Borrowing Powers under Article 160: A Forgotten Mandate of Pakistan's NFC Awards

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Pakistan's inter-governmental fiscal system has evolved over more than seven decades, shaped by historical legacies, constitutional reforms, and the political economy of federalism. The National Finance Commission (NFC) is at the heart of this system, tasked under Article 160 of the 1973 Constitution with ensuring equitable distribution of resources between the federal and provincial governments. While the NFC has made significant strides in addressing revenue-sharing issues, a critical dimension borrowing powers has been consistently neglected, despite its explicit inclusion in the constitutional framework *(Ahmed & Ahmad, 2016)*. The consequences of this omission are profound.

Pakistan today faces one of the highest public debt burdens in its history, accompanied by persistent fiscal deficits, limited tax revenues, and deep intergovernmental imbalances that strain the country's fiscal federalism *(IMF, 2023)*. This fiscal stress has created challenges in sustaining economic growth, financing development projects, and maintaining macroeconomic stability. Understanding how this situation evolved requires tracing the historical trajectory of the National Finance Commission (NFC) and examining the reasons why borrowing a constitutionally mandated agenda item under Article 160 has been consistently overlooked in successive NFC Awards.

To fully grasp why borrowing remains excluded from the NFC's deliberations, it is essential to first review Pakistan's early fiscal history and the evolution of its revenue-sharing mechanisms. These initial arrangements not only shaped the intergovernmental fiscal landscape but also entrenched patterns of dependency and centralization that continue to influence fiscal relations today.

Early Revenue-Sharing Arrangements (Pre-1973)

In the immediate aftermath of independence in 1947, Pakistan had no formal institutional mechanism for the equitable allocation of fiscal resources between the federation and the provinces. Initially, the country operated under an ad hoc arrangement based on the Niemeyer Award (1937). Under this arrangement, sales tax was treated as a provincial subject, while 50% of federal income tax collections were redistributed among the provinces. Pakistan inherited a highly centralized financial structure from British India, where most taxation and revenue powers were concentrated at the federal level, leaving the provinces dependent on federal transfers to meet their basic expenditure needs.

As a result, provincial governments were heavily dependent on federal transfers to meet their basic functional responsibilities, including education, healthcare, policing, and infrastructure development (*Khan, 2017)*. During this early period, ad hoc arrangements such as the Raisman Award of 1947 (implemented in 1952) and subsequent adjustments in the 1960s were introduced to distribute limited tax revenues. However, these arrangements focused exclusively on revenue sharing and did not establish a sustainable framework for fiscal autonomy or coordination between federal and provincial governments, laying the groundwork for the fiscal imbalances that persist today.

Raisman Award and Ad Hoc Grants

One of the first attempts to address fiscal disparities was the Raisman Award of 1947, implemented in 1952. This award provided a framework for distributing certain federal tax revenues among the provinces. Its key features included:

- Allocation of shares based almost entirely on population, favoring Punjab due to its demographic dominance.
- Provision of grants-in-aid to smaller provinces such as Balochistan to compensate for their weaker fiscal capacity.
- Central government control over major taxes such as customs duties and corporate income tax (*World Bank, 2019*).

Despite its significance, the Raisman Award was limited in scope, focusing narrowly on tax distribution. Borrowing was not considered relevant because:

- The federal government retained exclusive control over both domestic and external debt management.
- Provinces lacked institutional capacity to manage debt independently.
- The political context of the time emphasized state-building and national security, leaving little room for provincial fiscal autonomy *(Waseem, 2010)*.

Centralization and Fiscal Dependence

Throughout the 1950s and 1960s, Pakistan's fiscal framework remained highly centralized. Provinces relied almost entirely on federal transfers to fund their budgets. This dependence created vertical fiscal imbalances, where expenditure responsibilities were devolved to provinces without corresponding revenue powers *(Ahmed et al., 2020)*. Borrowing remained a federal monopoly, with provinces playing a minimal role in debt management. Consequently, subnational borrowing was never debated as a policy issue. This early pattern of centralization set the stage for future tensions over fiscal autonomy and resource distribution.

Constitutional Embedding of the NFC and Borrowing

The adoption of the 1973 Constitution marked a transformative moment for Pakistan's fiscal federalism. It was designed to address historical grievances by providing provinces with greater financial autonomy and creating mechanisms for equitable sharing of resources.

Establishment of the NFC

Article 160 of the Constitution formally established the National Finance Commission (NFC). It mandates that the President convene the NFC every five years (or earlier) to review and recommend new arrangements for intergovernmental finance *(Government of Pakistan, 1973, Art. 160)*. Article 160(2) outlines four specific areas for NFC recommendations:

1. Distribution of specified federal taxes between the federation and provinces.
2. Grants-in-aid to provincial governments.
3. The exercise of borrowing powers by the federal and provincial governments.
4. Any other financial matter referred by the President.

The explicit inclusion of borrowing in Article 160(2)(c) reflects a forward-looking vision of fiscal coordination. It acknowledges that debt management is as crucial to fiscal sustainability as tax allocation *(Rana, 2019)*.

Borrowing Provisions in the Constitution

In addition to Article 160, other constitutional provisions detail how borrowing is to be conducted:

- **Article 166:** Governs federal borrowing, allowing the federal government to raise loans secured by the Federal Consolidated Fund.
- **Article 167:** Governs provincial borrowing. Historically, provinces were restricted to domestic borrowing only.

The 18th Constitutional Amendment (2010) introduced Article 167(4), allowing provinces to borrow internationally within limits set by the National Economic Council (NEC) or federal law (*Government of Pakistan, 2010, Art. 167(4)*). This architecture theoretically empowers provinces while ensuring coordinated debt management through the NFC. In practice, however, borrowing remains governed by separate legal frameworks, with no role played by the NFC.

Evolution of NFC Awards: Exclusive Focus on Revenue

Since 1973, seven NFC Awards have been announced, each reflecting the political and economic dynamics of its time. While these awards have progressively improved revenue-sharing formulas, they have entirely ignored borrowing powers, leaving a critical constitutional mandate unfulfilled (*Ahmed & Ahmad, 2016*).

First NFC Award (1974)

The first NFC Award laid the foundation for Pakistan's modern fiscal framework:

- Introduced the concept of a divisible pool of federal taxes.
- 20% retained by the federation, 80% allocated to provinces, with intra-provincial distribution based solely on population *(Khan, 2017)*.
- Focused exclusively on tax sharing, ignoring borrowing entirely.

Fourth NFC Award (1990)

The fourth NFC Award expanded the divisible pool and included direct transfers, such as net hydropower profits to provinces. It sought to correct fiscal disparities but continued the pattern of neglecting borrowing powers *(World Bank, 2019)*.

Fifth NFC Award (1997)

The fifth NFC Award raised provincial shares to 50% and introduced incentives for provincial revenue mobilization *(Rana, 2019)*. Despite these progressive reforms, no mechanism was introduced for managing provincial borrowing.

Seventh NFC Award (2010) and the 18th Amendment

The 7th NFC Award represented a landmark in Pakistan's fiscal history:

- Increased provincial shares to 56% in 2010-11, rising to 57.5% thereafter.
- Introduced a multi-factor formula for intra-provincial distribution:
  1. Population – 82%
  2. Poverty/backwardness – 10.3%
  3. Revenue effort – 5%
  4. Inverse population density – 2.7%

Simultaneously, the 18th Amendment devolved significant powers to provinces and allowed them to borrow internationally. However, no framework for borrowing coordination was embedded in the NFC Award, resulting in a disconnect between revenue allocation and debt responsibilities.

Legal and Fiscal Implications of Excluding Borrowing

Legal Implications

The omission of borrowing from NFC deliberations has profound legal consequences:

1. **Violation of Constitutional Mandate:**
   - Article 160 uses the word "shall", creating a mandatory obligation for the NFC to address borrowing powers *(Ahmed & Ahmad, 2016)*.
   - By ignoring this mandate, successive NFCs have failed to implement the Constitution fully.
2. **Fragmented Debt Governance:**
   - Federal borrowing is managed through the Fiscal Responsibility and Debt Limitation (FRDL) Act 2005, which sets targets for debt sustainability *(Ministry of Finance, 2023)*.
   - Provincial borrowing remains governed by Article 167, with the federal government retaining veto power over provinces that owe debts to the center.
3. **Absence of Judicial Oversight:**
   - No judicial challenge has been raised to enforce Article 160(2)(c), reflecting the political sensitivity of debt issues and the reluctance of courts to intervene.

In a recent episode of Pakistan's fiscal governance, it is worth pondering that the explicit mention of borrowing in the Terms of Reference (ToRs) of the 10th and 11th National Finance Commissions (NFCs) represents a significant acknowledgement of the constitutional mandate enshrined in Article 160 of the 1973 Constitution of Pakistan. Article 160 clearly stipulates that the NFC is responsible for making recommendations not only on the distribution of federal taxes and grants-in-aid but also on the exercise of borrowing powers by both federal and provincial governments. Historically, earlier NFC Awards particularly the landmark 7th NFC Award of 2010 completely overlooked borrowing, focusing exclusively on revenue-sharing mechanisms. The inclusion of borrowing in the ToRs of subsequent NFCs was, therefore, a positive and much-needed development, reflecting a recognition that coordinated borrowing is integral to achieving fiscal federalism and macroeconomic stability.

However, this inclusion has largely remained symbolic rather than substantive. The 10th NFC[1] failed to produce any concrete recommendations, leaving the matter unresolved, while the deliberations of the 11th NFC are still ongoing. From a legal and constitutional standpoint, the explicit reference to borrowing in the ToRs reinforces that this matter is not discretionary, but rather a constitutional obligation of the NFC. Failure to address borrowing through a coherent framework represents a breach of the constitutional intent behind Article 160. The Constitution envisioned the NFC as a collaborative mechanism for federal-provincial financial coordination, ensuring that both tiers of government act within a unified fiscal strategy.

1 The 8th, 9th, and 10th NFCs all remained inconclusive and did not result in a finalized award.

By neglecting this mandate, successive NFCs have inadvertently contributed to structural fiscal imbalances, growing public debt, and intergovernmental disputes over resource allocation. Thus, moving forward, borrowing must be treated as a central pillar of NFC deliberations, with a formula-based, equitable approach that safeguards the interests of all provinces and strengthens Pakistan's overall fiscal governance.

Recommended Reforms for Pakistan

To effectively modernize Pakistan's fiscal federalism, the National Finance Commission (NFC) must evolve beyond traditional revenue-sharing to include borrowing coordination and allocation mechanisms. This will help prevent macroeconomic instability and ensure that national borrowing contributes equitably to sustainable development. The following reforms are proposed:

1) Integration of Borrowing Policies into NFC Awards

Borrowing should be a regular agenda item of every NFC Award, as envisaged under Article 160 of the Constitution. A structured framework must be established to:

- Set joint debt ceilings for both the federal and provincial governments, ensuring compliance with a coordinated macroeconomic strategy.
- Synchronize domestic and external borrowing, preventing duplication of efforts and reducing risks of unsustainable debt accumulation.
- Require that borrowing decisions align with national development priorities while respecting provincial fiscal autonomy.

2) Formula-Based Allocation of Borrowing for Development Projects

A formula-based allocation mechanism, similar to the existing NFC revenue-sharing formula, should be developed for domestic and foreign borrowings.

- Borrowing proceeds should be specifically earmarked for development projects that generate long-term economic and social benefits for all provinces.
- The minimum allocation for each province must not fall below its NFC revenue share percentage, ensuring fairness and avoiding fiscal imbalances.
- This allocation will be reviewed and reset every five-year NFC cycle, aligning with development planning and fiscal sustainability objectives.
- Projects of national interest, such as defense, strategic infrastructure, or climate resilience, should be financed separately and excluded from the divisible borrowing pool.

Example:

If a province has a 20% NFC share, at least 20% of total development-related borrowing must be allocated to projects directly benefiting that province.

Conclusion

By integrating borrowing into the NFC framework through a formula-based, equitable allocation system, Pakistan can:

- Ensure that all provinces benefit proportionately from national borrowing.
- Promote fiscal discipline and macroeconomic stability.
- Enhance transparency through independent monitoring and performance-linked incentives.

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