

Report Summary

Report of the 16th Finance Commission for 2026-31

The Finance Commission (FC) is a Constitutional body constituted by the President every five years to make recommendations on centre-state fiscal relations. The Report of the 16th Finance Commission (Chair: Dr. Arvind Panagariya) was tabled in Parliament on February 1, 2026 for the five-year period between 2026-27 and 2030-31. Key recommendations of the Commission include:

Share of states in central taxes

The share of states in the divisible pool of central taxes has been recommended at 41%. This is same as the share recommended by the 15th Finance Commission. Divisible pool is arrived at after excluding cost of collection and cesses and surcharges from the gross tax revenue collected by the central government.

Criteria for devolution

To provide for the distribution of central taxes among states, Finance Commissions define a formula with weightage for certain parameters. Table 1 below shows the criteria used by the 16th Finance Commission to determine each state's share in central taxes and the weights assigned to them. Table 3 in annexure shows the individual share of states.

Table 1: Criteria for distribution of central taxes among states

| Criteria | 15 th FC (2021-26) | 16 th FC (2026-31) |
|-------------------------|----------------------------------|----------------------------------|
| Income Distance | 45% | 42.5% |
| Population (2011) | 15% | 17.5% |
| Demographic Performance | 12.5% | 10% |
| Area | 15% | 10% |
| Forest | 10% | 10% |
| Tax and Fiscal Efforts | 2.5% | - |
| Contribution to GDP | - | 10% |
| Total | 100% | 100% |

Sources: Reports of the 15th and 16th Finance Commissions; PRS.

Per Capita GSDP Distance (Income Distance): The 16th FC has defined income distance as the difference between the per capita GSDP of a state and the average of the per capita GSDP of the top three large states with the highest per capita GSDP. Per capita GSDP has been computed as the average over the period 2018-19 and 2023-24, excluding the pandemic year of 2020-21. States with a lower per capita GSDP will receive a higher share on this parameter, to maintain equity among states.

Population: On this parameter, the share in devolution is determined based on the share in the population as per the 2011 Census.

Demographic Performance: The 15th FC had introduced this parameter to award states for controlling population on the basis of Total Fertility Rate (TFR). The 16th FC has redefined this to account for population growth between 1971 and 2011 instead of relying on change in TFR. States with lower population growth will have a higher share under this parameter.

Forest: The 16th FC has assigned weightage to both the share of a state in the overall forest area, and its share in the increase in overall forest area between 2015 and 2023. Further, it has also considered open forests in arriving at the total forest area. In contrast, the 15th FC had considered only dense and moderately dense forests, and defined the parameter only in terms of share in the overall forest area.

Contribution to GDP: The 16th FC has introduced this parameter to account for the contribution to national GDP. This replaces the tax and fiscal efforts parameter used by the 15th FC which rewarded states with a higher tax collection efficiency. Contribution to GDP by a state is calculated as the squared root of its GSDP to the sum of squared root of GSDP of all states. GSDP of each state has been measured as the average nominal GSDP between 2018-19 and 2023-24 (excluding the pandemic year of 2020-21).

Grants-in-aid

The 16th FC has recommended grants worth Rs 9.47 lakh crore over the five-year period. These comprise grants for: (i) urban and rural local bodies, and (ii) disaster management. The 16th FC has discontinued the following grants recommended by the 15th FC: (i) revenue deficit grants, (ii) sector-specific grants, and (iii) state-specific grants. See Table 5 in annexure for state-wise details.

Table 2: Grants-in-aid for 2026-31 (in Rs crore)

| Grants | Amount |
|----------------------------------|-----------------|
| Local governments | 7,91,493 |
| Rural local bodies | 4,35,236 |
| Basic Grant | 3,48,188 |
| Performance Grant | 87,048 |
| Urban local bodies | 3,56,257 |
| Basic Grant | 2,32,125 |
| Performance Grant | 58,032 |
| Special Infrastructure Component | 56,100 |
| Urbanisation Premium | 10,000 |
| Disaster management | 1,55,916 |
| Total | 9,47,409 |

Source: Report of the 16th Finance Commission; PRS.

Grants for local bodies: The 16th FC has recommended grants worth Rs 4.4 lakh crore and Rs 3.6 lakh crore for rural and urban local bodies, respectively. These grants are divided into basic (80%) and performance-based (20%) components. Special Infrastructure Grants and Urbanisation Premium Grants have also been recommended for urban local bodies. These are discussed in further detail below.

All local body grants will be made available upon fulfilment of three entry-level criteria: (i) constitution of the local bodies as per the Constitution, (ii) publication of provisional and audited accounts of the local bodies in the public domain, and (iii) timely constitution of the State Finance Commission.

Basic grants: 50% of the basic grant will be untied and the rest 50% will be tied to: (i) sanitation and solid waste management, and/or (ii) water management.

Performance grants: These grants for local bodies are further divided into state performance grants and local body performance grants. State performance grants will be made available upon meeting a minimum benchmark for transfers to local bodies from their own resources. Local body performance grants are linked to achievement of minimum targets specified by the Commission for own source revenue growth.

Special infrastructure grants: This component will be tied to the development of a comprehensive wastewater management system in cities with population between 10-40 lakh as per the 2011 census (see Table 4 in annexure for list of eligible cities). Grants worth Rs 56,100 crore have been recommended over five years.

Urbanisation premium grant: These will be released to states as a one-time grant for: (i) merger of peri-urban villages into adjoining urban local body areas and (ii) formulation of a Rural to Urban Transition Policy. Rs 10,000 crore have been recommended under the urbanisation premium component.

Disaster management grants: The Commission has recommended disaster management corpus of Rs 2,04,401 crore for State Disaster Relief and Management Funds (SDRF and SDMF). The cost-sharing pattern between the centre and states is recommended to be: (i) 90:10 for north-eastern and Himalayan states, and (ii) 75:25 for all other states. Centre's share in total will be Rs 1,55,916 crore.

Fiscal Roadmap

The Commission has recommended that the Centre should bring down fiscal deficit to 3.5% of GDP by 2030-

31. It recommended the annual fiscal deficit limit for states to be 3% of GSDP. It also recommended strictly discontinuing the practice of off-budget borrowings for states and bringing all such borrowings onto their budgets. The definition of fiscal deficit and debt should be expanded to uniformly include all off-budget borrowings.

The Commission has projected the combined debt of the central and state governments to decline from 77.3% in 2026-27 to 73.1% of the GDP in 2030-31.

Power-sector reforms

The Commission recommended that states should actively pursue privatisation of electricity distribution companies (DISCOMs). To shield the private investor from debt burden after discom takeover, a special purpose vehicle may be created to warehouse the debt. Pre-payment or eventual repayment of this debt may be allowed using the funds from the Special Assistance Scheme for Capital Investment. It also recommended that states should be allowed to utilise this assistance only after the privatisation process is complete.

Subsidy Expenditure

The Commission recommended states to review and rationalise their subsidy expenditure. It noted that schemes providing unconditional cash transfers tend to have large and untargeted beneficiaries. It recommended setting clear exclusion criteria and a rigorous review process to ensure effective targeting. In addition, it recommended discontinuing financing of subsidies through off budget borrowings.

The Commission also noted a lack of standardisation in defining and accounting of subsidies and transfers across states. It observed that subsidies and transfers across states are being misclassified as assistance, grants, or other expenditure. It recommended adoption of a uniform approach for accounting and disclosure of subsidies and transfers.

Public Sector Enterprise Reforms

The Commission recommended a review and closure of 308 inactive State Public Sector Enterprises (SPSEs). It recommended formulation of a state-level PSEs disinvestment policy to target inactive and underperforming SPSEs.

State or union PSEs, which incur losses for three out of four consecutive years, should be placed for the respective Cabinet's consideration. The Cabinet may decide closure, privatisation, or continuation depending on the strategic importance of the enterprise.

Annexure

Table 3: Individual share of states in the taxes devolved by the centre (out of 100)

| State | 14 th FC (2015-2020) | 15 th FC (2021-26) | 16 th FC (2026-31) |
|-------------------|------------------------------------|----------------------------------|----------------------------------|
| Andhra Pradesh | 4.31 | 4.05 | 4.22 |
| Arunachal Pradesh | 1.37 | 1.76 | 1.35 |
| Assam | 3.31 | 3.13 | 3.26 |
| Bihar | 9.67 | 10.06 | 9.95 |
| Chhattisgarh | 3.08 | 3.41 | 3.30 |
| Goa | 0.38 | 0.39 | 0.37 |
| Gujarat | 3.08 | 3.48 | 3.76 |
| Haryana | 1.08 | 1.09 | 1.36 |
| Himachal Pradesh | 0.71 | 0.83 | 0.91 |
| Jammu and Kashmir | 1.85 | - | - |
| Jharkhand | 3.14 | 3.31 | 3.36 |
| Karnataka | 4.71 | 3.65 | 4.13 |
| Kerala | 2.5 | 1.93 | 2.38 |
| Madhya Pradesh | 7.55 | 7.85 | 7.35 |
| Maharashtra | 5.52 | 6.32 | 6.44 |
| Manipur | 0.62 | 0.72 | 0.63 |
| Meghalaya | 0.64 | 0.77 | 0.63 |
| Mizoram | 0.46 | 0.5 | 0.56 |
| Nagaland | 0.5 | 0.57 | 0.48 |
| Odisha | 4.64 | 4.53 | 4.42 |
| Punjab | 1.58 | 1.81 | 2.00 |
| Rajasthan | 5.5 | 6.03 | 5.93 |
| Sikkim | 0.37 | 0.39 | 0.34 |
| Tamil Nadu | 4.02 | 4.08 | 4.10 |
| Telangana | 2.44 | 2.1 | 2.17 |
| Tripura | 0.64 | 0.71 | 0.64 |
| Uttar Pradesh | 17.96 | 17.94 | 17.62 |
| Uttarakhand | 1.05 | 1.12 | 1.14 |
| West Bengal | 7.32 | 7.52 | 7.22 |

Sources: Reports of the 14th, 15th, and 16th Finance Commission Reports; PRS.

Table 4: Eligible cities under the Special Infrastructure Component of ULB grants

| City | State |
|----------------|----------------|
| Pune | Maharashtra |
| Jaipur | Rajasthan |
| Lucknow | Uttar Pradesh |
| Kanpur | Uttar Pradesh |
| Nagpur | Maharashtra |
| Indore | Madhya Pradesh |
| Bhopal | Madhya Pradesh |
| Vishakhapatnam | Andhra Pradesh |
| Patna | Bihar |
| Vadodara | Gujarat |
| Ludhiana | Punjab |
| Faridabad | Haryana |
| Rajkot | Gujarat |
| Dhanbad | Jharkhand |
| Amritsar | Punjab |
| Howrah | West Bengal |
| Ranchi | Jharkhand |
| Coimbatore | Tamil Nadu |
| Vijayawada | Andhra Pradesh |
| Jodhpur | Rajasthan |
| Madurai | Tamil Nadu |
| Raipur | Chhattisgarh |

Source: Report of the 16th Finance Commission; PRS.

Table 5: State-wise details of grants-in-aid for 2026-31 (in Rs crore)

| State | Rural Local Body Grants | | | Urban Local Body Grants | | | Disaster Management Grants |
|-------------------|-------------------------|-----------------|-------------------|-------------------------|-----------------|-------------------|----------------------------|
| | Basic | RLB Performance | State Performance | Basic | ULB Performance | State Performance | |
| Andhra Pradesh | 13,302 | 1,663 | 1,663 | 9,727 | 1,216 | 1,216 | 6,125 |
| Arunachal Pradesh | 1,358 | 170 | 170 | 186 | 24 | 24 | 616 |
| Assam | 11,663 | 1,459 | 1,459 | 2,598 | 326 | 326 | 5,243 |
| Bihar | 41,539 | 5,192 | 5,192 | 7,335 | 917 | 917 | 13,615 |
| Chhattisgarh | 9,331 | 1,167 | 1,167 | 3,992 | 499 | 499 | 2,481 |
| Goa | 140 | 17 | 17 | 581 | 73 | 73 | 112 |
| Gujarat | 15,042 | 1,880 | 1,880 | 19,011 | 2,377 | 2,377 | 8,459 |
| Haryana | 6,616 | 827 | 827 | 6,267 | 784 | 784 | 2,922 |
| Himachal Pradesh | 2,996 | 374 | 374 | 348 | 44 | 44 | 2,682 |
| Jharkhand | 11,385 | 1,423 | 1,423 | 4,874 | 610 | 610 | 2,806 |
| Karnataka | 15,111 | 1,889 | 1,889 | 14,786 | 1,849 | 1,849 | 6,419 |
| Kerala | 2,647 | 331 | 331 | 13,347 | 1,668 | 1,668 | 1,935 |
| Madhya Pradesh | 25,627 | 3,203 | 3,203 | 12,813 | 1,602 | 1,602 | 11,697 |
| Maharashtra | 26,254 | 3,282 | 3,282 | 37,442 | 4,681 | 4,681 | 29,619 |
| Manipur | 1,009 | 127 | 127 | 487 | 61 | 61 | 259 |
| Meghalaya | 1,183 | 148 | 148 | 302 | 38 | 38 | 437 |
| Mizoram | 453 | 57 | 57 | 302 | 38 | 38 | 284 |
| Nagaland | 557 | 70 | 70 | 534 | 67 | 67 | 408 |
| Odisha | 14,973 | 1,871 | 1,871 | 4,062 | 508 | 508 | 8,900 |
| Punjab | 6,789 | 849 | 849 | 6,267 | 784 | 784 | 2,477 |
| Rajasthan | 25,173 | 3,147 | 3,147 | 10,145 | 1,268 | 1,268 | 9,211 |
| Sikkim | 174 | 22 | 22 | 162 | 21 | 21 | 455 |
| Tamil Nadu | 13,544 | 1,693 | 1,693 | 20,054 | 2,508 | 2,508 | 8,486 |
| Telangana | 7,974 | 997 | 997 | 9,239 | 1,155 | 1,155 | 2,774 |
| Tripura | 941 | 118 | 118 | 813 | 102 | 102 | 356 |
| Uttar Pradesh | 66,608 | 8,327 | 8,327 | 26,835 | 3,354 | 3,354 | 15,321 |
| Uttarakhand | 3,237 | 405 | 405 | 1,997 | 250 | 250 | 4,954 |
| West Bengal | 22,562 | 2,821 | 2,821 | 17,619 | 2,202 | 2,202 | 6,869 |
| Total | 3,48,188 | 43,524 | 43,524 | 2,32,125 | 29,016 | 29,016 | 1,55,916 |

Source: Report of the 16th Finance Commission; PRS.

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