
TAXING WITHOUT SHARING: THE CONSTITUTIONAL PROBLEM OF CESSES AND SURCHARGES UNDER INDIA'S FEDERAL FRAMEWORK

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ABSTRACT

India's Constitution gives the major taxes to the Union government. These include income tax, corporation tax and customs duty. The States on the other hand are responsible for spending on health, education, roads and agriculture. This creates a well-known problem. The Union earns more than it needs for its own work. The States need to spend more than they can earn from their own taxes. Article 280 of the Constitution deals with this problem. It requires the President to set up a Finance Commission every five years. The Finance Commission decides how much of Union tax money goes to the States. This transfer happens through what is called the divisible pool under Article 270. Cesses and surcharges are treated differently from other Union taxes. Articles 270 and 271 keep them completely outside the divisible pool. Every rupee collected through a cess or a surcharge stays with the Union. It is not shared with the States at all. What started as a small part of Union revenues has grown very large. The combined share of cesses and surcharges peaked at 20.23 percent of gross tax revenue in 2020-21. It came down to 14.09 percent in 2023-24. Total collections that year were Rs. 4,88,316 crores. The Comptroller and Auditor General of India in Report No. 4 of 2020 found that Rs. 2.74 lakh crore was collected through 35 cesses in 2018-19. Out of this only Rs. 1.64 lakh crore went to designated funds. By March 2024 the total amount not transferred to designated reserve funds had grown to Rs. 3,69,307 crores. This was recorded in CAG Report No. 16 of 2025. The Fifteenth Finance Commission Fixed States' share at 41 percent of the divisible pool. But States got only 29 percent of gross tax revenue in 2020-21. By 2024-25 this had barely moved to 32 percent. The Sixteenth Finance Commission in its report for 2026-31 found that cesses and surcharges had reduced the divisible pool from 89.1 percent of gross tax revenue in 2014-15 to a 74-80 percent range during the Fifteenth Finance Commission period. This study looks at Articles 246, 265, 270, 271 and 280 through a doctrinal lens. It uses official fiscal data to support the analysis. It asks whether the steady growth of non-shareable revenues under Articles 270 and 271 has damaged the fiscal federalism framework that Article 280 was designed to protect.

Keywords: Cesses and Surcharges, Divisible Pool, Article 270, Fiscal Federalism, Finance Commission, Basic Structure Doctrine.

1. Introduction

India's Constitution does two things at the same time. It divides governmental powers among different levels of government. It also decides which level can levy taxes and which level must take care of public spending. Article 246 read with the Seventh Schedule gives income tax, corporation tax, customs duty and most other big taxes to the Union.¹ The States are responsible for spending. Education, health, agriculture, roads and welfare services are mostly State subjects. This creates a well-known money gap. The Union collects more than it needs to spend on its own work. The States need to spend more than they can raise from their own sources. Article 280 of the Constitution addresses this gap. It requires the President to form a Finance Commission every five years.² The Finance Commission decides how Union tax money flows to the States. This flow happens through the divisible pool under Article 270. The Fourteenth Finance Commission set States' share of this pool at 42 percent for 2015-20. The Fifteenth Finance Commission fixed it at 41 percent for 2021-26. For most States in India, this transfer from the Union is the biggest single source of funds every year.³ Cesses and surcharges are different from ordinary taxes. Articles 270 and 271 keep them completely outside the divisible pool. Every rupee raised through a cess or surcharge stays with the Union. It is not shared with States at all.⁴ A cess is an extra charge added on top of an existing tax. It is supposed to be used for a specific purpose such as road building or education funding. A surcharge is similar but does not even need a stated purpose. Both have existed since the Constitution was adopted. But their use has grown sharply over the past two decades.⁵ Their combined share in Union gross tax revenue peaked at 20.23 percent in 2020-21. It stood at 14.09 percent in 2023-24 with total collections of Rs. 4,88,316 crore.⁶ Because this money falls outside the divisible pool, States received only 29 percent of gross tax revenue in 2020-21. The Finance Commission had recommended 41 percent. This was documented by PRS Legislative Research.⁷ The CAG audited the year 2018-19. It found that Rs. 2.74 lakh crore was collected through approximately

¹India Const. art. 246 r/w Seventh Schedule, Lists I & II.

²India Const. art. 280.

³PRS Legislative Research, State of State Finances 2021-22, at 15 (2022).

⁴India Const. arts. 270–271.

⁵Ashrita Prasad Kotha et al., Cesses and Surcharges: Concept, Practice and Reform 3 (Vidhi Ctr. for Legal Pol'y 2018).

⁶Comptroller & Auditor Gen. of India, Financial Audit Report No. 16 of 2025 on Union Government Finances 2023-24, § 2.5.1.1 (2025); PRS Legislative Research, State of State Finances 2019-20, at 12 (2020).

⁷PRS Legislative Research, State of State Finances 2021-22, at 15 (2022).

35 cesses. But only Rs. 1.64 lakh crore reached the designated funds. By March 2024 the total shortfall in transfers to designated reserve funds had grown to Rs. 3,69,307 crore. This was recorded in CAG Report No. 16 of 2025.⁸ The Finance Commission is supposed to correct the money gap between the Union and the States. But it can only work with the divisible pool. It has no authority over cesses and surcharges. Between 2020-21 and 2022-23 States received only about 30 percent of gross tax revenue through devolution. The Finance Commission formula had promised 41 percent.⁹ By 2024-25 this figure had moved only to 32 percent.¹⁰ In *S.R. Bommai v. Union of India* a nine-judge bench declared that federalism is part of the basic structure of the Constitution. This means it cannot be changed by any law or government action.¹¹ A nine-judge Constitution Bench reaffirmed this principle in 2024. This paper asks whether the steady growth of non-shareable revenues under Articles 270 and 271 has created a structural distortion of fiscal federalism. It asks whether this damages the purpose of the framework Article 280 was designed to protect.

1.1 Objectives

- To examine whether the exclusion of cesses and surcharges from the divisible pool under Articles 270 and 271 at the current scale is consistent with the principle of fiscal federalism recognised as part of the basic structure of the Constitution.
- To analyse whether the growing use of Articles 270 and 271 to expand non-shareable revenues has created a structural distortion of the devolution framework that defeats the mandate of Article 280.
- To evaluate whether the constitutional framework under Articles 270 and 271 requires reform to address the erosion of the States' share of national tax revenues.

2. Review of Literature

India's fiscal federalism was designed with a built-in money gap from the very beginning. The Constitution gave revenue authority mainly to the Union. Spending responsibilities for welfare,

⁸Comptroller & Auditor Gen. of India, Financial Audit Report No. 4 of 2020 on Union Government Finances 2018-19 (2020); Comptroller & Auditor Gen. of India, Financial Audit Report No. 16 of 2025 on Union Government Finances 2023-24, Executive Summary & para. 3.3.1 (2025).

⁹PRS Legislative Research, State of State Finances November 2024, at 8 (Tushar Chakrabarty & Shruti Singh eds., 2024).

¹⁰PRS Legislative Research, Finances of the Central Government 2024-25, at 6 (2024).

¹¹*S.R. Bommai v. Union of India*, (1994) 3 SCC 1.

roads and social services were given to the States. The Finance Commission was created as the main constitutional tool to manage this gap through regular transfers. Over the years States have become more and more dependent on Union transfers. This happened not because of any policy failure. It happened because of the way the Constitution divided taxing and spending powers. **(Bagchi, 2003)**

Data going back to the 1950s shows that States have raised only about 35 percent of total government revenues. At the same time, they are responsible for over 51 percent of total government expenditure. Many Finance Commissions pointed out this problem. They also noted the growing impact of cesses and surcharges. But none of those recommendations were seriously acted upon. **(Rao, 2000)**

The 101st Constitutional Amendment of 2017 introduced GST and changed Indian fiscal federalism in a very significant way. States gave up their independent power to tax goods and services. In return they were promised five years of revenue compensation. This meant States lost the last big area where they could raise their own revenue independently. At the same time cesses and surcharges outside the divisible pool were growing larger. States were losing their own tax tools exactly when the Union's non-shareable revenues were expanding the most. GST removed States' revenue cushion without fixing the cess problem. The two pressures hit States at the same time. The combined damage was much worse than either pressure would have caused alone. **(Chakraborty, 2019)**

A detailed study documented more than 42 cesses levied by the Union between 1944 and 2019. It found that many cesses collected much more than their stated purpose required. The money was also often not credited to the correct designated funds. Notably this study was commissioned by the Fifteenth Finance Commission itself. This confirms that the cess problem was not a minor academic concern. It was at the centre of the official policy debate on fiscal federalism. The study found that cesses had already exceeded 10 percent of gross tax revenue by 2015-16. It recommended that the Finance Commission include the fiscal impact of cesses and surcharges in its devolution formula. **(Kotha, Agarwal, Sengupta and Singh, 2018)**

The Finance Commission is limited by the Constitution to the divisible pool. This limit is the main reason it cannot fully correct the fiscal gap between the Union and the States. The only way to make the devolution framework work as it was intended is to expand the Commission's constitutional mandate to cover total Union revenues including cesses and surcharges. **(Reddy**

and Reddy, 2019)

Data for 2019-22 shows that State current revenues were only 51 percent of Union net current revenues. State current expenditure was 115 percent of Union current expenditure. GST made this worse by removing States' own indirect tax base. The study concluded that completely reassigning commodity taxation to the States is the only structural solution. This would bring the vertical fiscal imbalance close to zero. It would also remove the Union's justification for maintaining cesses and surcharges. (Srinivasan and Raja Sethu Durai, 2022)

All this literature documents the fiscal damage caused by cesses and surcharges. But none of it examines the constitutional question directly. No study has tested whether the sustained growth of non-shareable revenues under Articles 270 and 271 creates a structural distortion of fiscal federalism. No study has examined whether these conflicts with the basic structure doctrine declared in *S.R. Bommai v. Union of India* and reaffirmed in *Mineral Area Development Authority v. Steel Authority of India* in 2024. This paper takes up that task.

3. Research Methodology

3.1 Statement of Problem

The Constitution gives the Union the stronger revenue powers. The States carry the larger spending burden. The Finance Commission under Article 280 is there to correct this gap through the divisible pool. But Articles 270 and 271 remove cesses and surcharges from the pool entirely. What was once a small exception has grown into a large and permanent share of Union revenues. The Sixteenth Finance Commission found that this growth had reduced the divisible pool from 89.1 percent of gross tax revenue in 2014-15 to a 74-80 percent range during the Fifteenth Finance Commission period. States entitled to 41 percent received only 29 percent in 2020-21 and only 32 percent by 2024-25. The CAG found in 2018-19 that Rs. 1.10 lakh crore collected through cesses was never transferred to designated funds. By March 2024 this total shortfall had grown to Rs. 3,69,307 crores. No court has yet decided whether this pattern crosses the constitutional line.

3.2 Research Question

1. Whether the sustained growth of cesses and surcharges under Articles 270 and 271 at the current scale has created a structural distortion of the federal fiscal framework that is

inconsistent with the constitutional scheme of fiscal federalism.

2. Whether constitutional reform is needed to close the gap between what the Finance Commission recommends and what States actually receive.

3.3 Methodology

This study uses a doctrinal method of constitutional analysis. It is supported by official fiscal data from government sources. The constitutional text, judicial precedent and Constituent Assembly debates form the doctrinal foundation. PRS Legislative Research reports, CAG financial audit reports and Finance Commission reports from the First to the Sixteenth are used as primary government sources. Union Budget documents are also used. Secondary sources include peer-reviewed journal articles, NIPFP working papers and books on Indian public finance. The main cases studied are *S.R. Bommai v. Union of India*, *Kesavananda Bharati v. State of Kerala*, *Mineral Area Development Authority v. Steel Authority of India*, *Hingir Rampur Coal Co. Ltd. v. State of Orissa* and *Union of India v. Mohit Minerals Pvt. Ltd.* No fieldwork, surveys or independent data collection was done. The study relies entirely on published official government sources.

3.4 Limitations

No Indian court has directly decided whether the current scale of cesses and surcharges violates Articles 270 and 280 or the federal structure. Because there is no direct judicial ruling, the conclusions here rest on a doctrinal reading of the constitutional text and case law. The basic structure doctrine as declared in *S.R. Bommai v. Union of India* and reaffirmed in *Mineral Area Development Authority v. Steel Authority of India* is also used. The argument is one of constitutional interpretation. A court may read the provisions differently. The fiscal data from CAG and PRS sources covers periods up to 2024-25. More recent developments may have changed the position. The study does not independently audit how cess money is spent. It relies on the CAG's findings for that purpose.

4. Constitutional Framework of Cesses and Surcharges Under the Indian Federal Structure

4.1 Constitutional Design of Fiscal Federalism

The starting point is *S.R. Bommai v. Union of India*. A nine-judge bench held that federalism is a basic feature of the Constitution. No law or government action can reduce or damage the federal character of the country.¹² States have their own independent standing in the constitutional order. They are not administrative arms of the Union. The divisible pool under Article 270 gives States a constitutional right to a share of Union taxes. This right comes from the same federalism that *S.R. Bommai* placed beyond Parliament's reach. This position was recognised even earlier in *State of West Bengal v. Union of India*. The Supreme Court held that States have their own constitutional status. They are not agents of the Union.¹³ When the Constitution set up the Finance Commission and the divisible pool it was giving States a constitutional entitlement to Union tax revenues. This is not a favour. It is a structural part of Indian federalism that courts must protect. In *Union of India v. Mohit Minerals Pvt. Ltd.*, the Supreme Court reaffirmed that fiscal federalism is an active constitutional principle. Tax powers must be read in a way that protects the genuine fiscal independence of both levels of government.¹⁴ The Constituent Assembly debates of 4 August 1949 show what the framers intended.¹⁵ When Articles 270 and 271 were being debated, cesses were discussed as tools for specific defined purposes. Surcharges were treated as exceptional instruments for particular Union needs. The debates show that the divisible pool was meant to be the primary and normal channel for fiscal transfers. Cesses and surcharges were meant to be small and limited departures from that norm. What the data now shows is that these small departures have grown so large that they are working against the primary channel the framers designed. Before looking at the specific provisions it is important to understand vertical fiscal imbalance. This is the gap that arises when one level of government collects more than it needs while another level must spend more than it can raise. India's Constitution creates this imbalance by design. The Union holds the major revenue powers. The States carry the larger spending burden in health, education and infrastructure.¹⁶ The Finance Commission is the constitutional tool to correct this gap each year through the divisible pool. When cesses and surcharges take a growing share of Union revenues out of that pool the Finance Commission works on a smaller and smaller base. The gap between what States collect and what they need to spend keeps growing even when the Finance Commission percentage stays the same on paper.

¹²*S.R. Bommai v. Union of India*, (1994) 3 SCC 1, ¶ 237 (Ahmadi, J.) (India).

¹³*State of W. Bengal v. Union of India*, AIR 1963 SC 1241 (India).

¹⁴*Union of India v. Mohit Minerals Pvt. Ltd.*, (2022) 9 SCC 507 (India).

¹⁵Constituent Assembly of India, Constituent Assembly Debates, vol. IX (Aug. 4, 1949) (India).

¹⁶INDIA CONST. art. 280; INDIA CONST. Seventh Schedule, Lists II & III.

Article 270(1) says that all Union List taxes shall be distributed between the Union and the States except surcharges under Article 271 and any cess levied for specific purposes under any law of Parliament.¹⁷ The phrase 'levied for specific purposes' is the constitutional condition that defines a cess. The design of the provision suggests this condition was meant to keep cesses tied to their stated purpose. In *Hingir Rampur Coal Co. v. State of Orissa* the Supreme Court held that a levy tied to a specific purpose must actually be applied to that purpose. The link must be real and not just on paper.¹⁸ Although *Hingir Rampur* arose in a different context its principle applies here because Article 270(1) itself uses 'specific purposes' as the constitutional basis for keeping a cess outside the divisible pool. If a cess does not serve its stated purpose the justification for excluding it from the pool is weakened. In *Kedar Nath Bajoria v. State of West Bengal* the court held that both the power to impose a levy and what the money is actually spent on are legally relevant when testing whether the levy is valid.¹⁹ The CAG found in 2018-19 that Rs. 1.10 lakh crore out of Rs. 2.74 lakh crore collected through 35 cesses was not transferred to designated funds. By March 2024 this total shortfall had grown to Rs. 3,69,307 crore. In 2023-24 alone Rs. 3,79,598 crore was collected as cess charges equal to 10.95 percent of Union gross tax revenue.²⁰ Article 265 says no tax can be collected without authority of law.²¹ Article 271 allows Parliament to add a surcharge on any Union tax with full proceeds going to the Union.²² But the Constitution permitting this does not mean it approves of expanding it without any limit. In 2024 the Supreme Court returned to fiscal federalism in *Mineral Area Development Authority v. Steel Authority of India*. A nine-judge bench held at Para 48 that federalism is a basic feature of the Constitution. At Para 49 the court said every unit in a federal system must be able to carry out its core functions with genuine independence. The Constitution must be read in a way that does not damage its federal character. State legislatures must not be made subordinate to the Union in areas the Constitution has reserved for them.²³ This judgment was delivered in July 2024 when the cess problem had already reached the scale this paper documents. It adds strong judicial weight to the argument that a

¹⁷INDIA CONST. art. 270, § 1 (as amended by The Constitution (Eightieth Amendment) Act, No. 44 of 2000 (India)).

¹⁸*Hingir Rampur Coal Co. v. State of Orissa*, AIR 1961 SC 459 (India).

¹⁹*Kedar Nath Bajoria v. State of W. Bengal*, AIR 1953 SC 404 (India).

²⁰Comptroller & Auditor General of India, Financial Audit Report No. 4 of 2020 on Union Government Finances 2018-19 (2020); Comptroller & Auditor General of India, Financial Audit Report No. 16 of 2025 on Union Government Finances 2023-24, para. 3.3.1 (2025).

²¹INDIA CONST. art. 265.

²²INDIA CONST. art. 271.

²³*Mineral Area Dev. Auth. v. Steel Auth. of India*, Supreme Court of India, 9-Judge Constitution Bench, paras. 48–49 (July 25, 2024) (India).

practice which steadily reduces States' fiscal resources must be tested against the constitutional protection of federalism. Article 280 requires the Finance Commission to recommend how Union tax revenues are shared with the States.²⁴ PRS Legislative Research has shown that States received only 29 percent of gross tax revenue in 2020-21 and only 32 percent in 2024-25. The Finance Commission had recommended 41 percent.²⁵ Devolution stayed at about 30 percent between 2020-21 and 2022-23.²⁶ States plan their budgets based on the Finance Commission figure. But the actual transfer turns out to be far less. This is the gap between what the Constitution promised and what it actually delivers.

4.2 Doctrinal Analysis and Federalism Implications

To assess whether the current practice crosses the constitutional line we need to look at it at three levels. At the first level the practice is formally within Articles 270 and 271. Parliament has the power to impose cesses and surcharges. The Constitution expressly keeps them outside the divisible pool. A challenge based on lack of legislative power will not succeed. At the second level the practice must be tested against the purpose the devolution framework was built to serve. When the Union keeps increasing revenues raised through instruments excluded from sharing the Finance Commission gets less and less to distribute. This happens without any formal amendment to the Constitution. The result being produced through ordinary legislation is exactly the kind of result that Article 368 was supposed to govern.²⁸ At the third level the basic structure doctrine becomes relevant. We must honestly acknowledge that Indian courts have mainly applied this doctrine to constitutional amendments. Courts may be unwilling to extend it to ordinary fiscal legislation even where the cumulative harm is serious. This paper does not claim the answer is settled. What it argues is that the question deserves a judicial answer. Both *S.R. Bommai v. Union of India* and *Mineral Area Development Authority v. Steel Authority of India* make clear that any practice which progressively subordinates States to the Union must be open to constitutional challenge. Parliament's power under Articles 270 and 271 is not in dispute. The constitutional concern arises at a different point. Having a power is not the same as using it within proper constitutional limits. In *Kesavananda Bharati v. State of*

²⁴INDIA CONST. art. 280.

²⁵PRS Legislative Research, State of State Finances 2021-22, at 15 (2022); PRS Legislative Research, Finances of the Central Government 2024-25, at 6 (2024).

²⁶PRS Legislative Research, State of State Finances November 2024, at 8 (Tushar Chakrabarty & Shruti Singh eds., 2024).

²⁷PRS Legislative Research, State of State Finances 2021-22, at 15 (2022).

²⁸*S.R. Bommai v. Union of India*, (1994) 3 SCC 1 (India); INDIA CONST. art. 368.

Kerala the Supreme Court held that no constitutional power can be used in a way that destroys or seriously damages the constitutional framework.²⁹ When Parliament uses Articles 270 and 271 not as small exceptions but as a regular tool for building a growing non-shareable revenue base it creates a structural distortion of the federal fiscal framework. Article 280 was made to ensure revenue sharing between the Union and States is genuinely meaningful. Article 270 created the divisible pool for that purpose. When the continued use of Articles 270 and 271 shrinks the divisible pool from 89.1 percent of gross tax revenue to a 74-80 percent range over a decade what Article 280 can actually deliver changes significantly without the Constitution being formally amended.

The Union's Constitutional Defence

It is fair to consider the strongest arguments on the Union's side. Articles 270 and 271 were written this way on the first day of the Constitution. Parliament has exercised these powers deliberately. The Union can argue that the Constitution sets no upper limit on how much can be raised through these instruments. It can argue that earmarked levies serve real national purposes that general devolution cannot ensure. The Health and Education Cess funded the Pradhan Mantri Swasthya Suraksha Yojana for government hospitals and the Samagra Shiksha Abhiyan for school education. The 101st Constitutional Amendment in 2017 also abolished several pre-GST cesses showing Parliament is willing to wind up these instruments when they are no longer needed.³⁰ These are genuine points. But they do not resolve the constitutional problem. A power is not unlimited just because the Constitution does not expressly set a ceiling. The *Kesavananda Bharati* principle says no constitutional power can damage the constitutional structure it belongs to. The Union's strongest argument is that cess money goes to national programmes. But the CAG found in 2018-19 that Rs. 1.10 lakh crore collected through cesses was not transferred to designated funds.³¹ By March 2024 this shortfall had grown to Rs. 3,69,307 crores.³² When the factual premise fails the constitutional justification also weakens. There is also a structural reason. The Finance Commission has no authority over cess revenues. States have no constitutional right to any portion of them. When cess money comes back to

²⁹*Kesavananda Bharati v. State of Kerala*, (1973) 4 SCC 225 (India).

³⁰The Constitution (One Hundred and First Amendment) Act, No. 101 of 2016 (India); *Union of India v. Mohit Minerals Pvt. Ltd.*, (2022) 9 SCC 507 (India).

³¹Comptroller & Auditor General of India, Financial Audit Report No. 4 of 2020 on Union Government Finances 2018-19 (2020).

³²Comptroller & Auditor General of India, Financial Audit Report No. 16 of 2025 on Union Government Finances 2023-24, para. 3.3.1 (2025).

States through centrally sponsored schemes it does so at the Union's discretion. A constitutional right cannot be replaced by an administrative arrangement that Parliament can reduce or withdraw at any time. The Sixteenth Finance Commission's report for 2026-31 gives the most authoritative recognition of this problem. The Commission found that cesses and surcharges had reduced the divisible pool from 89.1 percent of gross tax revenue in 2014-15 to only 74 to 80 percent during the Fifteenth Finance Commission period. Para 7.67 of the report says no further reduction in States' share is sustainable. It proposed a grand bargain. The Union would fold cess and surcharge revenues into regular taxes. States would accept a smaller share of the resulting larger pool. Neither side would lose revenue. The Commission kept States' share at 41 percent for 2026-31 but left the structural problem unresolved. The fact that the constitutional body created to correct fiscal asymmetry has called the solution a grand bargain confirms that this is a recognised institutional failure.³³ Three reform paths exist. First an amendment to Article 270 could fix a ceiling on cess and surcharge revenues. Second another amendment could require cess collections to return to the divisible pool once their stated purpose is served. Third Article 280 could be amended so the Finance Commission calculates its recommendations on total Union revenues. No court has yet held that the current scale of cess retention creates a structural distortion. Article 131 gives the Supreme Court original jurisdiction over disputes between the Union and a State.³⁴ Any affected State can use this to place the question before the court.

5. Findings

The constitutional design of Articles 270 and 271 suggests they were meant to allow purpose-specific levies for defined national needs. They were not meant to give the Union a permanent right to retain a growing share of national tax revenues outside the sharing framework. The phrase 'specific purposes' in Article 270(1) is a constitutional condition. It ties the validity of a cess to its stated purpose. This is a constitutional requirement and not merely a policy choice. The numbers show how far the practice has gone. Cess and surcharge collections peaked at 20.23 percent of gross tax revenue in 2020-21. They stood at 14.09 percent in 2023-24 with total collections of Rs. 4,88,316 crore. The Sixteenth Finance Commission found that cesses and surcharges had reduced the divisible pool from 89.1 percent of gross tax revenue in 2014-15 to a 74-80 percent range during the Fifteenth Finance Commission period. States were

³³Sixteenth Finance Commission, Report for 2026-31, vol. I, para. 7.67 (Gov't of India 2026).

³⁴INDIA CONST. art. 131.

entitled to 41 percent under the Fifteenth Finance Commission formula. But they received only 29 percent of gross tax revenue in 2020-21 and only 32 percent by 2024-25.³⁵ This is well beyond what the constitutional design of Articles 270 and 271 was meant to allow. The mandate of the Finance Commission under Article 280 is also being weakened without any formal constitutional amendment. Tax devolution stayed at about 30 percent of gross tax revenue between 2020-21 and 2022-23 against the recommended 41 percent.³⁶ What Article 368 was designed to govern is being done through ordinary legislation. The CAG found in 2018-19 that Rs. 1.10 lakh crore collected through cesses was never transferred to designated funds. By March 2024 this total shortfall had grown to Rs. 3,69,307 crores as documented in CAG Report No. 16 of 2025.³⁷ Under the Kesavananda Bharati principle no constitutional power can be used in a way that materially damages another constitutional provision. The continued use of Articles 270 and 271 to shrink the divisible pool that Article 280 was designed to protect is exactly that kind of structural distortion. Under the principle in *Hingir Rampur Coal Co. v. State of Orissa* a cess that does not reach its designated purpose loses the constitutional justification for being kept outside the divisible pool. The nine-judge bench in *Mineral Area Development Authority v. Steel Authority of India* confirmed in 2024 that the Constitution must be read to prevent State legislatures from being subordinated to the Union in areas reserved for them. Without a court ruling or a legislative fix this erosion will continue unchecked.

6. Conclusion and Suggestions

India's Constitution gave the major revenue-raising powers to the Union. It gave the larger public spending duties to the States. Two constitutional instruments were created to manage this gap. These are the Finance Commission under Article 280 and the divisible pool under Article 270. In *S.R. Bommai v. Union of India* a nine-judge bench made federalism a basic feature of the Constitution. A nine-judge bench in *Mineral Area Development Authority v. Steel Authority of India* reaffirmed in 2024 that States must retain genuine independence in performing their constitutionally assigned functions.³⁸ These rulings mean that the revenue sharing arrangement under Articles 270 and 280 is not just a fiscal policy preference. It carries

³⁵ PRS Legislative Research, *State of State Finances 2021-22*, at 15 (2022); PRS Legislative Research, *Finances of the Central Government 2024-25*, at 6 (2024).

³⁶ PRS Legislative Research, *State of State Finances November 2024*, at 8 (Chakrabarty & Singh eds., 2024).

³⁷ CAG, *Financial Audit Report No. 16 of 2025 on Union Government Finances 2023-24*, para. 3.3.1 (2025).

³⁸ *S.R. Bommai v. Union of India*, (1994) 3 SCC 1; *Mineral Area Dev. Auth. v. Steel Auth. of India*, 9-Judge Constitution Bench, decided July 25, 2024, para. 49.

constitutional protection. This study has shown that this protection is being eroded in practice. Cess and surcharge collections stood at 20.23 percent of gross tax revenue in 2020-21 and 14.09 percent in 2023-24. States received only 29 percent of gross tax revenue in 2020-21 and 32 percent in 2024-25. Their constitutional entitlement was 41 percent.³⁹ The Sixteenth Finance Commission found that cesses and surcharges had reduced the divisible pool from 89.1 percent of gross tax revenue in 2014-15 to a 74-80 percent range during the Fifteenth Finance Commission period. It proposed a grand bargain as the only real solution. It is accepted that Parliament placed cesses and surcharges outside the pool deliberately. Programs like the Pradhan Mantri Swasthya Suraksha Yojana and the Samagra Shiksha Abhiyan (Comprehensive Education Campaign) do indeed serve national purposes. However, the total shortfall in cess transfers set aside funds by March 2024 reached ₹369,307 crore. Based on these facts, the argument that these schemes ultimately benefit the states is unjustified. The practice formally complies with Articles 270 and 271 but the Kesavananda Bharati principle makes clear that formal compliance does not protect the exercise of a constitutional power from scrutiny when it damages another constitutional provision. According to the basic structure doctrine, the structural distortion of the devolution framework poses a legitimate concern. Judicial intervention is the only way to provide a decisive response.

6.1 Suggestions

Parliament should amend Article 270 to fix a ceiling on how much of gross tax revenue can be raised through cesses and surcharges. A cap of 10 percent is a reasonable starting point. The Vidhi Centre study submitted to the Fifteenth Finance Commission found that cesses crossing 10 percent of gross tax revenue causes serious fiscal damage to States.⁴⁰ A further amendment to Article 280 should require the Finance Commission to base its recommendations on total Union revenues including cesses and surcharges. This would ensure States receive their actual share of national tax collections. The Sixteenth Finance Commission's grand bargain proposal should be implemented as a constitutional commitment. If Parliament folds cess and surcharge revenues into the regular divisible tax base with a corresponding reduction in the devolution percentage, neither side loses revenue and the structural distortion is corrected.⁴¹ As an

³⁹PRS Legislative Research, State of State Finances 2019-20, at 12 (2020); PRS Legislative Research, State of State Finances 2021-22, at 15 (2022); PRS Legislative Research, Finances of the Central Government 2024-25, at 6 (2024).

⁴⁰INDIA CONST. art. 368; Ashrita Prasad Kotha, Vinti Agarwal, Arghya Sengupta & Rav P. Singh, *Cesses and Surcharges: Concept, Practice and Reform*, at 18 (Vidhi Ctr. for Legal Pol'y 2018).

⁴¹ Sixteenth Finance Commission, *Report for 2026-31*, vol. I, para. 7.67 (Gov't of India 2026).

immediate step Parliament should attach a mandatory sunset clause to every cess law. Each cess should expire after five years unless renewed with a fresh purpose statement and an independent audit of prior collections. The GST Compensation Cess provides a ready domestic precedent for this approach.

Finally, the terms of reference of each Finance Commission should require a dedicated report on the fiscal impact of cesses and surcharges on States' effective share of gross tax revenue. This would create a regular public record before any legislative or constitutional action is taken.⁴²

⁴² INDIA CONST. arts. 270–271, 280; The Goods and Services Tax (Compensation to States) Act, No. 15 of 2017 (India).

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