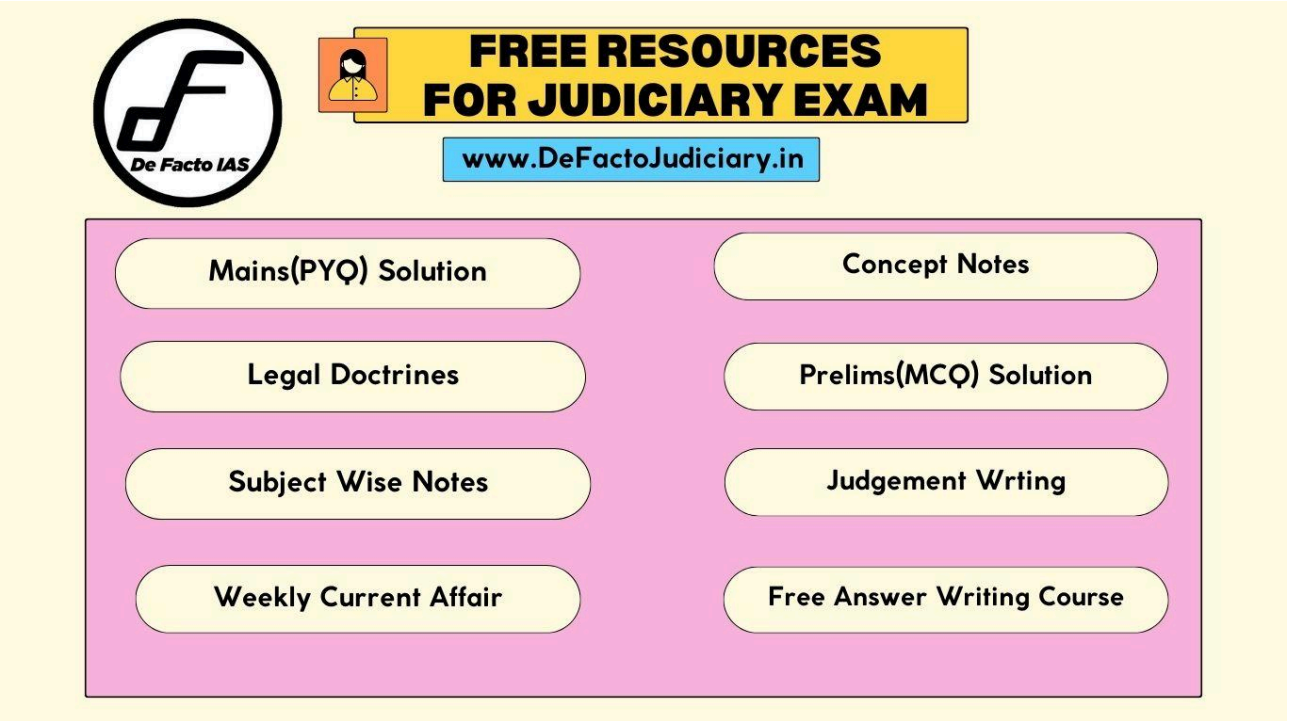
Further amendments include Article 269, which specifies the assignment of taxes on the sale or purchase of goods to the States, and Article 270, which mandates the distribution of taxes and duties referred to in the Union List between the Union and the States.

Role of the Finance Commission

The Constitution mandates the establishment of a Finance Commission by the President within two years of the Constitution's commencement and subsequently, at the conclusion of every five years (Art. 280).

Functions of the Finance Commission

Comprising a Chairman and four members, the Finance Commission's composition adheres to qualifications set by Parliament. The primary functions of the Finance Commission encompass recommending to the President the framework for distributing the net proceeds of taxes between the Centre and the States; advising on the principles governing grants-in-aid from the Consolidated



Fund of India to States; and offering guidance to the President on any other financial matter referred to the Commission in the interest of sound fiscal management. Article 281 stipulates that the President must present every recommendation of the Finance Commission before each House of Parliament, accompanied by an explanatory memorandum.