

Cooperative and Competitive Federalism – Explained Pointwise

The States in India are no longer looking only at the Centre for supporting them, but are also competing with each other for attracting investors & pitching their case with confidence & data. Thus, the federalism in India is believed to be moving towards maturity.

Federalism in India operates on two key principles: **cooperative federalism** and **competitive federalism**, both of which influence governance, economic growth, and fiscal discipline. However, the **growing trend of freebies-based competitive federalism** has raised concerns about sustainability, fiscal responsibility, and the long-term economic impact.

While competitive federalism fosters economic efficiency and innovation, an unchecked race to provide freebies threatens financial stability. This article explores the dynamics of cooperative and competitive federalism & their impact on governance, and their challenges.

COOPERATIVE & COMPETITIVE FEDERALISM



Source- Big Buzz

What is the concept of Competitive and Cooperative Federalism?

Cooperative Federalism

Cooperative federalism emphasizes **collaboration between the Union and state governments**. Both levels of government share responsibilities and work together for the larger public interest. It ensures coordination and alignment of policies across the Centre and states. **Examples include:**

1. **Goods and Services Tax (GST) Council**, where the Centre and states jointly decide tax rates and structures.
2. **Ayushman Bharat and PM-KISAN**, which require Centre-state collaboration for effective implementation.
3. **Zonal Councils**, established by the **States Reorganization Act, 1956**, to resolve inter-state disputes.

Competitive Federalism

Competitive federalism fosters **horizontal competition among states** and **vertical competition between the Centre and states** to attract investment, enhance governance, and improve public services. The **NITI Aayog** promotes competition through rankings in ease of doing business, education, and health. **Examples include:**

1. **Gujarat and Maharashtra's economic rivalry** in the 2000s, offering tax breaks and subsidies to attract manufacturers.
2. **State-specific welfare schemes**, such as **Telangana's Rythu Bandhu** and **Odisha's KALIA**, complementing central schemes like **PM-KISAN**.
3. **Vibrant Gujarat Summit**, attracting global investments.

Constitutional provisions supporting Cooperative & Competitive Federalism

1. **Seventh schedule:** It classifies legislative subjects into the **Union List, State List, and Concurrent List**, ensuring a balance of power and cooperation between different levels of government.
 2. **Article 261 (Full Faith and Credit Clause):** Mandates that public acts, records, and judicial proceedings of one state be recognized and upheld across all states, promoting legal uniformity.
 3. **Article 263 (Inter-State Council – ISC):** Provides for the establishment of the Inter-State Council (ISC) to investigate and discuss subjects of common interest among states and the Union, fostering cooperation.
 4. **All India Services (Article 312):** Provides for centrally-recruited officers serving in both the Centre and states, ensuring administrative cooperation.
 5. **Goods and Services Tax (GST) (Article 279A):** Establishes the GST Council, where states negotiate and compete over taxation policies, striving for a favorable business environment.
- NITI Aayog (Executive Initiative, Replacing Planning Commission):** Encourages a competitive approach through performance-based rankings, incentives, and best governance practices among states.

What is the present status of freebies Competitive Federalism?

1. **Shift from Cooperative to Competitive Freebies-** Instead of competing on efficiency and governance, **states now engage in populist policies** that include **reckless subsidies** and **fiscal imprudence**. This has turned competitive federalism into a fiscal bidding war, where states offer increasingly larger cash transfers and free services to gain political mileage.

Examples include: Monthly cash transfers to women announced by Karnataka and Rajasthan, despite fiscal constraints.

2. Unsustainable Fiscal Health:

- **States like Punjab and Delhi** struggle with debt due to excessive freebies.
- **Karnataka and Rajasthan's** policies of monthly cash transfers raise concerns about long-term sustainability.

- **Ease of doing business (BRAP rankings)** reflect a wide variation in competitiveness, with some states lagging due to fiscal mismanagement.

What is the significance of Competitive and Cooperative Federalism?

Competitive federalism:

- 1. Enhancing economic efficiency:** Encourages states to align policies with local needs, leading to investment and job creation.
- 2. Encouraging policy innovation:** States experiment with new governance models and regulatory frameworks.
- 3. Strengthening fiscal discipline:** Competitive federalism, when linked to financial prudence, ensures that states balance spending and revenue generation.
- 4. Improving public service quality:** To attract businesses and skilled workers, states invest in infrastructure, education, and healthcare.

Cooperative Federalism

- 1. Balanced Regional Development:** Promotes equitable growth by reducing regional disparities through collaboration between the central and state governments.
- 2. Facilitates Resource Sharing:** Encourages joint initiatives in infrastructure, disaster management, and environmental protection, ensuring optimal resource utilization and avoiding duplication of efforts.

What are the key initiatives undertaken to enhance both Competitive and Cooperative Federalism?

Competitive Federalism

State-Level Policy Initiatives	<ol style="list-style-type: none">1. TS-iPASS (Telangana) a single-window clearance for businesses2. Global Investors Meet (Tamil Nadu) attracts FDI and domestic investment3. GIFT City (Gujarat) turned into a global financial hub.
Investment Friendliness Index (IFI)	To be launched in 2025, the IFI will rank states based on investment attractiveness. It will be built on the Business Reform Action Plan (BRAP) by DPIIT, which has driven regulatory reforms since 2014-15.
PPP Project Pipelines	States mandated to develop public-private partnerships (PPP) for infrastructure projects.

Cooperative Federalism

National Manufacturing Mission (NMM):	Aims to foster cooperative federalism by aligning central and state efforts to strengthen manufacturing ecosystems . Encourages States to compete on efficiency while collaborating on systemic improvements.
India Infrastructure Project Development Fund (IIPDF):	The IIPDF fosters cooperative federalism by providing financial and technical assistance , enabling states—regardless of their fiscal capacity—to actively participate in national infrastructure development.
Economic Survey 2022-23	Highlights the importance of cooperative federalism in achieving sustainable development goals.

What are the challenges in Competitive and Cooperative Federalism?

Challenges in Competitive Federalism:

- 1. Quasi-Federalism & Central Dominance:** The **Union government holds superior powers** through the **residuary list** and **precedence in the concurrent list**, often overriding state authority and limiting competition.
- 2. Unchecked competition & Race to the Bottom:** States engage in reckless subsidies and tax breaks to attract investment, often leading to fiscal mismanagement. Bureaucratic inefficiencies negate the benefits of competition, preventing real structural reforms.
- 3. Conflict Between Finance Commission (FC) and GST Council:** **Article 269A(1)** empowers the GST Council to recommend tax-sharing for inter-state trade, while **Articles 270(1A) and 270(2)** state that GST revenues must be distributed as per Finance Commission (FC) recommendations. This **imbances both cooperative federalism (GST) and competitive federalism (FC)**.

Challenges in Cooperative Federalism:

1. Inequitable Distribution of Central Tax Revenue:

- States like **Bihar, Odisha, and Assam** argue that uniform funding **ignores economic disparities**, putting them at a disadvantage.
- Richer states feel burdened by having to **contribute more tax revenue** while receiving fewer central grants.

2. Implementation Gaps in Centrally Sponsored Schemes:

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- Many schemes (e.g., Smart Cities Mission, National Health Mission) suffer from bureaucratic inefficiency, leading to delays and poor execution.
 - States lack flexibility in implementation, leading to inefficient spending.
- What are the recommendations for Reform?

1. Conditional Grants Framework: The Finance Commission should link central grants to performance-based criteria to curb fiscal imprudence.

2. Policy Innovation: The National Manufacturing Commission should drive real policy shifts rather than duplicating existing schemes.

3. Yardstick Competition: Public rankings create reputational incentives for states to improve performance relative to peers. For ex- Scandinavian countries use competitive federalism while maintaining strict fiscal rules.

4. Accountability Mechanisms: Establish clear frameworks to prevent states from prioritizing populism over fiscal prudence.

5. Market-Preserving Federalism: Subnational competition drives efficiency and innovation, while a structured national framework prevents coordination failures. For ex- Germany's federal financial system ensures competition while maintaining equal development.

6. Balanced Competitive & Cooperative Federalism: Ensure responsible competition while collaborating on systemic improvements.

Read more: [The Hindu](#)

UPSC Syllabus- GS 2- Issues and challenges pertaining to the federal structure