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CHAPTER-I

INTRODUCTION

Pakistan is a federation comprising four Provinces which are unequal in area and level of economic and social development. The prime function of all the existing tiers of government system at Federal, Provincial and Local level is to provide services in keeping with the spirit of the mandate of people and law apart from fulfilling legal/regulatory obligations.

2. The fiscal decentralization to local governments is channelized through Provincial Finance Commission(PFC) which is a statutory body established under Section 52 of the Khyber Pakhtunkhwa Local Government Act, 2013. The PFC envisions its policies through its financial Award which is based on recommendations as to a self-contained fiscal transfer system meant for the whole Province. The main objective of a financial Award is to provide a transparent, formula-based equitable and predictable inter-governmental revenue-sharing system with a view to enabling the local governments to bring about improvement in their performance, service delivery and promote the general wellbeing of the people.

3. The Government of Khyber Pakhtunkhwa receives more than 90% of its revenues through Federal Transfers which consist of Federal Tax assignment, straight transfer on account of Royalty on Oil and Gas, Excise duty/Development Surcharge on Gas and Net Hydel profit.

4. The resource distribution through PFC Award is twofold: One, between the province and the local governments and, second, amongst the local governments inter se. For this purpose, a provincial pool is determined out of the proceeds of Provincial Consolidated Fund. Obligatory expenditure being common to both the provincial and local governments is subtracted from the Provincial Pool. The net proceeds thus emerging are bifurcated into Provincial Allocable Amount and Provincial Retained Amount. The Provincial Allocable Amount is further distributed amongst the local governments.

CHAPTER-II

PROFILE OF PFC AWARDS

So far, five PFC Awards have been pronounced. Three thereof were of interim nature while the 4th & 5th one were for 3-year period (i.e. 2005-06 to 2007-08 and 2008-09 to 2010-11). Through these Awards, the Local Governments received their due share from the net Divisible Pool. The inter-se distribution of Provincial Allocable Amount (Development and Non-Salary) in all the said interim Awards was made on the basis of following formula:-

1.	<i>Population</i>	50%
2.	<i>Backwardness(Based on MICS)</i>	25%
3.	<i>Lag in Infrastructure</i>	25%

2. At the 4th 3-year Award however, the said parameters were changed in terms of percentage as under:-

1.	<i>Population</i>	60%
2.	<i>Backwardness(Based on MICS)</i>	20%
3.	<i>Lag in Infrastructure</i>	20%

3. At the 5th PFC Award (2008-09 to 2010-11), the Commission continued to allow allocation/distribution of funds on the basis of aforesaid formula.

4. A brief summary of the Awards shows that Provincial Allocable Amount has gradually been increased since 2002 as under:-

Rs.in billion

i)	<i>1st PFC Award 2002</i>	15.162
ii)	<i>2nd PFC Award 2003</i>	16.098
iii)	<i>3rd PFC Award 2004</i>	18.773
iv)	<i>4th PFC Award 2005-2008</i>	29.412
iv)	<i>5th PFC Award 2008-2011</i>	32.248

CHAPTER-III

COMPOSITION OF PFC

The composition of PFC as per section 52 of the Khyber Pakhtunkhwa Local Government Act, 2013, is as under:-

S#	Composition	Designation
1.	Minister for finance Department	Chairman
2.	Minister for Local Government, Elections and Rural Development Department	Member
3.	Sami Ullah Alizai, MPA PK-65	Member
4.	Syed Muhammad Ali Shah, MPA PK-98	Member
5.	Secretary to Government, Finance Department	Member
6.	Secretary to Government, P&D Department	Member
7.	Secretary to Government, Local Government, Elections and Rural Development Department	Member
8.	Secretary to Government, Law, Parliamentary Affairs & Human Rights Department	Member
9.	Mr. Azizullah alizai, Nazim District Council, DI Khan.	Member
10.	Mr. Niaz Ahmad, Nazim District Council, Shangla.	Member
11.	Mr. Aslam Hayat Khan, Nazim Tehsil Council, Ghazi (Haripur)	Member
12.	Mr. Aizazullah, Nazim Tehsil Council, Serai Naurang (Lakki Marwat)	Member

Formal Notification is at **Annexure-I**.

CHAPTER-IV

FUNCTIONS OF THE COMMISSION

Under the provision of Section 53 of the Khyber Pakhtunkhwa Local Government Act, 2013 the functions of the Commission are as under:

- 1) The Finance Commission shall make recommendations to the Government on :
 - (a) the amount of grant for local governments out of the proceeds of Provincial Consolidated Fund in a financial year in addition to the grant in lieu of Octroi and Zilla Tax:

Provided that in addition to the establishment charges budgeted for the devolved functions and transfers in lieu of Octroi and Zilla Taxes, the development grant for local governments shall be so determined that it is not less than thirty percent of the total development budget of the province in the respective year.

- (b) formula for distribution of the grant among local governments in the province;

Provided that the development grant for village and neighbourhood councils shall be determined on the basis of population;

- (c) the amount of special grants for local governments with modalities and conditions to access the facility;
 - (d) grants in aid to local governments in need of assistance; and
 - (e) matters relating to local government finance.
- 2) While making recommendations, the Finance Commission shall take into account the principles of fiscal needs, fiscal capacity, fiscal efforts and fiscal performance of local governments.

- 3) The Finance Commission shall also take into consideration poverty, population, lag in infrastructure and revenue base of local governments as factors while formulating its recommendations.
- 4) The Finance Commission shall present to the Government annually a report on the analysis of fiscal transfers, the situation of own-source revenue in local governments and the reach and quality of their services and the Government shall cause the report to be laid before the Provincial Assembly.

CHAPTER-V

PFC RECOMMENDATIONS

PFC after taking into consideration the principles/ methodology expressed in Section 53(1)(a), (b) and (d), (2) and (3) of LGA, 2013 and due deliberations given in its 6th meeting held on 03.5.2016 have made the following recommendations for distribution of Provincial Allocable amount:

BASIC PRINCIPLES OF DISTRIBUTION OF RESOURCES BETWEEN PROVINCIAL AND LOCAL GOVERNMENTS

A. PROVINCIAL POOL

The Provincial Pool shall consist of the following items of revenue:

- i) Federal Tax Assignment
- ii) 1% of Divisible Pool for War on Terror.
- iii) Straight Transfers
- iv) GST on Services (Provincial)
- v) Provincial Own Receipts (Tax & Non Tax)
- vi) Net Profit from Hydel Power Generation
- vii) Arrears of Net Hydel Profit
- viii) Hydel Power Own Generation
- ix) Incentive bonus on cash balance

Details of the revenue budget are displayed at (**Annexure-II**)

B. OBLIGATORY EXPENDITURE

This being common to both Provincial and District Governments will be subtracted from the Provincial Pool for determination of the Divisible Pool and will comprise of the following items:

- (i) Debt Servicing
- (ii) Pension
- (iii) Subsidy
- (iv) Contribution to GP Fund and Pension Fund
- (v) Charged Expenditure (Governor's House/Secretariat, Provincial Assembly, High Court and Ehtisab Commission)
- (vi) Law and Order (Police)

C. DIVISIBLE POOL

The Divisible Pool will be the balance amount emerging as a result of subtracting the obligatory expenditure from the Provincial Pool.

D. SHARING PROCEEDS

The Divisible Pool will be shared between the Provincial and Local Governments as Provincial Retained Amount and Provincial Allocable amount at the ratio of 40:60 respectively. The Provincial Allocable Amount will be subject to fiscal needs, fiscal capacity, fiscal efforts & fiscal performance.

E. DISTRIBUTION OF PROVINCIAL ALLOCABLE AMOUNT

The Provincial Allocable Amount will be distributed amongst the Local Governments to meet the following expenditure:-

- i) *Salary*
- ii) *Non-Salary*
- iii) *Development*
- iv) *Grant to Local Councils*

F. FORMULA FOR INTER-SE DISTRIBUTION OF DISTRICT DEVELOPMENT FUNDS

The inter se distribution of District Development Share out of Provincial Allocable Amount shall be made on the basis of following formula to cater for development needs of the local governments:

- | | | |
|------|------------------------------|-----|
| i) | <i>Population</i> | 50% |
| ii) | <i>Poverty</i> | 25% |
| iii) | <i>Lag in Infrastructure</i> | 20% |
| iv) | <i>Revenue Base</i> | 5% |

G. TRANSFERS OF FUNDS TO LOCAL GOVERNMENTS

The Commission in its 6th meeting held on 03.5.2016 has made the following recommendations:

1) **Salary**

*It has proposed 5% annual incremental increase on the Revised Estimates (2015-16) for the devolved departments to cover the normal increase on account of annual increment during the next financial year 2016-17. With a view to allowing for anticipated increase in salary by the Federal Government and maintaining the level of indicative budgetary ceiling for each budget grant under the Medium Term Budgetary Framework (MTBF), the Provincial Finance Commission has recommended a lump sum provision/ block allocation of **Rs.10,255.476 million** in the next financial year 2016-17 so as to provide for a fiscal room in the budget/award.*

2) **Non-Salary**

Non-salary share has been proposed to be determined on the basis of 7.16% increase over the current year (2015-16) allocation in accordance with the indicative budgetary ceiling under MTBF to maintain over all fiscal discipline/ budgetary management. However, given the actual requirements of each district, a separate Block Allocation in respect of the following items of expenditure at district level has also been proposed:

(Rs. in million)

S#	Detail	Amount
i.	Provision of grant on need basis.	1000.000
ii.	Provision of Conditional Grant (Health & Education)	8000.204
iii.	Grant for Emergency Medicines in BHUs	425.000
iv.	Grant for M&R of WSS (PHE)	500.000
v.	Grant for Electricity Charges on need basis	500.000
vi.	Grant for Financial Assistance/Shuhada Packages	200.000
vii.	Grant for Advertisement Charges	20.000
viii.	Grant for Autonomy to HSS(Edu Sector)	600.000
ix.	Grant for Enrolment Campaign (E&SE)	12.000
x.	M&R of Roads and Buildings	500.000
Total:		11757.204

3) **Grant To Local Councils In Lieu Of Octroi & Zilla Tax**

The Grant in lieu of Octroi & Zilla Tax (OZT) equal to 1/6th of Sale Tax share of the Provincial Government out of the Federal Consolidated Fund has been discontinued by the Federal Government following the 7th NFC Award. Since then the Provincial Government has been providing share to Local Councils in lieu of OZT out of its own resources. Since provision of this grant has become a permanent liability for the provincial government, it has therefore, been renamed as “Grant to Local Councils” in the budget documents pertaining to financial year 2016-17 and will accordingly be reflected in the provincial budget so as to substitute it for the income previously derived from Octroi & Zilla Tax. To give legal cover to this arrangement and bring it in conformity with the Local Government Act, 2013, necessary amendments have been suggested through Finance Bill to be laid before the Provincial Assembly in the forthcoming budget session for financial year 2016-17.

i) Grant to TMAs

The historic share/grant to TMAs, District Councils and V.Cs/N.Cs has been proposed to be determined in the following manner:

- a) 10% increase over current year (2015-16) grant/share to TMAs in accordance with the indicative budgetary ceiling under MTBF.*
- b) A block provision of Rs.750.000 million has also been proposed for financially weak TMAs to be given on need basis. Local Govt. Department will evolve the mechanism for release/ transfer of such provision.*
- c) The historic share/collection of grant/share of Cantonment Boards (CBs) having share arrangement with adjacent TMAs shall continue to be transferred as usual.*

ii) Grant/share to District Councils, V.Cs & N.Cs

Given the actual needs of District Council Secretariat's staff, Village and Neighbourhood Councils on account of payment of salary, operational expenses, honorarium and other perks and privileges, the historic share of Zilla Tax in each District has been proposed to be determined on the basis of 24.15 % increase over the current year's allocation. The District Government will retain 20% share thereof while the remaining 80% share thereof will be transferred/released to the Designated Bank Account(s) of the V.Cs/N.Cs for utilization.

4) **District Development Share**

*Under the provision of Section 53 of LGA, 2013, the Development Grant to local governments shall not be less than 30% of the total development budget of the province in a respective year. The total Provincial ADP is **Rs.125.000 billion**. Out of this **Rs.12.200 billion** will be loan. It is worth pointing out that the provision of Section 53 of LGA, 2013 is not applicable to Loan. Similarly, **Rs.18.700 billion** of ADP will remain **dormant**, i.e. subject to actual materialization of resources. Consequently, the Provincial Government has allocated a sum of **Rs.33.900 billion** as District ADP. Out of this, **Rs.5.670 billion** will be subject to actual materialization of resources and **Rs.28.230 billion** will be transferable as District Development Grant to local governments to meet their requirements in the next financial year 2016-17. Local Council's tier-wise break up of District Development Funds is as under:*

(Rs. in billion)

S#	Provision for	B.Es 2016-17	Transferable
1	Districts	10.400	8.660
2	Tehsils (TMAs)	10.400	8.660
3	Village Councils/ Neighbourhood Councils	13.100	10.910
Total :		33.900	28.230

This distribution is subject to any relevant amendment in the Local Government Act, 2013.

Furthermore, the Commission has approved to continue the inter se distribution of District Development Funds on the basis of existing mechanism/previous PFC Awards (2008-09 to 2010-11) due to non-availability of district-wise data for determining factors under the approved formula.

*The detailed break-up of resources (Salary, Non-Salary, Development and Grant to Local Councils) intended to be transferred to Local Governments is exhibited at **Annex-III**.*

H. TERM OF THE AWARD

For want of necessary data, the Commission has recommended the present PFC Award for a term of **one year** (2016-17).

I. OTHER RECOMMENDATIONS

- i) In case of at-source deduction/adjustment from the revenue assignment of the Province by the Federal Government/PESCO on account of outstanding electricity charges against a District Government or Tehsil/Town Administration, proportionate at-source deductions will be made from the share of the respective District/Tehsil/Town Council. Further, in case any District Govt./Tehsil or Town Administration fails to make timely payment of monthly electricity dues to PESCO, Finance Department shall make such payment direct to PESCO and adjust the same amount against the District Government accounts. Similarly, such adjustments will also be made against the accounts of Tehsil/ Town Administration as the case may be.
- ii) In order to strengthen the Secretariat of Provincial Finance Commission in line with the spirit of Rule 3(1), (2) and (3) of Fiscal Transfer Rules, 2016, the Commission has also agreed to the creation of nine (9) additional posts during the next financial year 2016-17.

J. ACKNOWLEDGEMENT

The appreciation of PFC apart, the members of the Commission, officers and officials of the Finance Department need due vote of thanks in completion of this Award.

(Muzafar Said)
Minister for Finance
Government of Khyber Pakhtunkhwa,
**Chairman, Provincial Finance
Commission**

(Inayatullah Khan)
Minister for LGE&RD Dept
Government of Khyber Pakhtunkhwa
Member PFC

Secretary to Govt. of
Khyber Pakhtunkhwa
LGE&RD Department
Member PFC

Secretary to Govt. of
Khyber Pakhtunkhwa
P&D Department
Member PFC

Secretary to Govt. of
Khyber Pakhtunkhwa,
Law Department
Member PFC

(Sami Ullah Alizai)
MPA PK-65
Member PFC

(Syed Muhammad Ali Shah)
MPA PK-98
Member PFC

(Azizullah Alizai)
Nazim District Council
D.I.Khan
Member PFC

(Niaz Ahmad)
Nazim District Council
Shangla
Member PFC

(Aslam Hayat)
Nazim Nazim Tehsil
Council, Ghazi (Haripur)
Member PFC

(Aizazullah)
Nazim Tehsil Council, Serai
Naurang (Lakki Marwat)
Member PFC

Secretary to Govt. of Khyber Pakhtunkhwa,
Finance Department
Secretary/Member PFC



Annexure-I

**GOVERNMENT OF KHYBER PAKHTUNKHWA
LOCAL GOVERNMENT, ELECTION & RURAL
DEVELOPMENT DEPARTMENT**

Dated Peshawar, the 15th of October, 2015

NOTIFICATION

No. SO(LG-DLGC/4-116/2015): In pursuance to the provisions contained in Section 51 of the Khyber Pakhtunkhwa Local Government Act, 2013, the competent authority has been pleased to constitute the following Provincial Finance Commission with immediate effect to carry out its mandated functions and responsibilities provided in Chapter XI (Section 52 and 53) of the Khyber Pakhtunkhwa Local Government Act, 2013:

S#	Composition	Designation	Name of Member
13.	Minister for finance Department	Chairman	Mr. Muzafar Said, Ex-Officio
14.	Minister for Local Government, Elections and Rural Development Department	Member	Mr. Inayat Ullah Khan, Ex-Officio
15.	MPA nominated by the Chief Minister	Member	Sami Ullah Alizai, MPA PK-65
16.	MPA nominated by the Leader of Opposition in the Provincial Assembly	Member	Syed Muhammad Ali Shah, MPA PK-98
17.	Secretary to Government, Finance Department	Member	Mr. Ahmad Hanif Orakzai, Ex-Officio
18.	Secretary to Government, P&D Department	Member	Syed Zafar Ali Shah, Ex-Officio
19.	Secretary to Government, Local Government, Elections and Rural Development Department	Member	Syed Jamal ud Din Shah, Ex-Officio
20.	Secretary to Government, Law, Parliamentary Affairs & Human Rights Department	Member	Mr. Muhammad Arifeen, Ex-Officio
21.	Elected Nazim District Council	Member	Mr. Azizullah Alizai, Nazim District Council, DI Khan.
22.	Elected Nazim District Council	Member	Mr. Niaz Ahmad, Nazim District Council, Shangla.
23.	Elected Nazim Tehsil Council	Member	Mr. Aslam Hayat Khan, Nazim Tehsil Council, Ghazi (Haripur)
24.	Elected Nazim Tehsil Council	Member	Mr. Aizazullah, Nazim Tehsil Council, Serai Naurang (Lakki Marwat)

Note: Finance Department shall provide secretariat support and render assistance to the Provincial Finance Commission.

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Secretary, LGE&RDD

Copy endorsed with even No. and date:

- 1) Accountant, Khyber Pakhtunkhwa.
- 2) Principal Secretary to the chief Minister, Khyber Pakhtunkhwa.
- 3) Principal Secretary to the Governor, Khyber Pakhtunkhwa.
- 4) All Administrative Secretaries in Khyber Pakhtunkhwa.
- 5) PA to Secretary Provincial Assembly, Khyber Pakhtunkhwa.
- 6) All Members of Provincial Finance Commission, Khyber Pakhtunkhwa.
- 7) Director Information, Government of Khyber Pakhtunkhwa.
- 8) All commissioners in Khyber Pakhtunkhwa.
- 9) All Heads of the Attached Departments in Khyber Pakhtunkhwa.
- 10) All Nazimeen, District Governments in Khyber Pakhtunkhwa.
- 11) All Deputy Commissioners in Khyber Pakhtunkhwa.
- 12) PSO to Chief Secretary, Khyber Pakhtunkhwa.
- 13) All Nazimeen, Tehsil Councils in Khyber Pakhtunkhwa.
- 14) PS to Additional Chief Secretary, P&D Dept, Khyber Pakhtunkhwa.
- 15) PS to Senior Minister, LGE&RDD, Khyber Pakhtunkhwa.
- 16) PS to Special Secretary, LGE&RDD, Khyber Pakhtunkhwa.
- 17) PA to Director General, LG&RDD, Khyber Pakhtunkhwa.
- 18) PA to Secretary, Local Council Board, Khyber Pakhtunkhwa.
- 19) All Assistant Directors, LG&RD in Khyber Pakhtunkhwa.
- 20) All Tehsil Municipal Officers, Khyber Pakhtunkhwa.
- 21) Manager Government Printing Press, Peshawar for publication in official Gazette.
- 22) Office Record.

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Section Officer(Establishment)
LGE&RDD

Annexure-II

**STATEMENT SHOWING PROVINCIAL CONSOLIDATED FUND & ITS
DISTRIBUTION FOR THE YEAR 2015-16 & 2016-17**

(Rs.in
Million)

S#	Component	B.Es 215-16	R.E. 2015-16	B.E. 2016-17
A) Provincial Pool				
1	Revenue Assignment from Federal Divisible Pool	250,892.750	251,651.071	293,694.328
2	1% of Divisible Pool for war on terror	30,146.555	30,237.675	35,289.471
3	Straight Transfers	19,412.863	19,373.493	17,199.980
4	GST on Services (Provincial)	14,000.000	8,000.000	10,000.000
5	Provincial Own Receipts (Tax & Non Tax)	37,124.790	14,181.000	35,877.000
6	Net Profits from Hydel Power (Uncapping of NHP)	17,000.000	9,000.000	18,704.000
7	Arrears of Net Hydel Profit	51,873.042	25,000.000	15,000.000
8	Hydel Power Own Generation	3,300.000	3,300.000	3,630.000
9	Incentive Bonus on Cash Balance	2000.000	1197.683	300.000
Total-A		425,750.000	361,940.922	429,694.779
B) Obligatory Expenditure				
1	Debt Servicing Mark-up			
	(i) Mark-up (interest)	13,000.000	8,000.000	13,000.000
	(ii) Principal Amount	14,910.000	14,910.000	10,910.000
Total=		27,910.000	22,910.000	23,910.000
2	Pension	36,993.025	36,993.025	40,905.310
3	Subsidy on Wheat	2,900.000	2,900.000	2,900.000
4	Contribution to G.P. Funds	4,000.000	4,000.000	4,000.000

5	Hydel Development Fund	3,000.000	1,000.000	3,000.000
6	(Home,Police & Civil Defence)	34,194.079	35,179.347	34,488.308
7	Charge Expenditure(Provincial Assembly High Court Governor House/Secretariat and Ihtisab Commission).	2,698.414	2,669.660	2,757.095
Total		111,695.518	105,652.032	111,960.713
C) Divisible Pool				
1	Provincial Pool	405,750.000	361,940.922	429,694.779
2	Provincial Obligatory Expdr:	111,695.518	105,652.032	123,960.713
Net Divisible Pool (A-B)		314,054.482	256,288.890	305,734.066
	i) Provincial Allocable Amount (60%)	188,432.689	153,773.334	183,440.440
	ii) Provincial retained Amount (40%)	125,621.793	102,515.556	122,293.626
D) Amount Allocated to Districts				
	i) Salary	92,554.756	90,935.350	112,584.605
	ii) Non-Salary	5,302.777	10,726.811	17,440.064
	iii) Development	30,274.000	15,491.495	33,900.000
	iii) Grant to Local Councils	4,526.269	5,424.136	4,715.849
Total		132,657.802	122,577.792	168,640.518
%age of Divisible Pool		44.24%	47.83%	55.16%