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The National Finance Commission Award and Centre-Province Relationship: A Study of Pakistani Federal Structure*

Abstract

The constitution of 1973 entails a mechanism for the distribution of the revenue among the federating units. Since the distribution of revenue assets is considered a very technical and critical issue with its far reaching implications between the federation and the federating units, any kind of misappropriation causes economic, social and political discontent in the centre- province relationship. In the federation of Pakistan it is noticed that there is inter-provincial disparities in income distribution, capabilities in tax collection and expenditure disbursement. Through the constitution of Pakistan most of the revenues are collected by the Federal Government and then they are redistributed between the federal and provincial governments and then amongst the provinces under an arrangement called the National Finance Commission Award. The National Finance Commission was established in 1951 with following objectives, to support the provincial governments to meet their expenses and to reduce the horizontal imbalances among the provinces, 'the depending of the revenue capacity of the constituent units of the federation. Again the provincial government was strongly complainant against the federal government not helping and fulfilling the legal requirements needed for the external support of the power projects

Introduction

Financial management issues in our country revolve in a concept of fiscal federalism which is a part of broader public finance discipline. "Fiscal federalism deals with the division of governmental functions and financial relations among levels of government. The term fiscal federalism was introduced by the German-born American economist Richard Musgrave in 1959."¹

Considering the fact the fact that Pakistan is a developing country and democracies are weak and fragile in the developing countries. Most of these developing countries have a strong colonial legacy and many others have suffered authoritarian regimes.

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Democratic governments have remained in problem in these developing countries. Pakistan is a country with a history of conflicts and weak political institutions. The early years of the history of federalism in Pakistan has remained a period uncertainty with a number of national issues that the newly born state was facing. This uncertainty also resulted into civil military conflicts, mostly for the sake of power in the country. The military mindset or in other words the strong establishment has favoured strong federation and have resisted the concept of provincial autonomy. Financial dimensions are one of the most important concerns in the centre province relationship of Pakistan. “In the history of Pakistan the distribution of financial resources between the federation and the federating units has dominated the federal landscape.”²

Historical Perspective

Before independence and the establishment of Pakistan Revenue Sharing, *Niemeyer* Award was the distribution formula under the act of 1935. The formula was followed to distribute the resources between federal and provincial governments under the British. Under the act of 1935 sales tax was a provincial subject and income tax collection was redistributed as 50 percent of the total income tax collection. As Pakistan was established, it is observed that till March 1952, the same formula of award was followed with some adjustments.

After independence about the revenue Sharing Arrangements Sir Jeremy Raisman³ was assigned to make an arrangement and formulate an acceptable revenue sharing formula for the federation of Pakistan and federating units of the country. Extensive consultations were made by Raisman and an Award was finally announced by 1952.⁴ The arrangements made under Raisman Award were of 50 percent of income tax, “East Pakistan government was entitled to 45 percent of the federal divisible pool whereas West Pakistan got the remaining share.”⁵ By 1955, after the arrangements, two separate units were made for the federation, namely East and West Pakistan and two awards for year 1961 and 1964 were announced during that period under this award. It was out of the divisible pool (70% of sales tax plus other taxes), East Pakistan and West Pakistan got 54% and 46% share, respectively. 30% of sales tax was assigned to the provinces on the basis of collection in their respective areas.⁶

In these Awards the remaining duties especially on agricultural land and on assets value tax on property were given to the federating units as their own collection. In the 1964 National Finance Commission Award, it was constituted according to the “Article 144 of the 1962 Constitution. In this Award of 1964 the divisible pool was consisted of the collection from sales tax, income tax, the export duty and the excise duty. In the Award however 30% of sales tax was distributed in accordance with its collection in each province.”⁷

Financial Distribution Arrangements under the 1973 Constitution

The Constitution of 1973 clearly defines the arrangements, parameters and procedures regarding the establishment of National Finance Commission. There was also basic framework for allocation of financial powers and the distribution of revenues between the provinces and the federation. In the “Article 160 of the Constitution of Pakistan the details for the establishment of the National Finance

Commission”⁸ are provided. The constitution arrangements of National Finance Commission are as follows:

1. Inside a half year of the beginning day and from there on at interims not surpassing five years, the President will comprise a 'National Finance Commission' comprising of the Minister of Finance of the Federal Government, the Ministers of Finance of the Provincial Governments and such different people as might be named by the President after counsel with the Governors of the Provinces.⁹
2. It will be the obligation of the National Finance Commission to make suggestions to the President as to (a) the circulation between the Federation and the Provinces of the net continues of the expenses referenced in condition (3); (b) the creation of awards in-help by the Federal Government to the Provincial Governments; (c) the activity by the Federal Government and the Provincial Governments of the obtaining forces given by the Constitution; and (d) some other issue identifying with fund alluded to the Commission by the President.
3. The charges alluded to in passage (an) of condition (2) are the accompanying expenses raised under the expert of (Majlis-e-Shoora (Parliament)), to be specific: - (I) imposes on salary, including partnership charge, however excluding assessments on pay comprising of compensation paid out of the Federal Consolidated Fund; (ii) assesses on the deals and buys of merchandise imported, sent out, delivered, fabricated or expended; (iii) send out obligations on cotton, and such other fare obligations as might be indicated by the President; (iii) trade obligations on cotton, and such other fare obligations as might be determined by the President; (iv) such obligations of activity as might be determined by the President; and (v) such different duties as might be determined by the President.¹⁰
4. When might be subsequent to accepting the proposal, of the National Finance Commission, the President will, by Order, indicate, as per the suggestions of the Commission under passage (an) of proviso (2), the offer of the net continues of the duties referenced in condition (3) which is to be allotted to every Province, and that offer will be paid to the Government of the Province concerned, and, despite the arrangement of Article 78 will not shape some portion of the Federal Consolidated Fund.¹¹
5. The suggestions of the National Finance Commission, together with an illustrative notice with regards to the move made subsequently, will be laid before the two Houses and the Provincial Assemblies.¹²
6. At whenever before an Order under proviso (4) is made, the President may, by Order, make such revisions or adjustments in the law identifying with the conveyance of incomes between the Federal Government and the Provincial Governments as he may esteem vital or convenient.¹³
7. “The President may, by Order, make grants-in-aid of the revenues of the Provinces in need of assistance and such grants shall be charged upon the Federal Consolidated Fund.”¹⁴

In pursuance of the powers granted by the constitution, the President of Pakistan announced the 7th National Finance Commission on 24th July, 2009. The required deliberations and deep consultations amongst all the stakeholders were made. And ultimately the recommendations of the Award were announced on December 2009. Before the 7th National Finance Commission Award there were two arrangements made for the distribution of the financial assets. The white paper budget of the government of the Punjab describe as follows:

“...under the arrangements envisaged in 1973 Constitution, four regular, two interim awards and in 2006, a Presidential Order for distribution of revenue were announced for the resource distribution among the federation and different federating units.”¹⁵

The constitution of 1973 provides a mechanism for the distribution of the revenue among the federating units. The mechanism provided by the constitution about the distribution of revenues need to be revised every after five years. The distribution of revenue assets is considered a very technical and critical issue with its far reaching implications between the federation and the federating units. Any kind of misappropriation may cause economic, social and political unrest in the center province relationship. In the federation of Pakistan “...inter-provincial disparities in income distribution, capabilities in tax collection and expenditure disbursement there is a strong need for the fiscal arrangement between the federal and provincial governments.”¹⁶ It is considered that the federal government is more efficient in the revenue collection and it work is an open environment as compare to the federating units. In infrastructure the federal government is also facilitated more strong and efficient missionary to work for the collection of revenue. Similarly the small taxes are relatively managed by the provincial governments.

Financial management issues in our country revolve in a concept of fiscal federalism. Through the constitution of Pakistan “most of the revenues are collected by the Federal Government and then they are redistributed between the federal and provincial governments and then amongst the provinces under an arrangement called the National Finance Commission Award.”¹⁷ The National Finance Commission was established in 1951 with two prime objectives:

1. “To support the provincial governments to meet their expenses.
2. To reduce the horizontal imbalances among the provinces, ‘the depending of the revenue capacity of the constituent units of the federation.’”¹⁸

The financial situation of provincial governments is largely based on federal transfers of financial assets to the provinces as described in the constitution through National Finance Commission (NFC) Awards. The National Finance Commission is a series of planned award that the federal government of Pakistan gives to the provinces. This series for the distribution economic award was started in 1951.¹⁹ The National Finance Commission is described and structured in the constitution of Pakistan under the article 160.

The National Finance Commission program was emerged to adjust the financial issues and “equally managed the financial resources for all the federating units of the country. It was aimed that four provinces should meet their expenditure and liabilities while alleviating the economic disparities.”²⁰ Furthermore, “according to

the constitution of Pakistan, the National Finance Commission Awards are the designs of financial distribution formulas for the economic distribution to the provincial government for the five years.”²¹ In the history of the country together, a total number of seven awards have been awarded to the provinces since it has started dated 1951. These were the days of the founding leader and Prime Minister Liaquat Ali Khan. The directions are mentioned in ...“the Constitution, the provincial governments and federal government tries to get higher share of the financial revenues to make their own economy more strong and affective.”²²

In the light of the ...“constitution, these awards design the formula of distribution of resources between federal and provincial governments, and among the provinces for five years.”²³ It is observed and according to the spirit of the constitution the federal government and all federating units tries their best to get a maximum share of the financial resources in order to strengthen their own financial situation. So as a result, there are very few examples of consensus and conclusive National Finance Commission Awards in the past. There are very few conclusive awards in the history of the country with a different kind of gains. In the 1991 National Finance Commission Awards, the federating units (provincial governments) were the main beneficiaries and they received substantial amount of shares like sales tax and income tax. While in 1997, the biggest amount of the National Finance Commission Award was the federal government share which tried to raise its financial status. If we go in the details of the parameters of the National Finance Commission awards, the increase in the share of one unit will affect the rest of units by some kind of decrease in the share. So it was sensitivity attached to the sharing formula. One feels that it was difficult to reach on a consensus between the federal and the provincial governments. In his difficult pattern after 1971 only three times there was consensus over the financial distribution formula. These were the National Finance Commission years of 1974, 1991 and 1997, and one may also see the 2006, presidential distribution order during the Musharraf times.

The history of Pakistan has been very frequent in all kind of experiments which can be observed in politics, economy, institutional building and even constitution. Though the country is considered a resourceful one with various kind of natural resources. Most of the population of Pakistan is associated with agriculture and vast plains and the unique canal system provides a favorable atmosphere for agriculture. However it also gives an impression of a primitive society. The rural society of Pakistan still has to go for a transformation and there is a responsibility of the federal government for this essential change. The federating units are not satisfied with the policies of federal government particularly with the distribution of financial resources.

In the study of centre province relationship the power has played a very important role. Till the separation of East Pakistan in 1971, power has strongly affected the in the centre province relations. The main grievance of the people of Bengal was the fiscal issue and they were deeply concerned that the federal government had been adopting the strong centralized policies. Hussain Haqqani, a famous writer and former ambassador of Pakistan to the United States gives another view for the understanding of the political developments in the history of the country since 1947. This concern became deeper with the passage of time and a sense of being ignored was prevailing in East Pakistan.²⁴ As a result eventually the incident of 1971 was

witnessed by the history of the country. Later the history of the country can again be divided into democratic and dictatorial regimes. The military dictatorship have dominated the executive authority and thus weakened the democratic regimes by introducing the constitutional amendments, (details are given in the 4th chapter). The elections of 2008 brought the democratic government who tried to perform well after a long dictatorship of Pervaiz Musharrf. The National Finance Commission is the institution who divides the fiscal shares and revenues from the federal government to the provinces. The National Finance Commission Award is only presented as the provinces show consensus otherwise it is rejected. In the history of the country, the National Finance Commission Award is only accepted in the democratic regimes. In the long dictatorial tenure of General Zia (1977-1988) and later during General Musharaff (1999-2008) rule the National Finance Commission Award National Finance Commission remained failed. This is also a reflection that the country has suffered and the growth and development has hampered due to the dictatorial regimes. Out of the nine National Finance Commission awards only four times the award remained successful and conclusive. These successful awards came in the time of democratic governments.

The election of 2008 brought the democratic government back to the country. It was a very positive development in the disturbed political scenario of Pakistan. The post 9/11 situation brought a huge destruction for every sphere of the country. Terrorism was killing the innocent civilians. In this worse situation the social and economic development was hampered and the economy of the country was derailed. The election of 2008 brought the democratic government of PPP and the government tried to make some genuine democratic policies. The federal government tried to follow the policy of reconciliation. The major achievement was the restoration of the true spirit of the constitution of 1973. The 18th amendment was a strong move for the provincial autonomy and thus a way forward for successful strong federation. In Pakistan the financial resources of the provinces are largely dependent upon the share of revenue that the provinces get from the federal government. The 7th National Finance Commission Award of 2010 is a great example in the economic history of Pakistan so far as the provincial economy is concerned. The award was presented by PPP Prime Minister Yousaf Raza Gilani and it changed the traditional approaches of the federation towards the provinces and this was primarily due to the 18th amendment. The distribution of economic resources was according to constitution of 1973, the articles of 160 and 165 are the constitution of Pakistan deals with the National Finance Commission Award and the economic affairs. “According to the constitution of Pakistan the National Finance Commission Award is presented for five years.”²⁵

If we look in to the history of National Finance Commission Award, the previous distributions were made according to the proportion of population. It is important here to mention that traditionally the provinces always tried to get the maximum share in the National Finance Commission to stabilize their financial status. This had remained the main reason and there was hardly consensus in the National Finance Commission Awards. The history of National Finance Commission awards shows that the gainers have remained different. For example in 1991 the provinces got the main share in the resources while in 1997 the federal government was the main beneficiary in the National Finance Commission Award. The federal

government attached some sensitivity in the distribution formula.²⁶ However the 7th National Finance Commission Award was unique and followed changed approaches and other factors were also included along with the population, these were revenue collection, backwardness / poverty, and population density. The 18th amendment was a step towards a successful federation with autonomous federating units and it gave an independent working position to the provinces. There was a strong and positive impact among the relations of the provinces and some of the legal institutions brought provinces close to each other and close to the federation. These include CCI²⁷, NEC²⁸ and the National Finance Commission. These steps gave a platform to the provinces for a balanced growth of their specific regions. It was also a goodwill gesture from the federation which also resulted into the consensus of National Finance Commission Award. Regarding fiscal decentralization it is to be noted that the revenue is collected by the federal government and through National Finance Commission award the income is distributed between the federation and the federating units. The provincial governments further trickle it down for the development and the expenditures.

Conclusion

It is concluded that before 1971 the main grievance of the people of Bengal against the Federation were the fiscal issues and financial assets which Bengal complained about being given to it as had been apportioned in the Constitution of 1962. It was a very deep concern that the federal government had been adopting the strong centralized policies. This concern became more focused with the passage of time and a sense of being ignored was prevailing in East Pakistan. It was this deep concern that eventually the incident of 1971 was witnessed by the history of the country. Keeping in view the past mistakes the Constitution of 1973 was framed and thus a balance between Federation and its federating units was created. However, the history of Pakistan can again be divided into kind of regimes namely democratic and military dictatorial regimes. The military dictatorship have dominated the executive authority and thus weakened the democratic regimes by introducing the constitutional amendments and thus balance between the federation and provinces was disturbed and it encouraged centrifugal forces to demand for their appropriate share in the state structure of Pakistan. This led to the uneasiness and chaos in Balochistan especially after the assassination of Akbar Khan Bhugti in 2006 who was also complaining the over centralization of the federation. The history of Pakistan witness that the provinces complained against the over centralization of military regimes but in democratic period the balance somehow was restored and this exactly happened when the PPP and PMLN formed governments in the centre and provinces in 2008. As has been discussed above that the National Finance Commission is the institution which divides and distributes the fiscal shares and revenues from the federal government to the provinces and it was working neither justly nor appropriately when Musharraf era came to an end. The enforcement of the 18th Constitutional Amendment in 2010 and the other was approval of the National Finance Commission Award in 2009. Despite minor political differences the democratic parties under the democratic governments work with better understanding and take decisions with consensus and democratic process. Naturally these democratic values with sound and solid decisions for the betterment of the

people always lead to the consolidation of the federal structure and thus naturally country moves towards peace and prosperity.

Notes & References

- ¹ *Encyclopedia Britannica*, Fiscal Federalism.
- ² Mohammad Waseem, *Federalism in Pakistan* (Islamabad: Forum of Federation, 2010). 91.
- ³ Raisman, Sir (Abraham) Jeremy (1892–1978), he was a British economist and banker. He was born in Leeds in 1892 and in 1916 he join the Indian Civil Services, he was posted in Bihar and then in Orissa, then he joined the department of custom in Bombay and later in Calcutta and then served as commissioner of income tax in the Punjab and the Northwest Frontier Province. He joined India's central government in 1931 as a joint secretary in the Commerce Department. Then he was appointed secretary in the Finance Department. From 1939 to 1945 he served as finance member of the government of India. In 1944 he led India to the International Monetary Conference at Bretton Woods (New Hampshire). This conference resulted in the formation of the International Monetary Fund and the International Bank for Reconstruction and Development in 1944. In 1939 he was knighted. He was resigned in 1945 from the Indian civil service. He had been helpful for many Jewish refugees in the Europe. After his retirement he served as an adviser to several newly independent countries including Pakistan.
- ⁴ The Raisman Award was a series of economic programs established by Pakistan in 1951. The understanding of the program emerged in 1947 to provide a solution of the sharing of total revenue. The program was announced by PM Liaqat Ali Khan in 1947. It was a part of his new economic policy to curb the political discrepancies and economic preferences.
- ⁵ *White Paper Budget 2010-11* (Lahore: Government of the Punjab, June 14, 2010), 105.
- ⁶ *Ibid.* 105
- ⁷ *Ibid.*, 106.
- ⁸ <https://pakistanconstitutionlaw.com/article-160-national-finance-commission/> Retrieved on 15.04.2018.
- ⁹ *Ibid.*
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- ¹⁶ *Pakistan Economic and Social Review* Volume 44, No. 2 (Winter 2006), p. 209.
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²⁴ For Details see, *Haqqani, Hussain (2005). Pakistan: Between Mosque and Military. United Book Press. ISBN 978-0-87003-214-1.*, Chapter 3.

²⁵ Muhammad Sabir, “Financial Implications of the 7th National Finance Commission Award and the Impact on Social Services”, https://www.researchgate.net/publication/241764991_Financial_Implications_of_the_7th_National_Finance_Commission_Award_and_the_Impact_on_Social_Services. Accessed on 08.11.2017

²⁶ Ibid.

²⁷ Council of Common Interest (CCI)

²⁸ National Economic Council (NEC)