

**1. What are the most pressing challenges of governance arising due to India's federal polity? Examine.**

**Approach:**

As the directive in the question is 'examine' it is important to mention challenges in a detailed manner with clear logical exposition, use of proper and appropriate examples is a must, moreover explanation of the state of India's federal system is also important.

**Introduction:**

Federalism in its literal sense is a system of government in which power is divided between a central authority and constituent political units. India's federal structure is very peculiar in nature, it encompasses all those features which suit India's polity according to its own needs and thus has helped India to grow as the largest functional democracy of the world. According to K.C. Wheare the Indian Constitution, can be described as "a system of government which is Quasi Federal a unitary state with subsidiary federal state with subsidiary unitary features." Prof. Wheare observes that "the federal principles is the method of dividing powers so that the general and regional government are each within a sphere are co-ordinate and independent. Both the federal and the regional governments are co-ordinating and independent in their spheres and not subordinate to one another."

**Body:**

**Structure of India's federal polity-**

- Article 1 of the Constitution of India states that 'India that is Bharat shall be a union of states. Indian federation was not a product of coming together of states to form the federal union of India. It was rather a conversion of a unitary system into a federal system. It is a compromise between two conflicting considerations such as autonomy enjoyed by states within the constitutionally prescribed limit (State List) and the need for a strong centre in view of the unity and integrity of the country (Union List).
- India's federalism is asymmetric in nature the main forms of administrative units in India are the Centre and the States. But there are other forms, too, all set up to address specific local, historical and geographical contexts. Besides the Centre and the States, the country has Union Territories with a legislature, and Union Territories without a legislature. Just as the Centre and the States do not have matching powers in all matters, there are some differences in the way some States and other constituent units of the Indian Union relate to the Centre. This creates a notable asymmetry in the way Indian federalism works. Examples are Article 371, The Sixth Schedule to the

Constitution contains provisions for the administration of tribal areas in Assam, Meghalaya, Tripura and Mizoram. These create autonomous districts and autonomous regions.

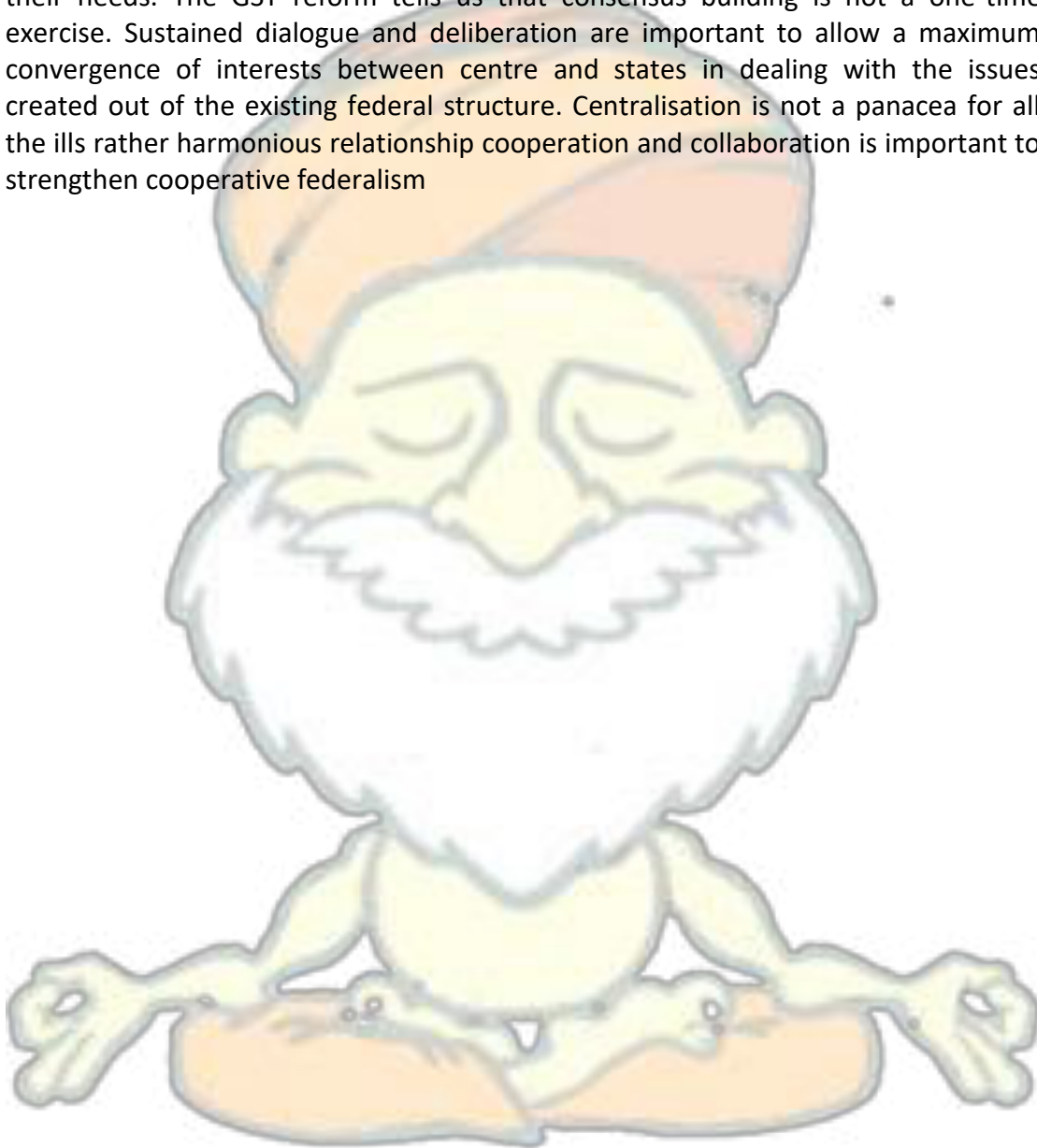
**Challenges of governance due to federal polity-**

- India has 25 major river basins with most rivers flowing across states, with rivers being shared between states. Adequate involvement of centre is necessary for preservation and equitable distribution of river water. However inter-state rivers have become sites of contestation between states because of the conflictual federalism dispute resolution has become a long and tiresome process which creates problems of water availability, for agriculture and drinking purpose. Centres role only comes in dispute resolution in spite of legal framework in the form of Inter State River Water Disputes Act 1956 and River Boards Act 1956.
- Even as Indian Federalism has a tendency towards centralised form, states have sought to assert their interests and influence over the years. This led to imbalance and inconsistency in central governments approach towards the issues which effect country in general such as Tamil issue in Srilanka, river water dispute with Bangladesh etc.
- Increased regional demands such as creation of new states developmental issues ad excess to the resources has led to the conflicts taking India's internal security a hostage.
- One of the most pressing needs of India after its independence was the distribution of land to the landless who have suffered at the hands of colonial powers, but because of the nature of federal polity with distribution of subjects and agriculture and land distribution coming under the purview of states idea of land reforms could not be materialised as envisaged.
- Uneven development is one of the important issues arising out of the existing federal structure in India many of the states inspite of being resource rich could not prosper because policy paralysis and politics based on emotions of caste, and communalism thus development took a back seat.
- Lax attitude of states in implementing centrally sponsored schemes has led to an imbalance in critical social sectors like health and education among the states. An important scheme in the heath sector like Jan Arogya has not been implemented in states like West Bengal, Maharashtra etc.
- In India it is too hard and difficult to bring in comprehensive socio economic and political reforms because of the nature of federal polity. Recent initiatives like GST which revolutionised indirect tax structure in India took around 15 years of deliberations and discussions between states and centre.
- New challenges like environmental issues are impossible to implement unless states play an important role to the commitments in implementing the decisions taken at central level and the commitments India have made at the Paris Conference on Climate Change.
- With the advancement of technology like Industrial Revolution 4.0 and internet of things machine learning, role of states is important in bringing out reforms like ease of doing business, skill development, infrastructural

development so that India does not lag behind and could reap the benefits of demographic dividend.

**Conclusion:**

A diverse country like India needs a proper Balance towards maintaining the needs of the states where they can frame and implement laws and policies according to their needs. The GST reform tells us that consensus building is not a one-time exercise. Sustained dialogue and deliberation are important to allow a maximum convergence of interests between centre and states in dealing with the issues created out of the existing federal structure. Centralisation is not a panacea for all the ills rather harmonious relationship cooperation and collaboration is important to strengthen cooperative federalism



**2. While briefly explaining the concepts, illustrate the benefits of cooperative and competitive federalism?**

**Approach**

A straightforward question where in you need to explain the concepts of cooperative and competitive federalism in brief in the first part of the answer while also illustrating the benefits of both competitive and cooperative federalism in the second part of the answer.

**Introduction**

The quasi-federal structure of the Indian nation was settled in after the country became free of colonialism and gained independence from the British. This style of federalism is responsible for the introduction of its cooperative as well as competitive variants in the country.

**Body**

- The Constitution of India has created a strong Central government, but at the same time, it has not made the state governments weak and has not reduced them to the level of administrative agencies for the execution of policies of the Central government. Rather, the states have an independent constitutional existence.
- The concept of cooperative federalism professes a horizontal relationship between the Central as well as the State governments. This essentially means that the legislature at the Union as well as the State levels cooperate to serve the larger public interest. Such an arrangement, if executed successfully, would be a significant leap in enabling the participation of States in determining national policies.
- Usually cooperative federalism is seen in socialist economies where most of the resources are controlled by the government. It is being promoted in India through steps like the formation of NITI aayog, passing of GST etc.
- On the other hand, competitive federalism, the States share a vertical relationship with the Central government while competing amongst themselves. Essentially, States individually work towards attracting funds and investment to aid their developmental activities. This leads to the formation of a free market scenario amongst the States wherein they play the role of the sellers and the investors become the buyers.
- A type of Competitive federalism is seen in India where states want more funds and perks from the state government for growth. Also states can be involved in International treaties and business deals. They are also trying to woo MNCs to get more FDI.

The benefits of co-operative federalism can be seen from the points given below –

- The essence of co-operative federalism is that the Centre and the State Governments should be guided by the broader national concerns of using the available resources for the benefit of the people.
- Co-operative federalism encourages the Government at different levels to take advantage of a large national market, diverse and rich natural resources and the potential of human capabilities in all parts of the country and from all sections of the society for building a prosperous nation.
- Co-operative federalism makes it possible to raise all the available resources by the Government at different levels in a co-ordinated way and channel them for use for the common good of the people. This requires a harmonious relationship and co-operative spirit between the Centre and the States and among the States themselves.
- Co-operative federalism is intended to ensure a minimum bundle of basic services and a nationally acceptable level of living for all the people of the country.

Similarly, the benefits of competitive federalism are listed in the points below –

- Competitive federalism follows the concept bottom-up approach as it will bring the change from the states. It ensures inclusive development in the country.
- It instil a spirit of positive competition and help utilisation of successful models of development across many states. Thus, it helps in reducing inter-states and intra-states inequalities through development.
- It ensure that every limb of the whole country is developing. E.g. there are many disparities between various cities in terms of development, competitive sub-federalism reduce such disparities. It help in instilling sense of responsibility in city administrations, ensuring no one have been left out.
- The policy of one-size-fit-all is replaced with different policies of various states based on the own priorities with in the state. Each state will design their own policies for development of the cities with self-fund. The concept also promotes discipline among the states.

Cooperation as well as Competition on a national level is not a small feat to achieve and thus it requires a mutual understanding between the Central and State governments. While prosperous States may be able to execute both policies effectively but economically backward States would require the Centre's support to achieve their goals.

### **Conclusion**

Instituting a system of cooperative and competitive federalism has been a hallmark of India's policy-making in the past five years and has achieved considerable results. Cooperative and competitive federalism are complementary ideas that will drive India's growth story in the coming decades

### 3. Critically evaluate the efficacy of the manner in which powers are distributed between the Union and the States.

#### Approach

Students are expected to write about the distribution of power between union and states. And then critically evaluate the efficacy of the manner in which powers are distributed.

#### Introduction

According to Dicey, power distribution is an essential feature of a federation. The object behind the formation of a federal State involves an authoritative division between the National Government and the Government of the separate States. The federal tendency is restricting every side of the Governmental action, and separation of the strength of the State among parallel and independent authorities is particularly noticeable as it forms a significant distinction between a federal system and unitary system of Government.

#### Body

The Constitution of India provides a dual polity with a clear division of powers between the Union and the States, each being supreme within the sphere allotted to it.

Efficient Manner in which powers are distributed between the union and states:

- Demarcation: The 7th schedule of the Indian Constitution having 3 lists is formulated to ensure the federal character of Indian polity. The division has been helpful in demarcation of subjects and fixing responsibility for lapses in administration.
- International relations and communications: UNO, foreign affairs etc., are subjects in Centre list and hence decisions are taken with uniformity and certainty. E.g. Ex-UN secretary Kofi annan noted Indian foreign policy as stable and credible.
- Holding Accountability: The lists have demarcated the functions and thus help in holding the state/Centre government answerable. E.g. imposition of president rule in UP after Babri masjid incident.
- Uniformity in Administration: subjects like trade and commerce, Banking, regulation of mines, labor etc., ensure uniformity. E.g. uniform interest rate in banks, labour costs etc., ensure that every state is competent in the sphere of economic attraction.
- External security: central government being responsible has been fairly successful in taking timely decisions with necessary force whenever required. E.g. any delays during war time causes set back. Quick decision taken during Kargil was possible only because the defence was entirely with the Centre.

Time and again centre-state relations come under scanner due to increasing centralization of power such as:

- Asymmetric distribution: States complain that Centre has more and important subjects and there is asymmetry in division. Thus, it results in unitary bias. E.g. Raising loans from international market, Banking regulations etc.
- Balance between flexibility and uniformity: Some laws leave little flexibility for states to sync the laws according to their needs for achieving uniformity. A higher degree of detail in law ensures uniformity across the country and provides the same level of protection and rights, however, it reduces the flexibility for states to tailor the law for their different local conditions.
- If a Proclamation of Emergency is in operation: During the operation of the Proclamation of Emergency, the Parliament shall be empowered to legislate for the entire Indian territory or any of its parts with respect to all the matters enumerated in the State List.
- Limited capacity of states: Some laws enacted by Parliament in the concurrent list might require state governments to allocate funds for their implementation. But due to federal supremacy while the states are mandated to comply with these laws they might not have enough financial resources to do so.
- Constitutional practice indicates that use of residuary powers has been at the cost of provincial autonomy, even though the principle of continuing exhaustiveness remains key to the structure of the Seventh Schedule.
- Composition variation: States allege that the union and concurrent list has grown over the years at the cost of state list. A majority government at the Centre helps in this. E.g. 42nd constitutional amendment transferring 5 subjects from state to concurrent list.
- Infringement in the domain of states: Some Bills may directly infringe upon the rights of states i.e. relates to central laws on subjects that are in the domain of state legislatures. E.g. anti-terrorist laws, Lokpal bill, issues with GST and Aadhar etc. where states' power are taken away in a cloaked manner.
- Colorable legislation: The allegations on Centre to encroach upon the state jurisdiction finding the loopholes. E.g. the recent Jammu Kashmir reorganization bill was passed under president rule. The President gave assent to the controversial farm Bills passed by Parliament.

#### Wayforward:

- Strengthening of Inter-State Council: Over the year committees starting from Rajamannar, Sarkaria and Punchi have recommended strengthening of Interstate Council where the concurrent list subjects can be debated and discussed, balancing Centre-State powers.
- Autonomy to states: Centre should form model laws with enough space for states to maneuver. Centre should give enough budgetary support to states so as to avoid budgetary burden. There should be least interference in the state subjects.

#### Conclusion

The Indian constitution aim at reconciling the national unity while giving the power to maintain state to the State governments. It is true that the union has been assigned larger powers than the state governments, but this is a question of degree and not quality, since all the essential features of a federation are present in the Indian constitution. It is often defined to be quasi-federal in nature. Thus, it can be safely said that Indian Constitution is primarily federal in nature even though it has unique features that enable it to assume unitary features upon the time of need. Federal but its spirit is unitary.





**4. What is National Infrastructure Investment Fund (NIIF)? What are its objectives and need? Explain.**

**Approach-** Question is straight forward. Candidate is required to give details of what is NIIF, what are its objectives and its functioning. Critically analysing the need of such funds, more analysis can be given with respect to bad loans and asset restructuring.

**Introduction**

NIIF, (National Investment and Infrastructure Fund), is an Indian-government backed entity established to provide long-term capital to the country's infrastructure sector. It was founded to provide investment for maximizing the economic impact of the commercially available projects (Greenfield Projects and Brownfield Projects).

**Body**

National Investment and Infrastructure Fund (NIIF) was set up as a sovereign wealth fund and is registered with the Securities and Exchange Board of India (SEBI) under SEBI Regulations, 2012 as a Category II Alternate Investment Fund (AIF) with a planned corpus of ₹40,000 crore. It provides long-term capital for infra-related projects.

The Indian government has 49 per cent stake in NIIF with the rest held by marquee foreign and domestic investors such as Abu Dhabi Investment Authority, Temasek and HDFC Group.

What are the objectives of the NIIF?

1. To raise funds through suitable instruments which also included the off-shore credit enhanced bonds.
2. To attract the anchor investors for their participation as partners in NIIF.
3. Servicing of the investors of the fund.
4. To consider and approve the candidate companies, institutions, and projects for investments.
5. To invest in the corpus created by the Asset Management Companies (AMCs) to invest in private equity.
6. To provide advisory service and prepare a shelf of infrastructure projects.

NIIF currently manages three funds each with its distinctive mandate.

The three funds are:

- Master Fund: Is an infrastructure fund with the objective of primarily investing in operating assets in the core infrastructure sectors such as roads, ports, airports, power etc.

- Fund of Funds: Managed by fund managers who have good track records in infrastructure and associated sectors in India. Some of the sectors of focus include Green Infrastructure, Mid-Income & Affordable Housing, Infrastructure services and allied sectors.
- Strategic Investment Fund: Is registered as an Alternative Investment Fund II under SEBI in India. The objective is to invest largely in equity and equity-linked instruments. It will focus on green field and brown field investments in the core infrastructure sectors.

What is the need of NIIF and why it is important?

- There is a clear need for big money to finance the burgeoning infrastructure sector in the country. Large and continuous capital infusions are needed across both old and new infrastructure projects and across the spectrum, in roads, railways, ports, airports and energy.
- Given the sector's long-gestation periods, these projects need long-term patient money. NIIF can play a key role in this. Especially so in the current challenging circumstances when the bad loan problem at many banks.
- Rapid infrastructure development can give a major boost to the country's economic prospects and employment generation. NIIF as a potential major financier can be a game changer.

What is the note of caution?

- NIIF needs to make its investing decisions on an arm's length basis, without pressures from its major backer, the government.
- Investment decisions has to be based solely on commercial objectives in order to deliver sustained long-term financial returns.
- But the NIIF cannot be forced to become a bail-out vehicle, similar to LIC and SBI. Investing in high-potential airports is one thing but putting money in troubled companies is another. NIIF might lose its credibility if it becomes a bailout arm of government.

### **Conclusion**

India with a fast growing demand is in need of infrastructure projects implemented at lightning speed. If demand is not met with supply, we might miss the bus and lose an opportunity. NIIF is right mechanism to fund large projects, with the failure of IL&FS it is now important to use NIIF with pure economic sense.

**5. Should corporate houses be allowed to own banks? Share and substantiate your views.**

**Approach**

Since question is asking you to substantiate so it requires you to substantiate already proven point and not debating between the various points.

**Introduction**

Before we go into discussions about the specific proposal of corporate houses owning banks, it is important to understand that the need is motivated by the desire to have greater competition by allowing for more banks. To put things in perspective, nationalization of banks was done to support India's growth objectives by facilitating credit to priority sectors.

**Body**

**SHOULD CORPORATE HOUSES BE ALLOWED TO OWN BANKS**

Consider this, the single largest shareholder in these public sector banks was not geared towards the objective of making profits. Thus, we ended up with a banking structure where the major banks were willing to lose money and the single largest shareholder was willing to recapitalize the bank. The model led to a situation where political agents started to influence the lending decisions of banks, creating a toxic cocktail of crony-capitalism assisted by the state through its ownership of the banking system.

Thus, what we need to recognize here is that indeed, there is a need for having greater players in the banking sector to ensure adequate savings can be mobilized to finance investments which are needed to create non-farm job opportunities. Therefore, the next logical question is what the ownership structure of the new entrants in India's banking space should be:

**SHOULD WE ALLOW MORE FOREIGN BANKS OR MORE PRIVATE BANKS OWNED BY DOMESTIC ENTITIES OR PERHAPS, MORE GOVERNMENT OWNED BANKS?**

- What we do know is that we do not need more government owned banks; if anything, we need less of them going forward, and the government should consider gradually reducing its ownership in a bulk of the existing public sector banks.
- So, the choice is between foreign banks and a greater number of private banks — and perhaps, both are equally important to develop our financial system.

- The proposal of allowing private corporate houses to set up banks has perhaps been done with the precise intention of allowing for greater space for private ownership of these banks.
- Indeed, many of the existing PSBs will also be privatized at some point and therefore, that is the overall direction of our public policy.
- The issue here pertains to allowing existing businesses houses to set up their banks, as many believe the model is 'risky' and would lead to greater concentration of economic power.
- Moreover, it has been argued that a bank cannot make good loans when it is owned by the borrower.
- It has, thus, been argued that a bank owned by the borrower may undertake poor lending decisions and information on loan performance will not be timely or accurate.
- The fundamental problems associated with lending decisions are the problems of adverse selection and moral hazard. Typically, if we have the borrower as the owner of the bank, there will be greater access to information which should make it better equipped to evaluate the proposal in the first place.
- Moreover, the assumption that a bank will be willing to lend to an unviable project using depositor's money ignores the effect of such decisions on the viability of the bank itself.
- A business group — if it owns a bank — will be geared towards ensuring that the company is viable, and maximizes shareholder wealth by generating a healthy stream of profits.
- While there are concerns of banks funding other entities owned by business-houses, including evergreening of loans — a practice which was mastered by India's public sector undertakings — however, we must realize regulations and mandatory disclosures can mitigate a major part of the risk associated with the same.
- Given that the fundamental challenge in the financial world is of information asymmetry, having private corporate ownership can significantly reduce the problem, paving way for an efficient banking system.
- The added advantage of the motivation for maximizing shareholder wealth and inherent incentive structures within such an ownership framework could also help in achieving several efficiently run banks.
- At the same time, we must recognize the risks associated with such a move and perhaps look at ways to minimize if not mitigate these risks through our regulatory frameworks rather than dismissing the idea altogether at such a premature stage.

### **Conclusion**

On the issue of frauds, more so in the financial system, we must recognise that while building roads may lead to accidents, we do not stop building them as a policy tool to prevent accidents. Similarly, we cannot let our policies be guided by the fears of

them being misused by economic agents — they must be guided by what works best for India’s development objectives and for every policy that is misused, we must proactively put in an adequate regulatory regime to prevent such instances from occurring in future.

Thus, let us not jump the gun and form too strong opinions about an idea that is still at a premature stage — it presents a solution to a challenge faced by the country even as it comes with risks. The debate and our focus should now be on finding ways that would minimise risks rather than trying to utilise our energies solely on junking the idea.

