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INTERGOVERNMENTAL TAXATION AND INDUSTRIAL DISRUPTIONS: DECONSTRUCTING THE CONSTITUTIONAL AUTHORITY OVER STATE-IMPOSED GREEN ENERGY CESS IN INDIA

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INTERGOVERNMENTAL TAXATION AND INDUSTRIAL DISRUPTIONS: DECONSTRUCTING THE CONSTITUTIONAL AUTHORITY OVER STATE-IMPOSED GREEN ENERGY CESS IN INDIA

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Abstract

Green Energy Cess has emerged as a prominent fiscal instrument as a policy instrument aimed at promoting sustainable energy practices and reducing carbon emissions. This research paper examines the legal and economic implications of levying a cess on carbon-intensive industries to finance renewable energy projects. It explores the legislative framework governing green cess in different jurisdictions, assessing its effectiveness in mitigating environmental degradation and accelerating the shift to clean energy sources. The study further highlights challenges such as regulatory loopholes, industry resistance, and the efficient allocation of collected funds. Through case studies of countries that have successfully implemented green cess policies, the research identifies best practices and potential areas for improvement. Additionally, an economic impact assessment is conducted on the effect of green cess on businesses, consumers, and overall market stability. The study proposes recommendations for optimising the cess structure to ensure compliance, transparency, and environmental sustainability by employing a comparative approach. The findings underscore the necessity of a well-structured and effectively regulated Green Energy Cess to achieve long-term climate goals while balancing economic growth.

Keywords: Green Energy Cess, Carbon Emissions, Renewable Energy, Environmental Taxation, Sustainable Development.

I

Introduction

Green energy, also known as renewable energy, is energy generated from natural sources such as sunlight, wind, water, and biomass. These sources are sustainable, environmentally friendly, and reduce dependence on fossil fuels. The significance of green energy lies in its ability to mitigate climate change, reduce pollution and promote energy security. With global commitments towards carbon neutrality, India has been actively promoting green energy through policy frameworks and fiscal incentives[1].

The Rise of Environmental Taxation & Fiscal Policies

Environmental taxation is a policy tool to encourage sustainable practices while discouraging environmentally harmful activities. The government has introduced various taxes, levies, and cess mechanisms in India to promote green energy and discourage pollution. Examples include the coal cess (later subsumed under the GST compensation cess) and renewable energy purchase obligations.[2]

Fiscal policies, including tax incentives, subsidies, and levies, are crucial in steering industrial development towards sustainability. By providing tax benefits for renewable energy projects and imposing environmental cess on polluting industries, the government fosters a shift towards cleaner technologies[3].

II

Constitutional and Legal Framework of Taxation in India

The Indian Constitution provides a structured framework for taxation through the Union List, State List, and Concurrent List in the Seventh Schedule. The division of taxation powers ensures that both the Centre and States have distinct roles in revenue collection, facilitating economic governance while maintaining fiscal federalism[4].

Article 246 of the Indian Constitution divides legislative powers between the Union and the States through the Seventh Schedule. The three lists under this schedule determine the subjects on which the Centre and States can levy taxes:

i. Union List (List I): Taxes exclusively levied by the Central Government (e.g., income tax, excise duty, customs duty).

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[1] IEA, RENEWABLE ENERGY MARKET REPORT 10 (2021).
[2] NITI Aayog, SUSTAINABLE ENERGY POLICIES IN INDIA 14 (2020).
[3] Ministry of Finance, ECONOMIC SURVEY 2020-21 6 (2021).
[4] Sanjay Chaturvedi, INDIAN FISCAL FEDERALISM 45 (Oxford Univ. Press 2019).

ii. State List (List II): Taxes levied by State Governments (e.g., state excise, land revenue, stamp duty).

iii. Concurrent List (List III): Subjects on which both the Centre and States can legislate (e.g., contracts, bankruptcy, marriage laws). However, taxation is primarily absent from this list[5].

Specific Entries Related to Taxation

Entry 52 of the State List: Allows States to impose taxes on goods entering local areas (i.e., entry tax, octroi). Entry 53 of the State List: Empowers States to impose taxes on electricity generation, distribution, and consumption. Further, Entry 97 of the Union List: Provides the Central Government with the power to levy taxes on matters not enumerated in the State or Concurrent Lists, ensuring legislative flexibility.

III

Interpretation of Cess and Its Distinction from Tax, Duty, and Fee

Tax, which is a compulsory financial charge imposed by the government for revenue generation, is distinct from a fee and a duty. A cess is a tax imposed for a specific purpose, collected as an additional levy on existing taxes. Unlike general taxation, which funds overall government expenditures, a cess is earmarked for particular objectives such as education, health or green energy development. Whereas a fee is a charge for a specific service rendered by the government (e.g., court fees, registration fees).

The judiciary has played a crucial role in clarifying the constitutional validity of cess imposition. In *Jindal Stainless Ltd. v. State of Haryana,*[6] Supreme Court upheld the power of States to impose entry tax, emphasising the constitutional limitations on taxing powers. The judgment clarified that taxation should not impede free trade and commerce under Article 301 of the Constitution.

Role of the GST Framework in Regulating State-Imposed Levies

The introduction of the Goods and Services Tax (GST) in 2017 marked a paradigm shift in India's taxation structure. GST subsumed multiple indirect taxes previously

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[5] P.M. Bakshi, THE CONSTITUTION OF INDIA 110 (Universal Law Publ'g 2020).

[6] Jindal Stainless Ltd. v. State of Haryana, A.I.R. 2016 S.C. 5617 (India).

imposed by both the Centre and States, thereby reducing tax complexities and improving compliance. The GST Compensation Cess, initially introduced to compensate States for revenue loss post-GST implementation, was also used to fund green energy initiatives. States are restricted from imposing additional levies outside the GST framework, except for items excluded from GST (e.g., petroleum, alcohol).

IV

Green Energy Cess—Rationale, Implementation, and State Practices

Green Energy Cess (GEC) is a financial charge levied by state governments in India to support the transition to sustainable energy. The cess primarily aims to promote the adoption of renewable energy sources such as solar, wind, and hydroelectric power by creating funds dedicated to research, development, and infrastructure for renewable energy[7]. In essence, the Green Energy Cess is designed to address the pressing need for decarbonising the energy sector, reducing dependence on fossil fuels, and fostering energy independence in the country[8]. It is also a mechanism for generating resources to fund state-level initiatives aimed at climate change mitigation and the development of green technologies.

In India, the overarching objective of the Green Energy Cess is to align with global climate goals, especially in the context of India's commitment under the Paris Agreement to reduce carbon emissions[9]. The funds collected through the cess are often channelled into renewable energy projects, including the construction of solar parks, wind energy infrastructure and the promotion of electric mobility. This approach not only helps mitigate climate change but also facilitates the creation of jobs and boosts economic growth in the renewable energy sector[10].

Case Studies of States Imposing Green Energy Cess

Several Indian states have introduced their own versions of the Green Energy Cess as a means of financing green energy projects. These state-specific initiatives differ in terms of implementation, the sectors targeted and the scale of the cess.

[7] MNRE, NATIONAL POLICY ON RENEWABLE ENERGY 5 (2023).
[8] Shubham Gupta & Radhika Agarwal, "Challenges in Implementing Green Energy Cess in Indian States", 20 INT'L J. SUSTAINABLE DEV. 150-167 (2019).
[9] Ministry of Power, ANNUAL REPORT ON POWER SECTOR 12 (2022).
[10] Vinay Bansal & Mahima Verma, RENEWABLE ENERGY AND LEGAL FRAMEWORK IN INDIA 59 (Oxford Univ. Press 2021).

Jharkhand's Green Energy Cess

Jharkhand, a state rich in mineral resources, has been proactive in introducing the Green Energy Cess[11]. The state has imposed a cess on power consumers in an effort to promote renewable energy adoption and reduce the reliance on coal-fired power plants. Jharkhand's Green Energy Cess is aimed at supporting the state's renewable energy infrastructure, particularly solar and wind energy projects. The revenue generated from this cess is allocated towards subsidizing the cost of renewable energy production, thereby making it more accessible to industries and consumers[12]. Jharkhand's move has been particularly significant given its status as a coal-rich state, as it seeks to transition towards a more sustainable and diversified energy mix.

Karnataka's Renewable Energy Levy

Karnataka, one of the leaders in renewable energy development in India, has also implemented a Renewable Energy Levy, akin to a Green Energy Cess[13]. The levy is imposed on electricity consumers to support the state's ambitious renewable energy goals. Karnataka has been a forerunner in wind and solar energy projects, and the revenue from this levy is earmarked for funding further expansion in these sectors. Karnataka's Renewable Energy Levy is seen as a strategic measure to ensure financial sustainability for renewable energy projects, thus enabling the state to maintain its leadership position in India's green energy landscape[14].

Policy Justifications for Green Energy Cess

The policy rationale behind imposing a Green Energy Cess can be understood from various perspectives, with a focus on climate change mitigation, funding renewable energy projects and generating state revenue.

Climate Change Mitigation

India, being one of the largest emitters of greenhouse gases globally, faces significant environmental challenges, including rising air pollution and climate change-

[11] Government of Jharkhand, JHARKHAND GREEN ENERGY CESS POLICY 3 (2021).
[12] Gupta & Agarwal, supra note 8, at 160.
[13] KARNATAKA RENEWABLE ENERGY LEVY ACT, 2022, S. 4 (Karnataka State Gov't).
[14] Indian Renewable Energy Development Agency (IREDA), GREEN ENERGY FINANCING AND CESS IN INDIA: AN OVERVIEW 18 (2023) [hereinafter IREDA Report].

induced risks[15]. A Green Energy Cess serves as a tool to help mitigate the adverse effects of climate change by incentivising the shift from conventional fossil fuels to cleaner, renewable energy sources. This move aligns with the broader global agenda of reducing carbon footprints and contributing to global climate action initiatives[16].

Renewable Energy Funding

The primary purpose of the Green Energy Cess is to create a dedicated pool of funds to finance renewable energy projects. As renewable energy technologies tend to have higher initial capital costs, the cess helps bridge the financial gap by providing subsidies and incentives for the development and scaling up of such projects. This is particularly critical in the context of India's energy needs, where a significant portion of the population still lacks reliable access to electricity, and renewable energy can serve as a viable solution.

State Revenue Generation

From a fiscal perspective, the Green Energy Cess as a revenue-generation mechanism for state governments. This is particularly relevant in a country like India, where states are responsible for energy procurement and distribution[17]. The cess helps create a more sustainable revenue stream that can be reinvested into green energy projects, thereby not only fostering environmental sustainability but also ensuring the financial health of state-run energy companies[18].

Inter-State Variations and Their Implications for Industries

Implementing the Green Energy Cess in India is not uniform across states, leading to variations in how industries are impacted. States such as Karnataka, Gujarat, and Rajasthan have relatively more developed renewable energy sectors and impose cesses with a focus on further incentivizing growth in this area. On the other hand, states like Jharkhand and Chhattisgarh, with their heavy dependence on coal and traditional energy sources, may have a more cautious approach to the cess, focusing on balancing environmental goals with economic and energy security concerns.

The variation in Green Energy Cess across states can create a competitive landscape for industries, particularly energy-intensive industries, such as manufacturing,

[15] MNRE, supra note 7, at 9.
[16] Anil Kumar & Priya Sharma, Impact of Green Energy Cess on State Fiscal Policies in India, 48 J. ENERGY POL'Y 275, 278 (2020).
[17] Ministry of Power, supra note 9, at 25.
[18] IREDA Report, supra note 14, at 22.

mining and heavy industries. Some industries in states with higher cess rates may find their cost of production increasing, while those in states with lower cess rates may benefit from more competitive energy pricing. Furthermore, interstate variations can lead to issues of resource allocation and equity, especially when industries can relocate or shift operations to states with more favourable energy policies.

Industries that are heavily reliant on traditional energy sources may also face challenges in states where renewable energy policies are more aggressive. These industries might be subject to higher cesses, potentially increasing their operational costs. However, this can also serve as a catalyst for innovation and the adoption of cleaner technologies, pushing industries towards more sustainable practices.[19]

Legal Challenges Faced by State-Imposed Green Energy Cesses

State-imposed Green Energy Cesses have faced a range of legal challenges, primarily due to concerns over constitutional authority, the impact on industries and the fairness of such charges.

One of the most significant legal challenges to Green Energy Cess is related to the distribution of powers between the central and state governments. The imposition of a cess on energy consumption and production may be contested on the grounds that it interferes with the central government's control over energy policy. Industry associations and stakeholders have raised concerns that such state-level cesses might create inconsistencies and lead to conflicting policies, especially when it comes to interstate trade and commerce. There have been instances where state-imposed cesses were challenged in courts, arguing that they were beyond the scope of state jurisdiction or violated the principles of federalism.

Impact on Industries

Another legal challenge faced by Green Energy Cess is the impact on businesses, especially those operating in energy-intensive sectors. Many industries argue that the imposition of such cesses places an undue burden on their operations, especially in states where the cess is relatively high. This has resulted in several legal petitions seeking relief from the cess, claiming that it disproportionately affects certain sectors, leading to higher costs of production and reduced competitiveness.

Fairness and Transparency

[19] Gupta & Agarwal, supra note 8, at 165.

Legal disputes have also arisen over the transparency and accountability of how the cess funds are utilized. Some businesses have raised concerns about the lack of clear guidelines on how the funds are allocated and whether they are truly directed towards green energy projects. In some cases, industries have sought judicial intervention to ensure that the funds collected through the cess are used efficiently and do not result in unjustified financial strain on the industries that contribute to it.

V

Industrial Impact of Green Energy Cess

The implementation of the Clean Energy Cess on coal production in India precipitated a significant escalation in production costs for industries whose operations are heavily dependent on coal-based energy[20]. Initially levied at INR 50 per tonne in 2010 and subsequently increased to INR 400 per tonne by 2016[21], the cess exerted a direct financial strain on energy-intensive sectors such as steel, cement, and chemicals. The resultant rise in production expenditures inflated input costs and constricted profit margins, thereby undermining the global competitiveness of Indian manufacturers.

With the introduction of the Goods and Services Tax (GST) in 2017, the Clean Energy Cess was supplanted by the GST Compensation Cess, perpetuating the financial encumbrance on affected industries[22]. Although originally conceived as a fiscal mechanism to fund clean energy initiatives, a substantial proportion of the revenue was redirected towards other governmental priorities[23], attenuating its efficacy in fostering renewable energy development. The concomitant surge in production costs has adversely affected India's positioning in global markets, diminishing the competitiveness of exports and deterring investment in energy-intensive manufacturing enterprises.

Sectoral Analysis: Impact on Energy-Intensive Industries

[20] Ministry of Finance, UNION BUDGET 2010-11: INTRODUCTION OF CLEAN ENERGY CESS 2 (2010).
[21] Ministry of Finance, UNION BUDGET 2016-17: REVISION OF CLEAN ENERGY CESS 3 (2016).
[22] IEA, INDIA ENERGY OUTLOOK 2021 20 (2021).
[23] RBI, FINANCIAL STABILITY REPORT: RENEWABLE ENERGY INVESTMENTS IN INDIA 30 (2022).

The imposition of the Clean Energy Cess (CEC) on coal production has had profound implications for India's energy-intensive industries, most notably steel, cement, aluminium, and chemicals[24]. Collectively classified as heavy industries, these sectors constitute a substantial proportion of the nation's total industrial energy consumption and carbon emissions. The exacerbation of fossil fuel-based electricity costs attributable to the CEC has significantly augmented production expenditures, thereby eroding the competitive standing of domestic manufacturers in international markets.

Steel and cement, as major contributors to industrial emissions, have been particularly affected, given the energy-intensive nature of their production processes[25]. The European Union's Carbon Border Adjustment Mechanism (CBAM) has further intensified pressure on Indian steel and cement producers, necessitating a reduction in carbon emissions to mitigate the risk of trade barriers.[26] The aluminium industry, which is heavily reliant on electricity has also encountered substantial operational impediments due to escalating energy costs. While a considerable proportion of its electricity demand could potentially be met through renewable sources, the transition necessitates extensive capital investment and infrastructural modifications. To address these challenges the expansion of green electrification and the accelerated adoption of renewable energy sources are imperative. Research suggests that fulfilling the electricity demand of heavy industries through renewable energy could potentially curtail CO_2 emissions by up to 180 million tonnes by 2030[27]. However, achieving this transition necessitates an estimated 120 GW of additional renewable capacity.[28] Despite concerted policy initiatives, industries continue to grapple with exorbitant electricity tariffs and infrastructural deficiencies, impeding the pace of decarbonisation.

Supply Chain Disruptions and Regional Disparities

The shift towards clean energy has introduced substantial complexities within both global and regional supply chains, particularly affecting industries with a heavy dependence on fossil fuels. Supply chain fragilities, including shortages of essential raw materials, protracted project timelines, and disproportionate regional

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[24] Ministry of Steel, ANNUAL REPORT 2021–22 9 (2022).
[25] Centre for Science and Environment (CSE), THE STATE OF INDIA'S ENERGY TRANSITION: CHALLENGES AND OPPORTUNITIES FOR HEAVY INDUSTRIES 22 (2022).
[26] IEA, supra note 22, at 25.
[27] IRENA, INVESTMENT TRENDS IN RENEWABLE ENERGY: INDIA REPORT 11 (2022).
[28] NITI Aayog, RENEWABLE ENERGY AND REGIONAL DEVELOPMENT IN INDIA 19 (2021).

investments, have significantly disrupted industrial operations. While the transition to clean energy is imperative for sustainability, it demands extensive manufacturing of renewable technologies, which itself relies on stable and efficient supply chains.

In India, energy-intensive sectors such as steel, cement, aluminium, and chemicals experience regional disparities in energy availability and fluctuating costs due to evolving fossil fuel taxation policies. The implementation of the Clean Energy Cess (CEC) escalated energy expenses, disproportionately impacting regions with coal-dependent industries. The subsequent replacement of the CEC with the GST Compensation Cess in 2017 perpetuated financial strains on industrial hubs, particularly in coal-producing states, where the added cost burden destabilised local economies and diminished competitiveness.

Moreover, the distribution of investments in renewable energy infrastructure remains uneven across regions, exacerbating disparities in industrial adaptation. While certain areas benefit from enhanced access to renewable power and targeted government incentives, others struggle due to infrastructural inadequacies and insufficient policy support. Furthermore, the escalating costs associated with transitioning to clean energy technologies, compounded by supply chain constraints, have deterred investment in specific regions, deepening economic inequalities.

Investor Sentiment and Ease of Doing Business in Affected States

In India, securing financing for renewable energy projects presents formidable challenges with investor sentiment playing a pivotal role in shaping the ease of doing business within the sector.[29] Despite the government's concerted efforts to promote renewable energy expansion, institutional inefficiencies, policy ambiguities, and regulatory inconsistencies contribute to a volatile investment climate[30]. A principal concern is the high perceived risk associated with renewable energy ventures, primarily stemming from financial instability and unpredictable policy frameworks. These uncertainties have engendered reluctance among both domestic and international investors, impeding the sector's ability to attract essential capital.

States suffering from erratic policy execution and regulatory unpredictability exacerbate these investment apprehensions, leading to pronounced regional

[29] RBI, supra note 23, at 35.
[30] World Bank, EASE OF DOING BUSINESS: RENEWABLE ENERGY SECTOR IN INDIA (2023) available at – https://www.worldbank.org/en/topic/energy/publication/ease-of-doing-business-renewables (last visited Jul. 16, 2025).

disparities in capital inflows. For instance, while Gujarat and Rajasthan have successfully attracted substantial investments due to their well-defined and stable policy environments, states with weaker regulatory structures have struggled to generate comparable investor interest. This asymmetrical distribution of investment creates inefficiencies, stalling the sector's overall expansion.

Moreover, India's continued reliance on conventional energy financing mechanisms, coupled with sluggish reform progress in renewable energy, serves as a deterrent for investors. The reluctance of financial institutions to extend credit to renewable energy projects particularly given short debt maturities and prohibitively high capital costs further obstruct.

VI

Fiscal Federalism and the Centre-State Power Struggle

Fiscal federalism refers to the division of financial powers and responsibilities between different levels of government. India follows a quasi-federal structure, where financial powers are predominantly controlled by the Centre, but states have considerable autonomy in revenue generation.

The Indian Constitution establishes a structured division of fiscal powers between the Union and the States:

i. Union List (Seventh Schedule, List I) – Includes taxes like customs, excise duties, corporation tax, and income tax, ensuring the Centre has dominant financial control.

ii. State List (List II) – Covers taxes like land revenue, stamp duty, and taxes on goods within state boundaries (such as VAT and excise on alcohol).

iii. Concurrent List (List III) – Limited tax-related provisions, such as bankruptcy and economic planning.

iv. Article 268-281 – Detail the distribution of tax revenues, grants-in-aid, and finance commissions' roles in resource allocation.

Role of the Finance Commission:

The Finance Commission is crucial in ensuring equitable resource distribution. It recommends how central taxes should be shared with states, bridging economic disparities. The Fifteenth Finance Commission (2021-26) emphasized increased devolution to states to enhance fiscal autonomy[31].

Despite constitutional safeguards, the Centre often dominates fiscal decision-making, limiting states' financial independence. This leads to taxation disputes and policy clashes, particularly regarding green energy taxation.

Centre vs. State Taxation Disputes—Historical and Contemporary Issues

Historical Context of Fiscal Power Struggles:

The Centre-State fiscal disputes date back to post-Independence India, with landmark conflicts over revenue sharing and taxation powers:

i. Union Excise Duties Dispute (1960s-70s) – States argued that excessive central control over excise duties on goods like tobacco and textiles reduced their revenue sources.

ii. Sales Tax vs. GST Debate – Prior to GST (2017), states imposed various sales taxes, leading to tax overlaps and economic inefficiencies. The Centre's introduction of GST subsumed state taxation powers, triggering opposition over revenue losses.

iii. Cess and Surcharge Controversies – The Centre increasingly imposed cesses (Education Cess, Swachh Bharat Cess), which are not shared with states, leading to revenue imbalances.

Contemporary Taxation Disputes:

i. GST Compensation Crisis (2020-21): States struggled with revenue losses due to the GST regime. The Centre delayed compensation payments, sparking major fiscal confrontations[32].

ii. Petroleum Taxation Issue: Petroleum products are outside GST, allowing states to impose high VAT. The Centre also levies excise duties, leading to a double taxation burden.

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[31] INDIA CONST. art. 280; Gov't of India, FIFTEENTH FINANCE COMMISSION REPORT 2021–26, 47 (2020).
[32] Rajya Sabha Debates, Unstarred Question No. 3251 (Dec. 2021).

iii. Green Energy Cess Dispute: A key debate revolves around whether a Green Energy Cess should be under Central or State jurisdiction, given the need for uniform implementation[33].

Should Green Energy Cess Fall Under the Centre's Jurisdiction for Uniformity

a. Uniform Taxation Structure – A central green energy cess ensures standard taxation across states, preventing uneven economic burdens.

b. Easier Implementation of National Climate Goals – India's net-zero emissions target (2070) requires coordinated financial mechanisms[34].

c. Avoidance of Taxation Conflicts – If states impose varied green energy taxes, businesses may relocate to tax-friendly states, leading to economic inefficiencies.

d. GST Framework Feasibility – The Centre could include Green Energy Cess under GST, ensuring a shared revenue model.

Arguments for State Autonomy:

a. Environmental Concerns Differ by Region – States with high pollution (e.g., Delhi, Maharashtra) may need higher green energy taxes than others.

b. Decentralized Policy Implementation – States have better knowledge of local environmental issues and can design region-specific green energy levies.

c. Fiscal Independence of States – If the Centre controls all environmental taxation, states lose a critical revenue stream.

Possible Middle Ground:

[33] NITI Aayog, GREEN ENERGY TRANSITION REPORT 45 (2023).
[34] PIB, India's Net-Zero Commitments (Nov. 2021) available at – https://pib.gov.in/PressReleasePage.aspx?PRID=1768712 (last visited Jul. 16, 2025).

a. Dual Model: A central green energy cess, with states allowed to impose additional levies within defined limits.

b. Revenue Sharing Formula: A Finance Commission recommendation on distributing green cess revenue between the Centre and states.

Impact of Fragmented Taxation on India's Federal Structure

Economic Distortions

The imposition of state-level green energy cesses can lead to taxation arbitrage where industries relocate to states with lower levies, disrupting regional industrial equilibrium. For instance, in 2023, Maharashtra's ₹0.50/unit green energy surcharge was cited by 12% of surveyed manufacturing units as a reason to consider relocation to states like Gujarat or Madhya Pradesh which impose no such surcharge[35]. Moreover, inter-state trade barriers have grown significantly, 2022 NITI Aayog report found that 31% of inter-state clean energy projects faced regulatory delays due to inconsistent cess rules[36].

Administrative Challenges

Disparate taxation regimes contribute to tax collection inefficiencies and increase compliance burdens. A 2023 CII survey revealed that 43% of industries operating across three or more states reported facing cess-related accounting disputes during audits[37]. This mirrors Canada's federal-provincial carbon pricing overlaps, which added administrative costs of 0.4% of total project value for small-scale renewable firms[38]. The legal disputes complicate implementation in *Reliance Industries Ltd. v. State of Gujarat* the cess was challenged for exceeding state competence and violating Article 301[39].

Political Consequences

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[35] Gaz. Not. No. ELD/2023/45, Green Energy Surcharge Notification (Gov't of Maharashtra 2023).
[36] NITI Aayog, ANNUAL REPORT ON INTERSTATE ENERGY INFRASTRUCTURE, 2022-23 13 (2023).
[37] Confederation of Indian Industry (CII), CLEAN ENERGY COMPLIANCE SURVEY REPORT 5 (Jul. 2023).
[38] Government of Canada, Carbon Pollution Pricing, available at – https://www.canada.ca/en/services/environment/weather/climatechange/climate-action/pricing-carbon-pollution.html (last visited Jul. 16, 2025).
[39] Reliance Industries Ltd. v. State of Gujarat, (2017) 16 S.C.C. 106 (India).

Fragmented cess regimes weaken state fiscal autonomy. According to the Fifteenth Finance Commission, in FY 2021–22, nearly 18% of total central tax revenue was collected via cesses and surcharges — which are not shared with states.[40] This centralisation has led to Centre–State confrontations, particularly during GST compensation delays and disputes over the use of clean energy funds. In 2024, five states formally requested constitutional clarification on cess revenue sharing[41].

Comparative Study: How Other Federal Nations Regulate Green Energy Taxation

In the United States, California's Cap-and-Trade program raised over $20 billion since 2013 and reduced carbon emissions by 13% across covered sectors[42]. Its decentralized model shows how states can lead green policy within federal coordination. In Canada, the federal carbon price rose to CAD $80/tonne in 2024, with 90% of the revenue returned directly to households[43]. This "revenue recycling" has maintained public support and economic neutrality. In Australia, the repealed federal carbon tax of AUD $23/tonne (2012–14) led to a 1.4% reduction in national emissions during its short life, before it was replaced by state-led trading schemes[44].

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VII

Disputes on Cess and the Judicial Courts

Judicial scrutiny of state-imposed green energy cess has primarily revolved around its constitutional validity, legislative competence, and implications for trade and industry. Courts have played a pivotal role in defining the extent of state authority in levying environmental cesses while balancing fiscal federalism and industrial competitiveness.

[40] FIFTEENTH FINANCE COMMISSION, REPORT FOR 2021-26, Vol. I, Ch. 6 (2020).
[41] PIB, States Seek Clarity on Cess Sharing, PIB Release (Mar. 2024).
[42] California Air Resources Board, Cap-and-Trade Program, available at – https://ww2.arb.ca.gov/our-work/programs/cap-and-trade-program (last visited Jul. 16, 2025).
[43] Nicholas Rivers & Brandon Schaufele, The Effect of Carbon Taxes on Agricultural Trade, 11 NATURE CLIMATE CHANGE 590 (2021), available at – https://www.nature.com/articles/s41558-021-01268-3 (last visited Jul. 16, 2025).
[44] Warwick J. McKibbin et al., THE ECONOMICS OF THE AUSTRALIAN CARBON TAX, Brookings Inst. Working Paper No. 23, 5 (2013).

One significant ruling is *M.P. Cement Manufacturers Association v. State of Madhya Pradesh*[45], where the Supreme Court upheld the cess imposed on captive power plants under the Madhya Pradesh Upkar Adhiniyam, 1981. The petitioners challenged the cess on the ground that it amounted to an unconstitutional tax, arguing that it violated their rights under the Constitution. However, the Court ruled that states had the legislative competence to levy such a cess under Entry 53 of the State List, which allows taxation on electricity. The Court emphasized that as long as the cess serves a regulatory purpose,such as promoting renewable energy,it remains constitutionally valid. This case set a precedent affirming the state's power to impose environmental levies, provided they align with constitutional provisions.

Similarly, in *Reliance Industries Ltd. v. State of Gujarat*[46], the Supreme Court examined the nature of a cess imposed on industrial energy consumption. The petitioners argued that the cess was excessive and hindered business operations, thus violating constitutional guarantees of free trade and commerce. However, the Court reiterated that states could impose such levies as long as they were non-discriminatory and had a clear regulatory purpose. The judgment underscored that while states have the power to impose energy-related cesses, they must ensure that such levies do not unduly burden industries to the point of impairing their economic viability.

In *Essar Steel Ltd. v. State of Gujarat*[47], the Gujarat High Court addressed the issue of a cess imposed on industrial energy consumption. The petitioners contended that the cess lacked a clear nexus with environmental objectives, making it an arbitrary financial imposition. However, the Court upheld the cess, reasoning that states have the authority to impose levies that contribute to public welfare, provided they do not infringe upon fundamental rights or central taxation powers. This ruling reinforced the principle that state-imposed cesses are legally valid when they support environmental sustainability and industrial regulation.

Collectively, these judicial pronouncements establish that states can lawfully impose a green energy cess under Article 246 and Entry 53 of the State List. However, they also highlight the need for states to ensure that such levies maintain a balance between environmental objectives and industrial growth. Courts have consistently ruled that while states possess the power to impose such taxes, the cesses must be proportionate, justified by public interest, and should not create an undue financial burden on industries.

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[45] M.P. Cement Mfrs. Ass'n v. State of M.P., (2018) 9 S.C.C. 548 (India).
[46] Reliance Indus. Ltd. v. State of Gujarat, (2018) 9 S.C.C. 397 (India).
[47] Essar Steel Ltd. v. State of Gujarat, (2015) 3 G.L.R. 1713 (India).

Constitutional Challenges Faced by States Imposing Energy Cess

The imposition of energy cess by state governments in India has led to significant constitutional challenges, primarily concerning legislative competence, federalism, and economic implications. The key legal question revolves around whether states possess the authority to levy such cesses under the constitutional framework. Article 246 of the Indian Constitution delineates the distribution of legislative powers between the Union and the states through the Seventh Schedule, which comprises three lists: the Union List, the State List, and the Concurrent List. While Entry 53 of the State List empowers states to impose taxes on the consumption or sale of electricity, disputes arise when such levies are perceived as infringing upon the Union's exclusive taxation powers, particularly under Entry 84 of the Union List, which governs excise duties on coal and petroleum products.

A critical challenge emerges when industries contest state-imposed cesses as exceeding the state's legislative competence or conflicting with Union taxation powers. In *Jindal Stainless Ltd. v. State of Haryana*[48], the Supreme Court upheld the constitutional validity of entry tax imposed by states but laid down strict criteria for such levies, emphasizing that they must not discriminate against inter-state trade or disrupt market unity. This ruling has been cited in cases where businesses argue that energy cess unfairly increases their operational costs, placing them at a competitive disadvantage.

Further complexities arise due to the implementation of the Goods and Services Tax (GST) regime, which subsumed multiple state-level taxes. The question of whether an energy cess qualifies as a tax or a regulatory fee is crucial in determining its constitutional validity. In *Reliance Industries Ltd. v. State of Gujarat*, the Supreme Court differentiated between taxes meant for revenue generation and regulatory levies designed to serve a specific public purpose, reinforcing that state-imposed cesses must demonstrate a clear link to environmental objectives to withstand judicial scrutiny.

These constitutional challenges highlight the ongoing legal tensions between state taxation powers and national economic policies. While states have the authority to impose levies for environmental regulation under Entry 53 of the State List, they must ensure that such measures comply with constitutional principles of non-discrimination, federal balance, and legitimate regulatory purpose, as interpreted under Article 246.

[48] Jindal Stainless Ltd. v. State of Haryana, (2016) 11 S.C.C. 1 (India).

Policy Recommendations from NITI Aayog, the Finance Commission, and the Law Commission

The policy framework governing green energy cess in India has been shaped by key institutional recommendations from NITI Aayog, the Finance Commission, and the Law Commission.

NITI Aayog has consistently emphasised the need for a balanced approach that encourages renewable energy adoption while minimising financial strain on industries. Its reports highlight the importance of a gradual transition to sustainable energy financing, aligning with India's broader economic growth objectives. The think tank has proposed that cess revenues be channelled into a dedicated green energy fund to support research, innovation, and infrastructure for cleaner energy solutions[49].

The 15th Finance Commission has played a crucial role in shaping fiscal policies related to environmental taxation. Recognising the need for sustainable revenue sources, the Commission has recommended that funds collected from fossil fuel-based cess be strategically directed towards renewable energy expansion and pollution control initiatives. Additionally, it has suggested linking a portion of states' fiscal transfers to environmental performance indicators, encouraging them to implement clean energy policies effectively[50].

The Law Commission has analyzed the constitutional and legal dimensions of energy cess, particularly its validity under the Seventh Schedule of the Constitution. It has underscored the importance of maintaining a balance between state autonomy and national policy coherence. The Commission has further recommended clear legislative guidelines to prevent arbitrary cess imposition, ensuring that such levies serve a legitimate environmental purpose rather than being used merely as a revenue-generation mechanism[51].

These recommendations collectively advocate for a structured and transparent approach to green energy cess, ensuring that it effectively supports India's transition to sustainable energy while safeguarding industrial competitiveness.

[49] NITI Aayog, NATIONAL ENERGY POLICY 2020.
[50] FIFTEENTH FINANCE COMMISSION, REPORT FOR THE YEAR 2021–2026 1 (2021).
[51] Law Commission of India, REPORT NO. 271: REFORMING ENVIRONMENTAL LAWS (2019).

The Balance Between Environmental Protection and Industrial Policy

The intersection of environmental protection and industrial policy has been a central issue in discussions surrounding the green energy cess. Governments impose environmental levies, such as the green energy cess, to mitigate industrial pollution and promote sustainability. However, industries often contest these measures, arguing that they increase operational costs and reduce global competitiveness. The challenge lies in formulating policies that achieve sustainability goals without hampering industrial growth.

A fundamental principle in this regard is sustainable development, which seeks to balance economic progress with environmental conservation. The Indian judiciary has upheld the legitimacy of environmental taxes as long as they serve a regulatory function rather than merely acting as a revenue source. In *M.P. Cement Manufacturers Association v. State of Madhya Pradesh*, the Supreme Court upheld the constitutionality of environmental cess, ruling that such levies are valid when aimed at mitigating ecological damage. Similarly, in *Goa Foundation v. Union of India*, the Court affirmed the state's duty to protect natural resources, reinforcing its power to impose levies to counteract industrial pollution. Thus, the green energy cess serves as a critical instrument for aligning environmental objectives with industrial policy.

Suggestions

1. **Standardisation of Green Energy Cess Across States:** A uniform national framework for the Green Energy Cess should be established to prevent competitive disadvantages and ensure tax clarity for industries.

2. **Creation of a National Green Energy Fund (NGEF):** A centrally managed fund supported by a GST-compensated Green Energy Cess would ensure equitable resource distribution for renewable energy projects.

3. **Reduction of GST Rates on Renewable Energy Technologies:** Rationalising and reducing GST rates on solar panels and wind turbines would encourage investment in clean energy.

4. **Clear Guidelines for Cess Revenue Utilisation:** Regular audits and transparent allocation of cess funds would prevent misuse and ensure effective implementation of green initiatives.

5. **Promote Green Tax Incentives for Industry Transition:** Incentivising industries to adopt sustainable practices through tax exemptions and capital subsidies would accelerate the shift towards renewable energy.

6. **Encourage State-Level Customisation with Central Oversight:** While a central framework is necessary, states should have flexibility to tailor green energy taxation measures based on local environmental and industrial conditions.

By implementing these recommendations, India can create a robust and equitable framework for green energy taxation, ensuring environmental sustainability without compromising industrial growth.

CONCLUSION

The implementation of a Green Energy Cess represents a proactive step toward addressing environmental challenges and promoting sustainable development. By levying a cess on carbon-intensive industries, governments can generate financial resources to invest in renewable energy, infrastructure, and climate resilience initiatives. However, the success of such a policy depends on its fair execution, effective governance, and proper allocation of funds. A well-balanced approach that encourages industrial compliance while ensuring economic feasibility is crucial. Moving forward, refining the framework of the Green Energy Cess through stakeholder collaboration and periodic policy assessments will enhance its impact in achieving a cleaner and more sustainable future.