



THE FINANCE COMMISSION

RECOMMENDATIONS - 2020 TO H.E. THE PRESIDENT

**(In terms of the Article 154 R (4) of the Constitution of the
Democratic Socialist Republic of Sri Lanka)**

September 2019



இதே கௌரவப் பதவி

(சான்றிதழ் வகைப்பாடு 154 "ர" வகைப்பாடு கீழ் பின்பற்றப்படும்)

நிதி ஆணைக்குழு

(சுரேயலாபம் 154 "ர" ஆம் உறுப்பினரின் கீழ் தாமிக்கப்பட்டது)

FINANCE COMMISSION

(Established under Article 154 "R" of the Constitution)

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மேல் எண் } FC/3/1/2019
எனது இல. }
My No. }

உமது இல. }
Your No. }

திகதி } 03.09.2019
Date }


His Excellency Maithripala Sirisena
President of the Democratic Socialist Republic of Sri Lanka
Presidential Secretariat
Colombo 01

Your Excellency,

In terms of Article 154R (4) of the Constitution of the Democratic Socialist Republic of Sri Lanka, the Finance Commission is required to make Recommendations as to "the principles on which such funds are granted annually by the Government for the use of Provinces, should be apportioned between the various Provinces".

I hereby submit the Recommendations of the Finance Commission in respect of the apportionment of the funds to be allocated from the Annual Budget for the use of the Provinces during the year 2020.

Yours respectfully,


Uditha H. Palihakkara
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Executive Summary

The Finance Commission was established in 1987 under Article 154 R of the Thirteenth Amendment to the Constitution of the Democratic Socialist Republic of Sri Lanka. In terms of the Constitutional mandate, the Finance Commission makes Recommendations to the Government on allocation of adequate funds from the Annual Budget to meet the needs of the Provinces. Accordingly, the Finance Commission assesses the needs of the Provinces and recommends to the President the principles of apportioning funds between the Nine Provinces, with the objective of achieving balanced regional development in the country.

The recommendations of the Finance Commission include: provision of adequate funds under the Government Grants to Provinces with the basis and principles of apportioning of funds among Provinces in a rational manner, and the policy recommendations to achieve balanced regional development with higher socio- economic standards of the people in the country and for effective implementation of public investment programme and service delivery at sub national level.

The Finance Commission recommends the Grants from the Government Annual Budget to the Provincial Councils in the following forms.

- a. Block Grant to meet the recurrent expenditure needs of the Provinces
- b. Province Specific Development Grant for financing capital nature development programmes
- c. Criteria Based Grant for financing capital nature
- d. Revenue Performance Grant in order to improve devolved revenue performance.

In the assessment and recommendation of the Block Grant for recurrent nature expenditure needs of the Provinces, the targeted devolved revenue and transfer of government revenue to the Provincial Councils are considered. In the Recommendation of capital grants under PSDG and CBG and apportionment of funds among the Provinces, the Finance Commission adopts a Composite Index using selected Provincial level variables.

The Finance Commission also recognizes and highlights the major issues and limitations in achieving balanced regional development and submits recommendations to overcome such issues for effective implementation.

1. Introduction

The Finance Commission was established in 1987 under Article 154 R of the Thirteenth Amendment to the Constitution of the Democratic Socialist Republic of Sri Lanka.

1.1. Mandate of the Finance Commission

The Thirteenth Amendment to the Constitution made provisions for the establishment and operation of the Finance Commission. The mandate of the Finance Commission as defined in Article 154 R (3), (4) and (5) of the Constitution is as follows;

154 R (3) The Government shall, on the recommendation of, and in consultation with, the Commission, allocate from the Annual Budget, such funds as are adequate for the purpose of meeting the needs of the Provinces.

154 R (4) It shall be the duty of the Commission to make recommendations to the President as to;

- a) the principles on which such funds are granted annually by the Government for the use of Provinces should be apportioned between the various Provinces; and
- b) any other matter referred to the Commission by the President relating to provincial finance.

154 R (5) The Commission shall formulate such principles with the objective of achieving balanced regional development in the country, and shall accordingly take into account-

- a) the population of each Province;
- b) the per capita income of each Province;
- c) the need, progressively, to reduce social and economic disparities; and
- d) the need, progressively, to reduce the differences between the per capita income of each Province and the highest per capita income among the Provinces.

The Article 154 R (7) of the Constitution requires that “The President shall cause every recommendation made by the Finance Commission under this Article to be laid before Parliament and shall notify Parliament as to the action taken thereon”.

1.2. Main Function of the Finance Commission

In terms of the Constitutional mandate, the main function of the Finance Commission is to make recommendations to the Government on allocation of adequate funds from the annual budget to meet the needs of the Provinces and to recommend the principles to the President as to how such funds should be apportioned between the nine Provinces, with the objective of achieving balanced regional development in the country. In this process, the Finance Commission provides Guidelines to the Provincial Councils for assessing the provincial needs.

Accordingly, the Finance Commission assesses the needs of the Provinces and recommends to the President the principles of apportioning funds between the Provinces.

The recommendations of the Finance Commission include: the budget recommendation with apportionment of funds among Provinces in a rational manner, provision of adequate funds under the Government Grants to Provincial Councils and the policy recommendations to achieve balanced regional development in the country for higher socio- economic standards of the people.

2. National Budget and Government Grants to the Provincial Councils

2.1. Constitutional Provision on Fiscal Devolution

The Thirteenth Amendment to the Constitution created three distinctive tiers of governance, i.e. the Central Government, Provincial Councils and Local Authorities. Accordingly, a devolved governance was established by demarcating the areas of legislative, executive and financial authority to be exercised by the Provincial Councils. The subject contents of powers are also specified in the three lists given in the Thirteenth Amendment, as the Provincial Councils List (powers devolved to the Provincial Councils), the Reserved List (powers of the Center), and the Concurrent List (subjects of shared responsibilities).

The public investment and service delivery at sub-national levels are performed by i) the Central Government spending agencies and ii) Provincial Council spending agencies including Local Authorities.

The Provincial subjects are extensive and include Education, Health, Local Government, Roads, Agriculture, Irrigation, Social Services, Rehabilitation, Rural Development and Sports etc. The Provincial Council List also includes the sources of revenue to be collected by the Provincial Councils. The Provincial Councils are responsible to implement activities in the Provincial Council List and have shared responsibilities under the Concurrent List.

2.2. Allocation of Funds to meet the Needs of the Provinces

The Constitution requires the Government to allocate adequate funds to meet the needs of the Provinces. In this context, the Finance Commission:

- Formulates principles in a rational manner for resource allocation to the nine Provinces under the Government Annual Budget with the objective of achieving balanced regional development in the country.
- Determines and recommends the needs of the Provinces based on the requirements submitted by each Provincial Council.
- Apportionment of such funds between the Provincial Councils with the objective of reducing disparities among the Provinces.

2.3. Allocation of Government Grants to the Provincial Councils

The Government allocates, funds in the form of grants to the Provincial Councils as follows:

- e. **Block Grant** meets recurrent expenditure needs of the Provinces for the purpose of sustaining and improving the public service delivery. Personnel Emoluments on approved cadre by the Department of Management Services is the major portion of Provincial Council recurrent expenditure. This grant includes the transfers to Local Authorities to meet their expenditure on salaries to staff and allowances to Members, and the expenditure on maintenance of capital assets. The allocation and release of Block Grant during the period from 2015 - 2019 is given in Annex - 01.
- f. **Province Specific Development Grant (PSDG)** is meant for financing capital nature development programmes with special attention to infrastructure and community development in various sectors under the devolved subjects. The Medium-Term Development Plan for the Provinces and the Provincial Annual Development Plans are formulated by the Provincial Councils in a common integrated framework aligned with the Guidelines provided by the Finance Commission.

The financing arrangements for the Provincial Annual Development Plans is made under different sectors. The following sectors are incorporated in the Provincial Development Plans, considering specific requirements of the Provinces, and the major part of PSDG is allocated among the sectors.

* Education	* Provincial Roads	* Land Development
* Western Medicine	* Estate Infrastructure	* Irrigation
* Indigenous Medicine	* Transport	* Agriculture
* Sports	* Housing	* Livestock
* Probation and Childcare	* Rural Electrification	* Inland Fisheries
* Social Services	* Local Government	* Small Industries
* Cultural and Religious Affairs	- <i>Local Authority Roads</i>	* Tourism
* Co-operative Development	- <i>Community Water Supply</i>	* Rural Development
* Early Childhood Development	- <i>Waste Management</i>	

A flexible amount is earmarked for each Province to address identified gaps in the Provincial investment programme and also to cater for villages with special needs. In addition to the recommended PSDG amount by the Finance Commission, the allocations for special projects of Provinces identified at national level are also included under PSDG.

The formulated Annual Development Plans with financial allocations to each Provincial Council under PSDG are jointly reviewed by the Finance Commission and the respective Provincial Councils and agree for implementation in the Provinces every year. The allocations and released funds under PSDG (excluding special projects) for implementation of Annual Development Plans of the Provinces during the period 2015 - 2019 are given in Annex - 02.

- g. **Criteria Based Grant (CBG)** is also for financing capital nature expenditure for improving the socio-economic conditions of the people, contributing towards reducing regional disparities. The CBG funds are available to the Provincial Councils for discretionary spending on development related activities within an agreed financing framework, following the Guidelines of the Finance Commission. The allocation and release of funds under Criteria Based Grant during the period 2015 - 2019 are given in Annex -3.
- h. **Revenue Performance Grant** is recommended to Provincial Councils in order to improve their revenue performance. This is a development oriented small grant pivoted on annual incremental devolved revenue collections. The Provincial Councils have discretionary power to use this grant for capital related development programmes. The details of revenue collected by Provinces in 2018 are given in Annex - 4.

3. Needs Assessment by Provincial Councils and Request for Government Grants

The annual requirement of needs on capital and recurrent nature expenditure of each Provincial Council is submitted to the Finance Commission. The requirements of Provincial Councils are reviewed by the Finance Commission before making recommendations to H E the President and the Government.

The development policy framework of the public expenditure management, and expected annual expenditure within the framework of the Medium-Term Development Plans of the Provinces and previous performances on spending public funds by the Provincial Councils are taken into consideration in the need assessment.

3.1. Socio Economic Conditions of Provinces

The development process moves with exercising the devolution of power at sub-national levels for achieving balanced regional development for the benefit of the people in all parts of the country. It will foster the extension of benefits of economic progress, including widespread transmission of economic opportunities to different parts of the country, applying resources over a wide area in various locations, especially in lagging regions and underserved areas, to reduce regional disparity adopting a gap-filling approach.

The Western Province has the highest population and also the highest GDP share with the least land area compared to other Provinces. The least population as well as the lowest GDP is in the Northern Province. The largest area belongs to the North Central Province.

The infrastructure and community facilities contribute to regional development enhancing the socio-economic conditions in the regions and sub-regions. Socio-economic indicators show disparities among the Provinces compared with the national average (Table 01). Considerable variances among the Provinces are observed in the areas on account of access to basic needs to people, such as health services, education facilities and the poverty level among the communities, prosperity of the Provinces and other socio-economic performances (Table 02).

Table - 01: Selected Socio-Economic Indicators of Provinces

Provinces	Land Area 2017 (Sq.km.)	Mid-year Population 2017 (‘000)	Provinci al GDP 2017 (Rs.Bn.)	Median Monthly Per Capita Income 2016 (Rs.) (per person per household)	Un- employment Rate 2017 (%)	Poverty Head Count Index 2016	Prosperity Index 2017
Western	3,593	6,081	4,949	14,400	3.2	1.7	1.28
Central	5,575	2,722	1,428	9,890	4.5	5.4	0.35
Southern	5,383	2,611	1,317	11,253	5.0	3	0.49
Northern	8,290	1,119	602	8,434	7.7	7.7	0.19
Eastern	9,361	1,677	754	11,420	6.0	7.3	0.07
North Western	7,506	2,508	1,412	11,420	3.7	2.7	0.35
North Central	9,741	1,349	749	11,248	4.3	3.3	0.20
Uva	8,335	1,349	1,047	10,139	3.5	6.5	0.14
Sabaragamuwa	4,921	2,028	1,060	9,711	3.7	6.7	0.15
Sri Lanka	62,705	21,444	13,317	11,307	4.2	4.1	0.77

Source: Central Bank of Sri Lanka, Department of Census and Statistics

Table - 02: Basic Needs and Infrastructure Facilities in Provinces

Provinces	Road Density 2017 (Km.)	Safe Drinking Water 2016 (HH %)	Electricity for Lighting 2016 (HH %)	Toilet Facilities 2016 (HH %)	No. of Hospitals 2017	No. of Schools 2017	No. of University Admissions 2017
Western	1.02	98.2	98.7	93.0	157	1,359	8,248
Central	0.72	77.7	96.8	91.5	170	1,519	3,224
Southern	0.60	92.7	98.6	92.8	120	1,112	4,525
Northern	0.41	92.3	92.4	89.1	105	997	2,039
Eastern	0.24	97.7	93.2	90.6	124	1,110	2,307
North West	0.55	92.7	95.9	90.3	147	1,256	3,142
North Central	0.32	71.2	97.3	88.7	89	812	1,554
Uva	0.42	79.4	96.0	92.4	91	900	1,770
Sabaragamuwa	0.82	76.0	96.4	91.8	113	1,129	2,887
Sri Lanka	0.50	88.8	96.9	91.7	1,116	10,194	29,696

Source: Central Bank of Sri Lanka, Department of Census and Statistics, Ministry of Education, Ministry of Health and Indigenous Medicine.

Note : Road Density is road length per Sq.km.

3.2. Service Delivery of Provincial Councils

As per the Constitutional provisions, the Provincial Councils perform service delivery functions with public investments at sub-national levels, and necessary institutional arrangements are made with required number of cadre for Provincial Councils and Local Authorities to perform their mandatory services.

The provincial subjects are extensive, and include major sectors such as Education, Health, Local Government, Roads, Agriculture, and Irrigation etc. (Table 03).

Table - 03: Service Delivery by Provincial Councils - Assets, Institutions and Employees

Provinces	Roads km.		No. of Schools 2017	No. of Hospitals 2017	No. of Local Authorities 2018	Approved Cadre of Provincial Council 2019
	Provincial	Rural				
Western	1,952	11,180	1,287	134	49	63,111
Central	2,244	13,216	1,465	165	47	50,744
Southern	1,630	10,491	1,046	116	49	46,551
Northern	2,120	11,668	975	104	34	36,148
Eastern	1,121	12,171	1,080	117	45	37,900
North West	2,745	20,571	1,221	145	33	47,541
North Central	1,947	12,709	802	87	27	29,887
Uva	2,371	10,923	864	89	28	32,054
Sabaragamuwa	2,371	7,871	1,101	110	29	37,703
Sri Lanka	18,921	83,956.8	9,841	1,067	341	382,639

Source: Department of Census and Statistics, Ministry of Internal and Home Affairs and Provincial Council and Local Government, Ministry of Education, Ministry of Health, Nutrition and Indigenous Medicine.

In this context, adequate funds for development are necessary to the Provincial Councils to deliver public services in the respective Provinces in line with their mandatory functions based on Provincial Medium-Term and Annual Development Plans.

3.3. Capital Expenditure Requirements of Provincial Councils

With the objectives of reducing inter/intra-regional disparity, balanced and integrated regional development, optimizing potential resources, the Provincial Councils have formulated Medium-Term Development Plans for the respective Provinces. These plans follow a multi-sector integrated results-based approach. The sector and sub-sector performance targets and sectoral programmes to achieve the goals are well defined and includes in the plans, with a tentative summarized annual financial requirement.

In line with the Medium-Term Integrated Plan of the Provinces and expected service delivery, each Provincial Council has developed an Agency Results Framework which incorporates the result framework of every development sector and spending agency.

The Finance Commission issued Annual Capital Guidelines to Provincial Councils in February 2019 to prepare their capital needs for 2020, giving due consideration to the following:

- National Development Policy Framework
- Special development programmes of the Government at sub-national level
- Achievement of the Sustainable Development Goals (SDGs)
- Optimum utilization of physical and human resources in the Provinces
- Reduction of inter and intra - regional disparities in development
- Readiness in project implementation and their feasibility
- Public Investment Programme (PIP)

3.4. Recurrent Expenditure Requirements of Provincial Councils

The major portion of recurrent expenditure accounts for Personal Emoluments (PE) on the cadre of Provincial Councils. The other recurrent expenditure includes travelling, supplies, maintenance, contractual services and transfers to others agencies such as Local Government Authorities, Early Childhood Development Authorities, Provincial Passenger Transport Authorities and Provincial Road Development Authorities. The maintenance requirements of capital assets e.g. roads, buildings, irrigation, are also accounted under Other Recurrent Expenditure (ORE).

The Finance Commission issued Annual Recurrent Guidelines to Provincial Councils in February 2019 to identify their recurrent needs for 2020, considering the following:

- Approved cadre
- Actual living cadre and vacancies at the Province
- New appointments made by the Line Ministries to Provincial Councils
- Estimates of Personal Emoluments, salary arrears and staff loans
- Estimates of other recurrent expenditure including maintenance of capital assets
- Allowances for elected Members
- Transfers to the Local Authorities and other agencies
- Relevant Government Circulars

3.5. Requirement of Capital and Recurrent Budget of the Provinces for 2020

All Provincial Councils have submitted their requirements of capital and recurrent budget needs under the Government grant for the year 2020.

Table - 04: Requests of Provincial Councils on Capital and Recurrent Budget Needs - 2020
(Rs. mn.)

Provincial Councils	Capital Needs	Recurrent Needs			Total Needs
		PE	ORE	Total	
Western	6,171.7	50,618.4	31,928.3	82,546.7	88,718.4
Central	14,475.6	37,479.5	11,432.7	48,912.2	63,387.8
Southern	12780.3	32,132.5	10,300.0	42,432.5	55,212.8
Northern	14,639.6	25,215.0	8,017.9	33,232.9	47,872.5
North Western	9,125.9	34,445.7	9,998.3	44,444.1	53,569.9
North Central	6,967.5	21,689.1	6,343.5	28,032.5	35,000.1
Uva	12,029.3	23,337.2	6,960.3	30,297.5	42,326.8
Sabaragamuwa	7,328.0	30,917.2	8,190.0	39,107.2	46,435.2
Eastern	18,619.5	26,114.9	10,034.4	36,149.2	54,768.8
Total	102,137.4	281,949.5	103,205.3	385,154.8	487,292.3

3.6. Provincial Revenue Sources

Provincial revenue originates from two main sources:

i) Transfer of Government Revenue

As per the Fiscal Policy Circular No. 01/2010, issued by the General Treasury on 29th December 2010, the national revenue authorities, namely the Commissioner General of Department of Inland Revenue, the Director General of Customs, and the Commissioner General of Department of Motor Traffic, have been directed to transfer the collected revenue to the Provinces on the following basis.

- a. 33 1/3 % of the Nation Building Tax (NBT)
- b. 100 % of Stamp Duty
- c. 70 % of Vehicle Registration Fees

ii) Revenue from Devolved Sources

Provincial revenue sources through tax revenue and non-tax revenue are listed in 36.01 to 36.20 in the Ninth Schedule of the Thirteenth Amendment to the Constitution. The main sources of provincial revenue include Motor Vehicle License Fees, Excise Duty, Stamp Duty and Court Fines. The Stamp Duty and Court Fines collected by the Provinces are transferred to the Local Authorities.

3.7. Revenue Forecast for year 2020

Setting of revenue targets for the Provinces is based on two main sources of revenue, viz. transfers of Government revenue and target for devolved revenue sources. The total amount of forecasted revenue under the above two sources is deducted from the assessed provincial recurrent needs. The Finance Commission engages in a consultative process with the General Treasury and Provincial Councils, in setting the revenue targets.

i) Transfer of Government Revenue

The Department of Fiscal Policy estimates the annual total amount of transfers of Government revenue to be distributed to the Provinces. The provincial share of the total amount of Government transfers in terms of the Fiscal Policy Circular No: 01/2010 of 29.12.2010 is given in Table - 05.

Table - 05: Share of Transfers of Government Revenue to the Provinces - 2020

(Rs.mn.)

Province	Provincial Share %
Western	48
Central	09
Southern	09
Northern	05
North Western	09
North Central	05
Uva	05
Sabaragamuwa	05
Eastern	05
Total	100

ii) Targets for Devolved Revenue Sources -2020

The forecasted revenue collection for 2020, including stamp duty and court fines, is Rs. 49,756 million. The forecast revenue for 2020, excluding stamp duty and court fines, is Rs. 20, 111 million. The revenue forecast made for 2020 under the devolved sources is given in Table - 06.

Table - 06 : Revenue Forecast under Devolved Sources for 2020

(Rs.mn.)

Province	Revenue Forecast excluding Stamp Duty & Court Fines			Revenue Forecast including Stamp Duty & Court Fines		
	Provincial Estimate	FC Forecast	Percentage of Provincial Share (FC Forecast)	Provincial Estimate	FC Forecast	Percentage of Provincial Share (FC Forecast)
Western	7,096	7,750	39	25,046	26,750	54
Central	2,067	2,095	10	4,137	4,195	08
Southern	1,904	2,030	10	4,224	4,550	09
Northern	772	880	04	1,697	1,860	04
North Western	2,494	2,545	13	4,869	4,970	10
North Central	1,296	1,406	07	1,716	1,826	04
Uva	919	1,025	05	1,359	1,605	03
Sabaragamuwa	1,247	1,375	07	2,047	2,275	05
Eastern	946	1,005	05	1,636	1,725	03
Total	18,740	20,111	100	46,730	49,756	100

The forecasted amount of stamp duty and court fines are required to be transferred to the Local Authorities from total revenue for 2020 is Rs. 29,645 million. The provincial break-down of stamp duty and court fines to Local Authorities is given in Table - 07.

Table - 07: Stamp Duty and Court Fines to be transferred to the Local Authorities for 2020

(Rs.mn.)

Province	Stamp Duty	Court Fines	Total	Provincial Share (%)
Western	18,000	1,000	19,000	64.1
Central	2,000	100	2,100	7.1
Southern	2,000	520	2,520	8.5
Northern	800	180	980	3.3
North Western	2,100	325	2,425	8.2
North Central	180	240	420	1.4
Uva	360	220	580	2.0
Sabaragamuwa	700	200	900	3.0
Eastern	550	170	720	2.4
Total	26,690	2,955	29,645	100.0

4. Recommendation for Fund Allocation from Government Annual Budget and Apportionment of Funds among Provincial Councils 2020.

4.1. Composite Index and Apportionment of Capital Expenditure Funds

The Finance Commission developed an improved statistical formula in collaboration with the Department of Census and Statistics for the apportionment of funds to the Provinces. Viz a Composite Index adopting a multivariate statistical technique called “Factor Analysis” is used by the Commission to apportion capital funds among the Provinces in a rational manner. The Composite Index recognizes the following Provincial level variables. The selected variables are given Annex - 05.

- Mid-year population
- Provincial GDP
- Number of persons under poverty
- Median Monthly Per-capita Income
- Persons per Medical Officer
- Number of candidates qualified for Universities in Science Stream

Table - 08: Composite Index and Percentages for Apportionment of Capital Funds among the Provinces for the Year 2020

Provinces	Composite Index	Percentage
Western	0.71179	7.83 %
Central	1.01822	11.21 %
Southern	0.93367	10.28 %
Northern	1.17468	12.93 %
North Western	0.92328	10.16 %
North Central	1.03606	11.40 %
Uva	1.05958	11.66 %
Sabaragamuwa	1.08216	11.91 %
Eastern	1.14696	12.62 %

The percentage value attributable to respective Provinces is used in the allocation of capital funds for PSDG and CBG among the Provincial Councils in 2020.

4.2. Recommendation on Apportionment of Capital Funds for 2020

In the assessment of capital needs requirement by Provincial Councils, the Finance Commission organized a series of discussions with the participation of the Honorable Governors, Chief Secretaries, Provincial Secretaries and Heads of Departments.

Based on the Composite Index, the Finance Commission determines the total amount of estimated capital expenditure for PSDG under the Government Annual Budget which has to be disbursed to Provincial Councils.

Provincial Councils prepared their annual capital budget requirement under the Government grant in line with the sector performance targets in the Medium-Term Development Plan of the respective Provinces. The requirement of grants considered by them excludes the other possible sources of funds that could be available for the respective Provinces during the financial year.

The Finance Commission recommends the following amounts under the capital grants for Provincial Councils for the year 2020.

Table - 09: Recommended Capital Grants for Provincial Councils - 2020

(Rs. mn.)

Province	Capital Grants - 2020		
	PSDG	CBG	RPG
Western	7,047.0	704.7	849.0
Central	10,089.0	1,008.9	282.0
Southern	9,252.0	925.2	468.0
Northern	11,637.0	1,163.7	396.0
North Western	9,144.0	914.4	333.0
North Central	10,260.0	1,026.0	132.0
Uva	10,494.0	1,049.4	141.0
Sabaragamuwa	10,719.0	1,071.9	177.0
Eastern	11,358.0	1,135.8	222.0
Total	90,000.0	9,000.0	3,000.0

Other than the PSDG and CBG, a Revenue Performance Grant (RPG) has been introduced to encourage provincial revenue collection. Therefore, this new grant will be included in the National Budget 2020. CBG and RPG will not be an additional burden to the Government as they represent a small amount carved out amount from the total amount to be apportioned between the Provinces.

4.3. Recommendation and Apportionment of Recurrent Funds

After a review on recurrent budget needs submitted by each Provincial Council, the Finance Commission organized a series of discussions with relevant provincial officials to assess the required recurrent needs. However, the estimated devolved revenue collection should be deducted from the total estimated recurrent expenditure. As revenue transfers from the Government to Provincial Councils have not yet been estimated by the Department of Fiscal Policy, the recommendation of the Block Grant, subject to deduction of revenue transfers discussed above is given in Table-10.

Table - 10 : Recommended Block Grant for Provincial Councils - 2020*(Rs. '000.)*

Province	Estimated Total Recurrent Expenditure*	Rev. Target Excluding Stamp Duty and Court Fines by Prov. Councils	Total Block Grant (before deduction of transfers)
Western	66,282,976	7,750,000	58,532,976
Central	47,550,078	2,095,000	45,455,078
Southern	40,353,850	2,030,000	38,323,850
Northern	33,263,115	880,000	32,383,115
North Western	42,992,551	2,545,000	40,447,551
North Central	27,878,598	1,406,000	26,472,598
Uva	31,447,956	1,025,000	30,442,956
Sabaragamuwa	37,160,832	1,375,000	35,785,832
Eastern	35,684,706	1,005,000	34,679,706
Total	362,614,662	20,111,000	342,503,662

* includes Personal Emoluments for vacancies, line ministry attachments and salary arrears

It is recognized that the expenditure on maintenance of capital assets such as roads, buildings and irrigation is included in the estimated total recurrent expenditure. In addition, the transfers to the Local Authorities for payment of salaries of the approved cadre and allowances for Members is also included in Table -11.

Table - 11: Transfers to the Local Authorities - 2020*(Rs. '000.)*

Province	Allowances for Members	Reimbursement of Salaries	Local Government Transfers (Total)
Western	353,040	10,826,746	11,179,786
Central	236,880	3,741,964	3,978,844
Southern	213,960	2,818,375	3,032,335
Northern	145,800	2,104,526	2,250,326
North Western	181,980	2,334,326	2,516,306
North Central	110,580	1,071,045	1,181,625
Uva	115,235	1,425,519	1,540,754
Sabaragamuwa	163,450	1,540,266	1,703,716
Eastern	172,260	2,059,236	2,231,496
Total	1,693,185	27,922,003	29,615,188

5. Issues and Limitations in Making Recommendations to Achieve Balanced Regional Development

Currently the Provincial Councils receive funds in the following forms for their service delivery in the respective Provinces.

- a) Grants from the Government Annual Budget for capital and recurrent expenditure needs based on the Recommendations of the Finance Commission
 - b) Allocation from Line Ministries for implementation of development activities by Provincial Councils
 - c) Allocation for Implementation of Provincial Component of Special Foreign funded Projects
- I. The Commission observed that there is no proper coordination between the Department of National Planning, Department of National Budget, Finance Commission, Provincial Councils and other stakeholders. In the absence of an integrated planning mechanism with effective coordination, the respective agencies fail in their responsibilities leading to duplication and wastage of resources.
 - II. The Provincial Authorities have opined that the Government grant for capital expenditure to Provincial Councils is insignificant and requested an increase in the capital budget grant to the Provincial Councils at least to 25% of the total capital expenditure budget of the Government for service delivery in line with the mandatory functions under the Provincial Council List of the Constitution.
 - III. It is noted that a substantial amount of allocations is made for implementation of devolved nature development activities through Line Ministries and also for the implementation of provincial component of special projects. These allocations are outside the knowledge and the recommendation of the Finance Commission. The Finance Commission is of the view that these allocations are made in an ad-hoc manner without proper need assessments. This practice affects the Balanced Regional Development process to a great extent inevitably leading to sub-optimizations of socio-economic returns.
 - IV. As per the Constitutional provisions, only five ministries have been established in a Provincial Council. However, the portfolio of the ministries at Provincial level is irrationally distributed among the five provincial ministries leading to a lack of coordination in sector planning, budgeting and accounting in Provincial Councils. It needs to be addressed effectively.

- V. Currently, most of the contracts at provincial levels are awarded sub-dividing work with the view to assigning the works to Community Based Organizations. This affects quality and desired outcomes.
- VI. Although around twenty devolved revenue sources of Provincial Councils are identified in the Constitution, revenue mechanism at Provincial Councils is ineffective in view of the following.
- a) BTT was the major source of provincial revenue and this has been withdrawn.
 - b) Revenue from major sources are collected centrally and distributed to Provincial Councils.
 - c) Provincial Councils are unable to pass revenue legislations since such legislations require the Parliamentary approval
 - d) The rates of devolved revenue in a number of cases need to be approved by Parliament.
- VII. Government allocations for Health and Education sectors have been on the increase despite substantial investments are made by the private sector resulting in duplication and sub-optimization. An increase in out of pocket expenses of the people is also noted.
- VIII. The Finance Commission receive the Auditor General's Report in respect of Provincial Councils with serious observations. The Finance Commission has no mandate to control or monitor the activities of Provincial Councils other than the major highlights noted by the Commission are referred to Provincial Governors and Chief Secretary.

6. Policy Recommendation - 2020

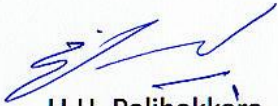
Taking into consideration of the issues and limitations, discussed in Section 5 above, the Finance Commission recommends the following.

- I. It is observed that lack of coordination in policy making and planning on public investments at national and sub-national levels has led to a slowdown in balanced regional development and the development of the country as a whole. Therefore, the Finance Commission has initiated a comprehensive uniform planning system for the nine Provinces with the involvement of the Department of National Planning and Provincial Councils for need assessment process, aiming at effective development oriented investments. Further, it is recommended to strengthen this process by adopting an integrated approach with the participation of all stakeholders at national and sub-national levels, and establishment of a common framework for national and sub-national planning, within the concept of devolution. The Department of National Planning and the Finance Commission have to take a lead role in comprehensive intergrated planning, effective need assessment and allocating resources for public investment.
- II. A large volume of mandatory services delivered at sub-national level have been devolved to the Provincial Councils by the 13th Amendment to the Constitution. To perform the devolved responsibilities, all Provincial Councils have developed their own Medium-term Development Plans and Annual Implementation Plans following the Guidelines of the Finance Commission. Furthermore, Provincial Councils have established institutions to implement devolved subjects. Currently Provincial Councils perform some development activities of the national ministries who do not have the capacity for implementation at sub-national level. However, line ministries continue to receive funds from the Treasury to implement devolved subjects. Therefore, it is recommended that adequate funds be provided to Provincial Councils for investing on devolved subjects, and implement such subjects only through the Provincial Councils. Providing adequate funds to Provincial Councils will not be an additional burden to national budget if the allocation for national ministries on devolved subjects could be avoided. It is noted that only an insufficient amount of funds is distributed among the Provincial Councils following a rational methodology. It will undermine the achievement of Balanced Regional Development in the country, since only a small part of the National Budget is spent through the Provincial Councils. In addition, it is recommended that the National Ministries and Departments should also distribute their allocations among the Provinces in a rational manner based on an acceptable formula, in consultation with the Finance Commission to achieve balanced regional development.
- III. The implementation of devolved nature projects identified at the national level should also be carried out through the Provincial Councils within the agreed development framework. The budgetary allocation for provincial components of special donor funded projects in relation to

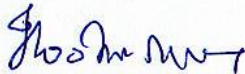
devolved subjects should be made to the Provincial Councils directly for implementation and such information should be made available to the Finance Commission. This would minimize duplication of funds and overlapping of activities thereby enhancing effective utilization of funds and improving transparency and accountability in public investments.

- IV. In place of the current practice of irrational distribution of ministries in the Provincial Councils, It is recommended that the portfolio of five ministries in Provinces is designed appropriately enabling an efficient and effective management, implementation, coordination and compatibility.
- V. The Finance Commission has observed that allowing direct contracts to Community Based Organizations have led to proliferation of small development activities. This will not assure quality, productivity and good delivery of services for overall benefit to communities. Therefore, the Commission recommends that direct contracts should be limited only to societies in a GN division where the project is located without permitting any sub-contracts.
- VI. The Finance Commission has observed that the revenue sources assigned to Provinces under the 13th Amendment to the Constitution are not adequate to meet the expenditure and roles and assigned responsibilities on devolved subjects. Further, Provinces cannot introduce any new revenue source without the approval of Parliament. Therefore, it would be appropriate to carry out an in-depth study on the revenue aspects by the Department of Fiscal Policy in collaboration with the Provincial Councils on this matter with a view to formulating appropriate policies. The Provincial Councils should endeavor to maximize their revenue in order that the burden on Government could be alleviated. In this regard reference to item 21 of the Provincial Council List under the Ninth Schedule on income generating projects is imperative.
- VII. The health system in the country has contributed to achieve a better Human Development Index. However, the cost of health borne by the Government has increased over the last several years inspite of high investments in health by the private sector, leading to negative outcomes. Therefore, it is recommended to carry out an intensive study on this matter jointly by the Ministry of Health and the Ministry of Finance. It is also suggested a similar study be carried out for the education sector. It is noted that out of pocket expenditure on health by the general public is also been increasing over the years. Promotion of contributory system for healthcare is also recommended.
- VIII. Auditor General's reports highlight serious issues of concern, which need the attention of Provincial Governors and Chief Secretaries. We recommend that the Audit Committees at Provincial level should meet regularly to address these issues and make recommendations to Provincial Councils to overcome the weakness in an effective manner. The internal audit system and control mechanisms at Provincial Councils should also be strengthened.

The Finance Commission submits the recommendations for highest consideration and effective implementation.



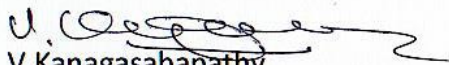
U.H. Palihakkara
Appointed Member and Chairman



Indrajit Coomaraswamy
Ex-officio Member and the Governor of the Central Bank of Sri Lanka



R.H.S. Samaratunga
Ex-officio Member and the Secretary to the Treasury



V. Kanagasabapathy
Appointed Member



H.M. Zafrullah
Appointed Member

Annex – 01 : Allocation and Release of Block Grant 2015 – 2019

(Rs. Mn.)

Province	2015		2016		2017		2018		2019	
	Allo.	Release	Allo.	Release	Allo.	Release	Allo.	Release	Allo.	Release up to May 2019
Western	18,842	18,842	21,744	21,741	15,091	14,989	14,962	14,962	16,700	6,987
Central	23,542	23,542	23,375	23,374	23,320	23,233	25,894	25,894	29,000	12,112
Southern	21,459	21,459	20,508	20,507	21,033	21,084	23,807	23,807	23,200	9,725
Northern	16,268	16,268	16,757	16,754	17,078	17,034	19,035	19,035	20,550	8,606
North Western	21,705	21,634	20,829	20,821	21,866	21,788	22,463	22,463	24,250	10,118
North Central	13,616	13,616	14,174	13,722	13,829	13,686	15,355	15,355	16,300	6,850
Uva	16,237	16,237	16,422	16,249	16,115	15,971	16,268	16,268	17,900	7,587
Sabaragamuwa	18,410	18,410	18,219	18,218	19,350	19,281	21,828	21,828	22,300	9,350
Eastern	17,475	17,475	17,166	16,996	18,668	18,430	20,482	20,482	20,500	8,600
Total	167,554	167,483	169,194	168,382	166,350	165,496	180,094	180,094	190,700	79,935

Source: Finance Commission and General Treasury

Annex – 02 : Allocation and Release of Province Specific Development Grant 2015- 2019

(Rs. Mn.)

Province	2015		2016		2017		2018		2019	
	Allo.	Release	Allo.	Release	Allo.	Release	Allo.	Release	Allo.	Release up to May
Western	2,598	2,641	2,894	1,400	765	400	1,306	450	1,463	323
Central	3,879	2,575	3,684	1,353	1,169	1,800	1,996	1,350	2,236	634
Southern	3,997	2,211	2,246	874	1,168	1,778	1,994	1,300	2,233	608
Northern	5,038	2,399	3,199	1,800	1,657	2,327	2,830	1,828	3,169	904
North Western	2,500	2,151	3,216	1,505	1,228	1,800	2,097	1,500	2,348	694
North Central	2,230	2,658	2,838	1,550	1,448	2,310	2,473	1,650	2,769	828
Uva	3,361	2,229	2,736	1,100	1,682	1,790	2,873	1,983	3,218	955
Sabaragamuwa	4,360	2,966	2,913	1,042	1,365	1,500	2,331	1,700	2,611	778
Eastern	2,469	1,830	3,297	1,510	1,544	1,952	2,637	1,839	2,953	887
Total	30,432	21,660	27,026	12,134	12,026	15,657	20,537	13,600	23,000	6,611

Source: Finance Commission and General Treasury

Note: Allocation is including Development Projects. Release Amount P S D G and C B G only

Annex – 03 : Allocation and Release of Criteria Based Grant 2015 – 2019

(Rs. Mn.)

Province	2015		2016		2017		2018		2019	
	Allo.	Release	Allo.	Release	Allo.	Release	Allo.	Release	Allo.	Release up to May 2019
Western	525	2,641	460	200	254	100	254	60	254	20
Central	500	2,575	423	117	389	200	389	200	389	75
Southern	385	2,211	413	369	388	400	389	275	389	100
Northern	400	2,399	475	437	551	589	551	522	551	150
North Western	425	2,151	375	360	408	400	408	250	408	50
North Central	375	2,658	400	400	482	300	482	250	482	50
Uva	375	2,229	475	415	560	315	560	400	559	65
Sabaragamuwa	400	2,966	514	293	454	432	454	280	454	50
Eastern	400	1,830	465	445	514	500	514	312	514	50
Total	3,785	21,660	4,000	3,036	4,000	3,236	4,001	2,549	4,000	610

Source: Finance Commission and General Treasury

Annex – 04 : Provincial Revenue Collection by Sources 2018

(Rs. '000)

Province	Target Including Stamp Duty & Court Fines 2018	Revenue Collected form Devolved Sources						Total
		BTT *	Motor Vehicle Revenue License Fees	Excise Duty	Other **	Stamp Duty	Court Fines	
Western	23,725,000	846	4,244,750	649,350	2,313,894	17,284,580	955,860	25,449,280
Central	3,492,000	1,636	963,025	424,991	527,808	1,845,477	97,068	3,860,006
Southern	4,010,000	985	1,251,751	132,947	517,982	2,003,469	472,295	4,379,429
Northern	1,220,000	-	378,372	35,255	394,602	798,260	177,033	1,783,522
North Western	4,340,000	7,804	1,396,531	151,058	503,591	1,913,484	444,571	4,417,040
North Central	1,490,000	792	604,011	64,313	600,336	167,162	237,681	1,674,295
Uva	1,570,000	1,060	451,897	97,824	357,462	349,821	213,478	1,471,542
Sabaragamuwa	2,245,000	-	768,347	119,509	333,878	320,364	192,348	1,734,446
Eastern	1,520,000	-	495,604	124,822	283,790	526,221	154,374	1,584,811
Total	43,612,000	13,123	10,554,288	1,800,069	5,833,343	25,208,838	2,944,708	46,354,371

Source: Monthly Revenue Reports of Provincial Councils – 2018

* Collection of due BTT up to 2010,

**Others Include Rents, Interests, Examination Fees, Sale of Capital Assets, Betting Tax etc.

Annex – 05: Selected Variables for the Fund Allocating Formula - 2020

Province	Mid-year Population 2017 (000')	PGDP 2017 (Rs. Mn.)	No of Persons under Poverty 2016	Median Monthly Per Capita Income 2016 (Rs.)	Persons Per Medical Officer 2017	Candidates Qualified for Universities Science Stream 2016
Western	6,081	4,949	102,476	14,400	805	30
Central	2,722	1,428	145,260	9,890	1,066	11
Southern	2,611	1,317	77,250	11,253	1,245	18
Northern	1,119	602	85,239	8,434	926	5
North Western	2,508	1,142	120,085	11,426	1,490	10
North Central	1,349	749	66,879	11,268	1,320	4
Uva	1,349	1,047	86,645	10,139	1,481	6
Sabaragamuwa	2,028	1,060	134,605	9,711	1,546	10
Eastern	1,677	754	120,085	8,261	1,153	6
Sri Lanka	21,444	13,048	938,524	94,776	11,032	100

Source: Department of Census and Statistics, Central Bank of Sri Lanka, Ministry of Health, Nutrition and Indigenous Medicine, Department of Examinations