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The Indian Union has come into existence in the most perfunctory manner imaginable. The Instrument of Accession and the Standstill Agreement which were negotiated between the Government of India and the Indian States vest the Indian Princes with powers and prerogatives which cut right across the rights and privileges of the peoples of Indian States. Five hundred and eighty-two States are unleashed as a result of the abolition of Paramountcy, which is contingent on the withdrawal of Britain from India. There cannot be any unequal yoking of the Indian Provinces and the Indian States in the unionised polity of India, if the new Sovereign Republic of the future is to endure as a strong and integrated entity.

The authors of this unique book have examined the existing financial and economic systems of the States and Provinces and have evolved an integrated system of finances for the Union amidst a wealth of statistical and other data. The necessity and usefulness of such a book at this juncture for our constitution-makers and students of public affairs can hardly be overemphasized.

UNION FINANCES

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UNION FINANCES

An Inquiry into the Basis of Integration of the Fiscal and
Economic Systems of States and Provinces in an
Indian Union

By

Dr. LANKA SUNDARAM, M.A., Ph.D. (London),
Member of the Indian Delegations to the General Assembly (1946)
and the Human Rights Commission (1947) of the
United Nations

AND

V. VITTAL BABU,
Research Section, Congress Party in the
Indian Central Legislature.

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PREFACE

This is a book more on the Indian States than on the Indian Provinces, the Indian Union and Pakistan.

We have planned and executed this inquiry long before Partition was ordained by the British Government and accepted by the representatives of the future Indian Union, without any fore-knowledge that the controversies of the past four weeks in regard to the future of the Indian States would at all take place.

So far, no study has been made of the manifold problems involved in unionisation, particularly from the viewpoint of the relationships which ought to subsist between the Indian Provinces inside of a Union on the one part and the Indian States on the other, apart from the one-sided inquiries of the Nind, Butler and Davidson Committees in the early thirties of the present century. We have come across numerous difficulties in our investigation of the problems relating to the quantum of Paramountcy, and that of the sovereignty of the Indian Princes, particularly in regard to questions like financial contributions, taxes on income, customs, excises, salt, defence, reconstruction finance etc. We, however, believe that the thesis we have built up on the most up-to-date statistics, which we were able to bring together with respect to these and many other matters, would be accepted as a yard-stick for the measurement of the problems involved in Unionisation.

While the book was in the hands of the printer, numerous developments took place almost daily, nay hourly, and we have made attempts to revise the MSS, by adding paragraphs and footnotes and by correcting data in each chapter, and we venture to hope that though there will be some cause for irritation on the part of the reader that the text has become more or less out of date in isolated parts (eg. the adhesion of Travancore to the Union), the march of events, including the acceptance of a draft Instrument of Accession, a Standstill Agreement and the actual adhesion of some States to the Union, has not at all vitiated our argument.

We hold that the Indian States Department of the Government of India, over which Sardar Vallabhbhai Patel so ably

presides, has agreed to the Instrument of Accession and the accompanying documents *under duress*, for we have not the slightest doubt that the architects of the Indian Union have made frantic efforts to bring almost every one of the Princes into the Union, even before August 15, 1947. We consider that this is a very tragic thing indeed, for no examination was made of the implications of unionisation on this perfunctory basis, in which the sovereignty of the Constituent Assembly of India and of the Indian Union, leave alone the interests of the people of the Indian States, has been virtually entrenched upon. The Standstill Agreement will have to be revised within a period of two years, and we believe that our inquiry and statistics will come into considerable use when the re-definition of the relationships of the Princes and their *darbars* to the Indian Republic of the future takes shape and permanence.

We have added an Introduction, setting out the texts of the Instrument of Accession, the Standstill Agreement, and the recommendations of the Union Constitution Committee of the Constituent Assembly on Union finance and borrowing, with as little comment as possible, in order to fix the implications of our inquiry in their proper setting. No other course (eg. printing them as an appendix) was possible for us, since the book was completely set up in type even before we knew the contents of the drafts of these three vital documents.

Since we had to traverse an unusual and almost uncharted inquiry, we naturally sought, and gratefully received, assistance from numerous friends, who would like to remain anonymous. To Col. Hori Lal Varma, formerly Political Minister and acting Prime Minister of Rampur, we are obliged to sage counsel and assistance. Pandit Dayanand Thapliyal has put us under great obligation with cheerful help at every stage. But no one is responsible for the views expressed by us, or for the shortcomings of this book.

NEW DELHI,
July 30, 1947. }

Lanka Sundaram.
V. Vittal Babu.

I would like to state that the views expressed in this book are entirely my own, and do not in any way involve the Research Section of the Congress Party in the Central Legislature.

V. Vittal Babu.

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INTRODUCTION

"The States have complete freedom—technically and legally they are independent. Presently I will discuss the degree of independence which we ourselves feel is best in the interests of your own States. But there has grown up, during the period of British administration, owing to the fact that the Crown Representative and the Viceroy are one and the same person, a system of co-ordinated administration on all matters of common concern, which meant that the sub-continent of India acted as an economic entity. That link is now broken. If nothing can be put in its place, only chaos can result, and that chaos, I submit, will hurt the States first—the bigger the State the less the hurt and the longer it will take to feel it—but even the biggest of the States will feel itself hurt just the same as any small State."

—Lord Mountbatten, in his address to the Conference of Rulers and Representatives of States, on July 25, 1947.

Within a few days of the promulgation of the Indian Independence Act, setting up the two Dominions of India and Pakistan, Lord Louis Mountbatten, who was accepted as the first Governor-General of the Indian Union, set into motion the entire machinery of the Indian States Department (which is a re-incarnation of the Political Department of yesterday), and brought into existence a new situation for the Indian Princes. They were asked, peremptorily enough, to adhere to either of the two Dominions, or otherwise face the consequences of isolation. With an adroitness which must have baffled both the Princes and the representatives of India, Lord Mountbatten succeeded in bringing one by one the principal Indian States into the Indian Union. Even the fire-eating *dewan* of Travancore had to climb down and arrange for the adhesion of his Maharaja to the Indian Union. The position of certain other States, like Hyderabad and Bhopal, is still obscure, and even this introduction to the book is likely to become out of date on publication on account of the march of *legal developments* involved in the adhesion of the States to the Indian Union or Pakistan.

We have attempted to write this introduction last, in order to make it possible that our main thesis, which is to follow, is fixed in its proper setting. It is claimed that the Princes have been bamboozled into agreements against their will. We desire to show in the following pages that the Instrument of Accession, the Standstill Agreement, and even the recommendations of the Union Constitution Committee in the

sphere of finance and borrowing; are completely unrelated to the implications of the proposed integration of the Provinces and the States within the framework of the Indian Union. As a matter of fact, the Instrument of Accession and the Standstill Agreement completely load the dice in favour of the Princes, and by, comparison, the Constituent Assembly of India loses its sovereignty and plenary powers in the sphere of unionisation. In other words, the balance of advantage in these documents is entirely in favour of the Princes, whose peoples were not at all consulted during the fateful negotiations of July 1947, between New Delhi on the one part and the Indian States on the other.

When the history of India comes to be written, after the present complexities and controversies disappear, and when a proper perspective and sense of values becomes available, it will be said that the constitution-makers have completely let down the people of the Provinces and the States, by making it possible for the Princes to retain their prerogatives and perquisites almost untrammelled. It is more than likely that, during the two-year period of the Standstill Agreement, the representatives of the Indian Union and of the Indian States would sit together and work out plans for a proper integration of the fiscal and economic systems of the two component parts of the Union. If this is not attempted, the greatest possible harm will be done to the people of the States and of the Provinces, who must march shoulder to shoulder in their quest for sanctions behind their Freedom, as a proud people, who are well knit and ready to assume their national and international obligations with self-respect and confidence.

INSTRUMENT OF ACCESSION

The following is the Instrument of Accession for a ruler to accede to either of the dominions of India and Pakistan:

“Instrument of Accession of * * * *

Whereas the Indian Independence Act, 1947, provides that as from August 15, 1947, there shall be set up an independent Dominion known as India, and that the Government of India Act, 1935, shall with such omissions, additions, adaptations and modification, as the Governor-General may by order specify,

be applicable to the Dominion of India; And whereas the Government of India Act, 1935, as so adapted by the Governor-General provides that an Indian State may accede to the Dominion of India by an Instrument of Accession executed by the ruler thereof: now therefore I * * * * ruler of * * * * in the exercise of my sovereignty in and over my said State do hereby execute this my instrument of accession and I hereby declare that I accede to the Dominion of India with the intent that the Governor-General of India, the Dominion Legislature, the Federal Court and any other Dominion authority established for the purposes of the Dominion shall, by virtue of this my Instrument of Accession, but subject always to the terms thereof, and for the purposes only of the Dominion, exercise in relation to the State of * * * * (hereinafter referred to as "this State") such functions as may be vested in them by or under the Government of India, Act 1935, as in force in the Dominion of India on August 15, 1947, (which Act as so in force is hereinafter referred to as "the Act").

2. I hereby assume the obligation of ensuring that due effect is given to the provisions of the Act within this State so far as they are applicable therein by virtue of this my instrument of accession.

3. I accept the matters specified in the schedule hereto as the matters with respect to which the Dominion Legislature may make laws for this State.

4. I hereby declare that I accede to the Dominion of India on the assurance that if an agreement is made between the Governor-General and the ruler of this State whereby any functions in relation to the administration in this state of any law of the Dominion Legislature shall be exercised by the ruler of this State, then any such agreement shall be deemed to form part of this instrument and shall be construed and have effect accordingly.

5. The terms of this my Instrument of Accession shall not be varied by any amendment of the Act or of the Indian Independence Act, 1947, unless such amendment is accepted by me by an Instrument supplementary to this Instrument.

6. Nothing in this Instrument shall empower the Dominion Legislature to make any law for this State authorising

the compulsory acquisition of land for any purpose, but I hereby undertake that should the Dominion for the purposes of a Dominion law which applies in this State deem it necessary to acquire any land, I will at their request acquire the land at their expense or if the land belongs to me transfer it to them on such terms as may be agreed, or, in default of agreement, determined by an arbitrator to be appointed by the Chief Justice of India.

7. Nothing in this Instrument shall be deemed to commit me in any way to acceptance of any future constitution of India or to fetter my discretion to enter into arrangements with the Government of India under any such future constitution.

8. Nothing in this Instrument affects the continuance of my sovereignty in and over this State, or, save as provided by or under this Instrument, the exercise of any powers, authority and rights now enjoyed by me as ruler of this State or the validity of any law at present in force in this State.

9. I hereby declare that I execute this Instrument on behalf of this State and that any reference in this instrument to me or to the ruler of the State is to be construed as including a reference to my heirs and successors.

Given under my hand this * * * day of August, 1947.

I do hereby accept this instrument of Accession, Dated this * * * * day of August, 1947.

(Governor-General of India).

SCHEDULE

The schedule attached to the Instrument of Accession which prescribes matters with respect to which the Dominion Legislature may make laws for an acceding State are:

(a) *Defence.* 1. The naval, military and air forces of the Dominion and any other armed force raised or maintained by the Dominion; any armed forces, including forces raised or maintained by an acceding State, which are attached to, or operating with any of the armed forces of the Dominion. (2) Naval, military and air force works, administration of cantonment areas (3) Arms; fire-arms; ammunition; and (4) Explosives.

(b) *External Affairs*: 1. External affairs; the implementing of treaties and agreements with other countries; extradition, including the surrender of criminals and accused persons to parts of His Majesty's Dominions outside India. (2) Admission into, and emigration and expulsion from, India, including in relation thereto the regulation of the movements in India of persons who are not British subjects domiciled in India or subjects of any acceding State; pilgrimages to places beyond India. (3) Naturalisation.

(c) *Communications*: 1. Posts and Telegraphs, including telephones, wireless, broadcasting, and other like forms of communication. (2) Federal railways; the regulation of all railways other than minor railways in respect of safety, maximum and minimum rates and fares, station and service terminal charges, interchange of traffic and the responsibility of railway administrations as carriers of goods and passengers: the regulation of minor railways in respect of safety and responsibility of administrations of such railways as carriers of goods and passengers. (3) Maritime shipping and navigation, including shipping and navigation on tidal waters; Admiralty jurisdiction. (4) Port quarantine. 5. Major ports, that is to say, the declaration and delimitation of such ports, and the constitution and powers of port authorities therein. 6. Aircraft and air navigation; the provision of aerodromes; regulation and organisation of air traffic and of aerodromes. 7. Lighthouses, including lightships, beacons and other provisions for the safety of shipping and aircraft. 8. Carriage of passengers and goods by sea or by air. 9. Extension of the powers and jurisdiction of members of the police force belonging to any unit to railway area outside that unit.

(d) *Ancillary*: (1) Elections to the Dominion Legislature, subject to the provisions of the Act and of any order made thereunder. (2) Offences against laws with respect to any of the aforesaid matters. (3) Inquiries and statistics for the purposes of any of the aforesaid matters. (4) Jurisdiction and powers of all courts with respect to any of the aforesaid matters but, except with the consent of the ruler of the acceding State, so as not to confer any jurisdiction or powers upon any courts

other than courts ordinarily exercising jurisdiction in or in relation to that State.

STANDSTILL AGREEMENT

The following is the text of the Standstill Agreement:

Whereas it is to the benefit and advantage of the Dominion of India Pakistan as well as of the Indian States that existing agreements and administrative arrangements in matters of common concern should continue for the time being:

Now, therefore, it is agreed between the parties that:—

1. No State shall be liable to pay any cash contribution falling due after the 15th August, 1947 in so far as it exceeds the value of any privilege or immunity which the State enjoys.
2. Until otherwise provided by mutual agreement, a State shall be entitled to the continuance of any privilege or immunity which it enjoyed immediately before 15th August, 1947, provided that it continues duly to fulfil all conditions or reciprocal obligations attached to each such privilege or immunity.

EXPLANATION

The term "cash contribution" and "privilege or immunity" in the above clauses have the meanings assigned to them in section 147 of the Government of India Act, 1935.

3. (i) Until new agreements in this behalf are completed, all relations and arrangements as to matters of common concern now existing between the Crown and any Indian State shall in so far as may be appropriate continue as between the Dominion of India Dominion of Pakistan and the State.

(ii) In particular, and without derogation from the generality of sub-clause (1) of this clause, the matters referred to above shall include the matters specified in the Schedule to this agreement.

4. Until otherwise provided by mutual agreement, the criminal, revenue and civil jurisdiction heretofore exercisable in any Indian State of Class III as defined in para 11 of the Indian States Committee's Report 1928-29, by, or by persons

acting under the authority of, the Crown Representative shall hereafter be exercisable by, or by persons acting under the authority of the Government of the Dominion of India.

(Note:—This clause applies only to the non-jurisdictional and semi-jurisdictional estates and talukas in Kathiawar and Gujarat).

SCHEDULE

- | | |
|------------------------------------|---|
| 1. Air Communications. | 11. Motor Vehicles. |
| 2. Arms and equipment. | 12. National Highways. |
| 3. Control of Commodities. | 13. Opium. |
| 4. Currency and coinage. | 14. Posts, Telegraphs and Telephones. |
| 5. Customs. | 15. Railways (including police and other arrangements, in Railway lands). |
| 6. Defence. | 16. Salt. |
| 7. External Affairs. | 17. Taxation. " |
| 8. Extradition. | 18. Wireless. |
| 9. Import and Export Control. | |
| 10. Irrigation and Electric Power. | |

FINANCE AND BORROWING POWERS

The following are the powers sought to be invested with the Union Centre, in the spheres of finance and borrowing, according to the Report of the Union Constitution Committee of the Constituent Assembly of India:

"1. Revenues derived from sources in respect of which the Federal Parliament has exclusive power to make laws will be allocated as Federal revenues, but in the cases specified in the next succeeding paragraph the Federation will be empowered or required to make assignments to Units from Federal revenues.

"2. Provision should be made for the levy and, if necessary, distribution, of the following taxes, viz., customs, Federal excises, export duties, death duties and taxes on income other than agricultural income and taxes on companies.

"3. The Federal Government will have power to make subventions or grants out of Federal revenues for any purpose, notwithstanding that the purpose is not one with respect to which the Federal Parliament may make laws.

"4. The Federal Government will have power to borrow for any of the purposes of the Federation upon the security of Federal revenues subject to such limitations and conditions as may be fixed by Federal law.

Lord Mountbatten had earlier created the "atmosphere" for this dictum by stating that "if any of the Indian States came to him for having a separate treaty—economic or military—with His Majesty's Government, he would transmit such a request to His Majesty's Government." Inscrutable are the ways of the British Imperialists! The same Viceroy who, in his broadcast to the people of India, protested his belief in the unity of India, offered to create two Dominions in the country, transmit the wishes of Indian States to have separate treaties with Britain, and finally rounded off his exposition by declaring that the States are "absolutely free to choose between one or the other of the Constituent Assemblies," though he felt that "geography would play a large part in their decisions". The mischief is, thus, completely wrought by Britain,* which proposes to quit India long before June 1948—the date set for it in the Declaration of February 20, 1947—but not before unleashing all the centrifugal forces inside the community, whether they be the communalists in the Provinces, or the medieval despots of Princely India.

In case we exaggerate, let us quote a well-known administrator. On the showing of Sir C. P. Ramaswami Iyer, the Dewan of Travancore, the following will be the fantastic position on the day when the Indian Union and Pakistan come into existence: We have now "reached a stage when India has to be divided into Hindustan and Pakistan—two States which must maintain an unstable equilibrium, with possibilities of perpetual conflict and frontier incidents, and with foreign, commercial, excise, taxation, communication, defence and other policies, in all likelihood, diametrically opposed to each other. What was then to happen to the States like Travancore who are not concerned with those quarrels and had their own special problems to face? If the Congress, instead of allowing its camp-followers to go about making fiery speeches and embarrassing administrations, came to grips with actual problems like currency, communications, defence etc., and sought agreement,

* Accepting the British Plan of June 3, 1947, for the division of India, the All-India Congress Committee, at its session in Delhi on June 15, passed a resolution, of which the following are important portions:

"The Congress has consistently upheld that the unity of India must be maintained. Ever since its inception, more than 60 years ago, the

they would find that Travancore would go not only the proverbial half-way, but three-quarters-way to meet them.”*

India today lies prostrate before a master who promises to do the vanishing trick. Truly, a Leviathan finds her even otherwise unwieldy limbs mercilessly lacerated. We in this country must now have two “sovereign” territories, call them Pakistan, or Groups B and C, and the Union Centre, otherwise Hindustan or Group A. In addition, we may have numerous independent kingdoms springing out of nowhere, for if we are to believe Britain, 582 princes will become completely sovereign the moment Paramountcy becomes abolished, and there are the Bhopals, the Travancores and the Nizams who are willing to oblige Britain, in the time-honoured fashion of Quaid-e-Azam Jinnah and his Muslim League.†

India is to be divided and regrouped, whether one likes it or not, and we as a people struggling for our Freedom cannot wait even for the day on which Britain is to quit, but must straightaway grapple with the gigantic problems of the proposed division and regrouping of territories comprising the Pro-

Congress has laboured for the realisation of a free and united India and millions of our people have suffered in this great cause. Not only the labours and sacrifices of the past two generations, but the long course of India's history and tradition bear witness to this essential unity. Geography and mountains and the seas fashioned India as she is, and no human agency can change that shape or come in the way of her final destiny. Economic circumstances and the insistent demands of international affairs make the unity of India still more necessary. The picture of India we have learnt to cherish will remain in our minds and hearts. The All-India Congress Committee earnestly trusts that when present passions have subsided, India's problems will be viewed in their proper perspective, and the false doctrine of two nations in India will be discredited and discarded by all.

“The proposals of June 3, 1947, are likely to lead to the secession of some parts of the country from India. However much this may be regretted, the All-India Congress Committee accepts this possibility in the circumstances now prevailing.”

* At a press conference at Trivandrum on June 11, 1947.

† The decisions of the Partition Council are not available to us, and it is not possible to say with certainty how the assets and liabilities of the Indian Union and Pakistan would become separated. We are, however, given to understand that the spokesmen of Pakistan found themselves to be tied up into knots, as a result of the inextricable character of the administrative polity of India. We are further given to understand that Mr. Jinnah had to concede the principle that the Indian Union is the “successor State,” though he is still loudest in proclaiming to the world that the Indian Union is merely Hindustan, which is left behind in India after Pakistan has been lopped off and created into a separate entity!

vinces and the States, either into one polity or two, or even into a heterogeneous mass of polities in which the six hundred odd Princes become sovereign.

For the purposes of this monograph, we assume Group A of the Cabinet Mission Plan to be the Indian Union, and Pakistan (comprising broadly Groups B and C) must be presumed to have the same problems as the Union Centre, though to a smaller extent. The division of assets and liabilities between two Indias is a gigantic problem which we do not propose to discuss in detail, for we are only concerned with the problems of the integration of the Provinces with the States, even supposing that the latter would have their allegiance divided between two sovereign Indias in the future.

Though the Declaration of the British Cabinet Mission of May 16, 1946, regarding India's future is declared to be inoperative with reference to the Provinces, the British plan of June, 1947, (paragraph 18) maintains unchanged what Lord Pethick-Lawrence and his colleagues had laid down for the States. For our purposes in this chapter we have to begin with the Cabinet Declaration, and visualise the manner in which the States can become yoked to the Provinces in the Indian Union, or even Pakistan, though geography, in terms of Lord Mountbatten's prognostication, does not provide even half a dozen States for integration with Mr. Jinnah's Dominions to the East and the West.

A new precedent is created in Indian and interational history by the proposed relinquishment of Paramountcy by the Crown in respect of the States. The Cabinet Mission (paragraph 14) states: "It is quite clear that with the attainment of independence by British India, whether inside or outside the British Commonwealth, the relationship which has hitherto existed between the Rulers of the States and the British Crown will no longer be possible. Paramountcy can neither be retained by the British Crown, nor transferred to the new Government....." The intention of His Majesty's Government to relinquish Paramountcy, which in other words means the re-vesting of sovereignty with the Princes, has created an exceptionally difficult position in India. While it is clear that the vast majority of the 582 States would *eventually* come

into the Indian Union, or Hindustan, it is obvious that quite a good few of the major States may contract out of the Union. The sabre rattling of the Dewan of Travancore is a typical illustration of the desire, if it were possible, of some of the States to remain in isolation and in medieval grandeur. The Nizam of Hyderabad, who has declared his independence, and is reported to be ready for the establishment of his Legation in London, also supplies another illustration of the present portent to the fortunes of India.* As we write, there is an appreciable agitation among certain States to function as a virtual "Rajastan", and the resignation of the Nawab of Bhopal from his office of Chancellor of the Chamber of Princes, coupled with the proposal for the formation of a group of States which adheres to his ideology, must necessarily compel us to recognise one point of exceptional importance. This deals with the possibility, at any rate for a considerable period, of certain States electing to stay out of the Indian Union or even Pakistan. If

* In a *firman* issued on June 12, 1947, the Nizam of Hyderabad declared as follows :

"The result in law of the departure of the Paramount Power in the near future will be that I shall become entitled to resume the status of an Independent Sovereign. But the question of the nature and extent of the association or relationship between my State and the units in British India remains for decision at a later stage, when their constitution and powers have been determined. Whatever form of constitution they ultimately adopt, it will be the desire of Hyderabad to live in closest friendship and amity with both. Meantime, I and my Government will lose no opportunity of reaching, by active negotiations, working agreements on matters of common interest for the mutual benefit of all. When the time comes to decide on the nature of the States' association or relationship with new units after they have settled their constitutions, I shall continue to be guided by the consideration of the best interests of both Hyderabad and India as a whole."

Earlier in the *firman* the Nizam claimed that the division of Indian Provinces as ordered by the British in the Plan of June 3, 1947, was communal, and that, since in his territories the Hindus and Muslims have always been regarded "as the two eyes of the State," he could not join either of the Constituent Assemblies of the Indian Union or of Pakistan!

At his press conference to New Delhi on July 7, 1947, Ambassador Henry Grady declared categorically that the U. S. A. does not propose to establish any legations as such in any of the States, though he admitted that the question of the establishment of consulates in some of the bigger States will have to be considered in terms of the volume of work available. Sir Hartley Shawcross, Attorney-General, during the course of the debate on the Indian Independence Bill, on July 14, 1947, declared that the British Government "do not propose to recognise the States as separate international entities." It is, however, not clear to us whether Britain would reject the claim of Hyderabad and other States of the same ilk to establish Legations in London.

the Nizam, Travancore and Bhopal are illustrations with reference to a possible single Union, Kashmir and Manipur are vital examples of a similar decision on the part of rulers to stay out with reference to Pakistan.

For our immediate purposes, we must take note of two sets of factors which are bound to determine the fortunes of the Indian Union. It would appear that His Majesty's Government have decided to abolish the office of the Crown Representative and the entire Political Department of the Government of India, in addition to the abolition of Residencies in the States, even long before June 1948, the date on which the British propose to quit India. As has been said earlier, the abolition of Paramountcy and the revesting of the States with sovereign powers might, at any rate as far as a few of the major States are concerned, create a situation in the country which would not be far dissimilar to that prevailing after the death of Aurangzeb. We are not suggesting that virtual anarchy would result if the States choose to stand out of the Union Centre. But we do suggest that enormous problems enveloping political relations, constitutional practices, financial problems, defence etc., would emerge from the situation arising out of Britain's decision to quit India, and the Crown's decision to disappear from the States. It is necessary for us here to state the position as it exists today, in order that certain reasonable conclusions might be drawn, which are calculated to help bring the States into the Indian Union, which would at once be comprehensive and of an enduring character.

Today the Viceroy and Governor-General of India has a dual capacity, one with reference to the administration of the Provinces, and the other (as Crown Representative) dealing with the States. The Political Department of the Government of India had upheld the Butler Committee recommendation that "Paramountcy must remain paramount". In fact, the Political Department, with its hierarchy of Residents in the States, had come to function all these long years both as a party and a judge with reference to the Princes. If there is maladministration and fiscal injustice in the States today, the greater portion of the responsibility must be laid at the doorstep of the Political Department. The "administrative deci-

sions" of the Political Department have become more the *firman*s of a Moghal Emperor or the *encyclicals* of the Pope, than the decisions of a judicial body. We are not here concerned with the tyranny of the Political Department, or the injustice to the States as they exist today. We are, however, concerned with the problems arising out of the abolition of Paramountcy, and what is euphemistically called the re-vesting of the States with the attributes of sovereignty.

NATURE OF PARAMOUNTCY

The Butler Committee (paragraph 57) clearly describes Paramountcy as follows: "Paramountcy must remain paramount; it must fulfil its obligations, defining or adapting itself according to the shifting necessities of the time and the progressive development of the States." This definition of Paramountcy must now be considered to be a thing of the past, but since the States would become vested with the attributes of sovereignty, which do not exist at present and which had not at all existed before, it is necessary that a brief examination of the question of Paramountcy is undertaken at this place.

An elaborate case on treaty rights has been put up in the joint opinion of legal luminaries like Leslie Scott, Stuart Bevan, Wilfrid Green, Valentine Holmes and Donald Somervell, on behalf of the Indian States, (Appendix III to *Butler Committee Report*) which may be summarised as hereunder:

- (1) The relationship between the States and the Crown is determinable by legal principles;
- (2) The States possess all original sovereign powers, except those which have been transferred to the Crown;
- (3) Such transfer has been effected by the States concerned and in no other way;
- (4) The consent of a State to transfer sovereign rights to the Crown is individual to that State, and the specific agreement involving that transfer is investigable to determine the rights and obligations created;
- (5) Where such transfer of sovereign power by a State is made informally, the onus of proof of such transfer rests with the Crown;

(6) The relationship of the Crown as Paramount Power in the States involves mutual rights and obligations, and does not confer upon the Crown any authority or discretion to do acts which are not necessary for the exercise of such rights and the performance of such duties; and

(7) The relationship of States is only with the Crown, and the rights and obligations of the Crown are of such a nature that they cannot be assigned to or performed by any persons who are not under its control.

This opinion of Counsel on the welter of treaties, engagements and *sanads*, which exist between the Princes on the one part and the Crown on the other, is today of greater practical import than it was at the time when the opinion was given in 1928 for submission to the Butler Committee. It must, however, be remembered that the Paramount Power consistently resisted the claims of the States to sovereignty in operation, and a *resumé* of this controversy would prove very helpful, in regard to the delimitation of the future relations between the States on the one part and the Union Centre on the other.

In the famous Baroda Case (1873-75), misrule on the part of the ruler was utilized as justification for intervention by the Paramount Power in the internal administration of the State. In the Manipur Case (1891-92) the plea that the ruler was independent was rejected, and the dictum was laid down that "the principles of international law have no bearing upon the relations between the Government of India as representing the Queen Empress on the one hand and the Indian States under the suzerainty of Her Majesty on the other". It was also further laid down that "the paramount supremacy of the former presupposes and implies the subordination of the latter."*

Apart from further definitions of Paramountcy available, e.g., in Lord Minto's speech at Udaipur on November 3, 1909, etc., the famous dictum of Lord Reading with reference to the Nizam must be recorded here. On March 27, 1926, the Nizam wrote to the Viceroy and Governor-General of India, claiming that in the internal affairs of Hyderabad the Nizam stood "on the same footing as the British Government in India in respect

* These cases are fully reported at pages 16-18 of the *Butler Committee Report*.

of the internal affairs of British India." The following is the operative portion of the Nizam's claim: "Save and except in matters relating to foreign powers and policy, the Nizams of Hyderabad have been independent in the internal affairs of their State, just as much as the British Government in British India. With the reservation mentioned by me, the two parties have on all occasions acted with complete freedom and independence in all inter-governmental questions that naturally arise from time to time between neighbours. Now the Berar question is not and cannot be covered by that reservation. No foreign power or policy is concerned or involved in its examination, and thus the subject comes to be a controversy between the Governments *that stand on the same plane without any limitations of subordination of one to the other.*" (Italics ours.)

Lord Reading in his reply on March 27, 1926, disputed this claim, and reiterated the point that the Nizam had, on a par with other rulers, received a *sanad* from the British Government in 1862, that the right of the British Government to intervene in the internal affairs of the Indian States is one of the consequences "necessarily involved in the supremacy of the British Crown," and that the Nizam has the glorious title "Faithful Ally". Lord Reading further laid down as follows: "The sovereignty of the British Crown is supreme in India, and therefore no ruler of an Indian State can justifiably claim with the British Government on an equal footing. Its supremacy is not based only upon treaties and engagements, but exists independently of them, and quite apart from its prerogative. In matters relating to foreign powers and policies, it is the right and duty of British Government, while scrupulously respecting all treaties and engagements with Indian States, to preserve peace and good order throughout India."

Proceeding, Lord Reading said: "The right of the British Government to intervene in the internal affairs of Indian States is another instance of consequences necessarily involved in the supremacy of the British Crown. The British Government have indeed shown, again and again, that they have no desire to exercise this right without grave reason, but the internal, no less than the external, security which the Ruling Princes

enjoy is due ultimately to the protecting power of the British Government, and where imperial interests are concerned, or the general welfare of the people of a State is seriously and grievously affected by the action of its Government, it is with the Paramount Power that the ultimate responsibility of taking remedial action, if necessary, must lie. The varying degrees of internal sovereignty which the Rulers enjoy are all subject to the due exercise by the Paramount Power of this responsibility.....It is the right and privilege of the Paramount Power to decide all disputes that may arise between States or between one of the States and itself, and even though a Court of Arbitration may be appointed in certain cases, its function is merely to offer independent advice to the Government of India, with whom the decision rests.”

We have not dwelt with this question of Paramourtey and the proposed retrocession of sovereignty to Indian Princes, at this great length, in order merely to whet historical or academic curiosities.* Vital principles are involved in the proposed entry of States, at any rate a greater portion of them, into the Indian Union. Even though such entry is subject to the execution by the rulers of the States of specific Instruments of Accession, the powers of the Union Centre must be put beyond a shadow of doubt, if the proposed politico-economic integration of Provinces and States is to endure. Does the Union Centre, as at present contemplated to include the States, possess

* The following resolution was passed by the Standing Committee of the All-India States Peoples Conference, at its session in Delhi on June 12, 1947 :

“ It is the considered opinion of the Standing Committee of the All-India States Peoples Conference that, on the termination of Paramourtey, sovereignty should, as a matter of course, rest in the people of the States. In view of this, the attempt of the rulers of States in certain agencies, at the instance of local residents, to form Councils of Rulers of States, to annex to emselves certain administrative functions of Paramourtey, is indefensible and constitutes a serious encroachment on the sovereign rights of the people. So long as the States are not sufficiently democratised to enable the people of the States to exercise their sovereignty, the administrative functions of Paramourtey should continue to be exercised by the Interim Government of India, which commands the confidence of the people of the States as well. The Committee further calls upon the States that during the intervening period, popular interim Governments should be established in the States or groups of States, and that steps should be taken for setting up a suitable machinery in each State or group of States, for framing the constitution on the basis of full responsible government through a Constituent Assembly composed of the duly elected peoples' representatives.”

that specific quantum of sovereignty which alone can keep the Provinces and States together, in a framework of polity and administration which can weather the storms of organised political life of today and tomorrow? If the Union Centre is made to possess these attributes of sovereignty, then it is bound to be based on a solid foundation. If, however, the Union Centre is not vested with these attributes of sovereignty, enveloping suzerainty and control over even a categorical list of items relating to policy and administration inside Indian States, then such a Union Centre is not worth the paper on which its Constitution is to be written. A Union Centre which is denied minimum attributes of sovereignty, especially over the States, would become a mockery, and need not be created at all, even at the risk of not having an Indian Union, which is capable of including the States.

It is necessary to record here the viewpoint of the Congress. While regretting that the position in regard to political and constitutional liberty in States is not as it should be, the All-India Congress Committee, in a resolution passed at its Delhi session of June 15, 1947, refuted the British interpretation of Paramountcy. The following is the operative portion of this resolution: "The Committee does not agree with the theory of Paramountcy as enunciated and interpreted by the British Government; but even if that is accepted, the consequences that follow from the lapse of Paramountcy are limited in extent. The privileges and obligations, as well as the subsisting rights as between the States and the Government of India, cannot be adversely affected by the lapse of Paramountcy. These rights and obligations have to be considered separately and renewed or changed by mutual agreement. The relationship between the Government of India and the States would not be exhausted by the lapse of Paramountcy. The lapse does not lead to the independence of the States. Both from the point of view of the spirit underlying the memorandum of May 12, 1946, and the Statement of May 16, 1946, as well as the acknowledged rights of the people all over the world today, it is clear that the people of the States must have a dominating voice in any decision regarding them. Sovereignty, it is admitted, resides in the people, and if Paramountcy lapses,

resulting in the ending of the relationship of the States to the Crown, the inherent rights of the people are not affected thereby for the worse. The arrangements made under Paramountcy in the past dealt, *inter alia*, with the security of India as a whole. In the interest of that security, various agreements were agreed to, limiting the power of the States' authorities and at the same time granting them protection. The question of the security of India as well as other matters are as important today as at any time previously, and cannot be ignored in deciding the future of the States. The All-India Congress Committee cannot admit the right of any State in India to declare its independence and to live in isolation from the rest of India. That would be a denial of the course of Indian history, and of the objectives of the Indian people today. The All-India Congress Committee trusts that the Rulers of the States will appreciate fully the situation as it exists today, and will in full co-operation with their people enter as democratic units in the Indian Union, thereby serving the cause of their own people, as well as of India as a whole."

Right through the course of the argument of this book, we have strictly adhered to the point that the Princes who come into the Indian Union, at any rate so far as they are to be re-vested with sovereignty attributed to the Paramount Power prior to their entry, must *voluntarily* surrender definite portions of that sovereignty. There is no question of any coercion on the part of the proposed Union Centre, or the Provinces, to rope the States into a political and administrative framework against their will. And, yet, it is clear as crystal that chaos must be avoided in the relations *inter se* of the States and the Union Centre, of Indian States among themselves, and of the States and the Provinces, now that the Provinces are permitted direct dealings with adjacent States. In framing this dictum of ours, we are swayed only by the imperative consideration that geographically the States and Provinces are interwoven into a mesh, from which they cannot be extricated either today or tomorrow.

Thus, we arrive at the point where some of the attributes of the Paramount Power, which are in operation today, must become vested with the Union Centre, for otherwise the Indian

Union would become widowed of power and purposiveness. In so far as fiscal and economic matters are concerned, the broad proposition must be enunciated here as being beyond all shadow of doubt, that it is not the intention of constitution-makers today that the Union Centre must be something like a *Zollverein* or a *Hanseatic League*. The Union Centre must be a State integral to both the Provinces and the States. Perhaps, we should say that the States and Provinces are integral to the proposed Union Centre. There is no alternative to an organic Union enveloping, to the extent possible in the prevailing circumstances, both States and Provinces, for otherwise the proposed Union Centre would lack stability, and would crumble at the first wafting of an unfriendly breath.

VOLUNTARY ENTRY OF STATES

The States must come into the Indian Union or Pakistan obviously of their own volition. They cannot be coerced into such an entry into the polity of India. In fact, one of the statements of Pandit Nehru at the recent Gwalior Session of the All-India States' Peoples' Conference created for that leader of the Interim Government a delicate situation, for he said that such of the States which choose to remain outside the framework of the Indian Union would be virtually indulging in a hostile act. The fact of the matter is that the States, at any rate some of them, are staying out, and would continue to stay out for some time to come. In other words, the presumption is that the States which stay out of the Union would become the latest sovereign satrapies of the Atomic Age. There cannot be any binding procedure for or controlling authority over, the States, which, for example, was visualised in the Constitution Act of 1935.

The resolutions passed by the Princes on January 29, and on April 2, 1947, which laid down the lines on which the States are willing to treat with the Constituent Assembly now in session and with a Union Centre, are no longer documents of binding value as regards Princely India! In the first place, the prestige, authority and unity of the Chamber of Princes have been reduced to almost the vanishing point, thanks largely to a wide degree of divergence of opinion among the individual

Princes comprising it, leave alone the added difficulties which the staying out of some of the premier States like Hyderabad from the Chamber itself, and the passage of events, after the Cabinet Declaration of May 16, 1946, have brought into existence. Secondly, a good many of the States have already come into the Constituent Assembly without any reference to, and obviously in defiance of, explicit or implied understandings inside the Chamber. Thirdly, it is now widely assumed that the Chancellor of the Chamber of Princes, the Nawab of Bhopal, and the Princes who share his views, are likely to secede from the existing Chamber, and form a body of their own, on the basis of the well-known technique of Pakistan ideology. With all these qualifications, it is clear that these two resolutions of Princely India must be examined in some detail.*

The resolution of January 29, 1947, declares: "The States will retain all subjects and powers other than those ceded by them to the Union. Paramountcy will terminate at the close of the interim period, and will not be transferred to or inherited by the new Government of India. All the rights surrendered by the States to the Paramount Power will return to the States. The proposed Union of India will, therefore, exercise only such functions in relation to the States in regard to Union subjects, as are assigned or delegated by them to the Union. Every State shall continue to retain its sovereignty and all rights and powers, except to the extent that those rights and powers have been expressly delegated by it. There can be no question of any powers being vested or inherent or implied in the Union in respect of the States, unless specifically agreed to by them."

Under their resolution of April 2, 1947, the Princes declared their willingness "to render the fullest possible co-operation in framing an agreed Constitution and to make all genuine efforts towards facilitating the transfer of power on an agreed basis." Basing their position upon the statement of Premier Attlee on February 20, 1947, the Princes declared that "all the rights surrendered by the States to the Paramount Power will revert to them, and they will be in a position, as *independ-*

* Since the above was written, the Chamber of Princes underwent a quick process of disintegration, and was actually wound up.

dent Units, to negotiate freely in regard to their future relationship with others concerned." (*Italics ours.*)

It was on this basis that the Chamber of Princes established a Negotiating Committee which held parley with a similar Committee of the Constituent Assembly, specifically to decide the question of the distribution of seats in the Constituent Assembly (which, incidentally, conforms to the disposition set out in the First Schedule to the Constitution Act), and to determine the method by which the representatives of the States should be returned to the Constituent Assembly.

Pandit Nehru, as spokesman of the Committee of the Constituent Assembly, treating with the States' Negotiating Committee, made three points of importance. In the first place, the Cabinet Mission's Statement of May 16, 1946 was accepted *in toto*, and an assurance was given on behalf of the members from the Provinces in the Constituent Assembly that there would not be any compulsion at all for rulers, as individuals, groups or otherwise, to come into the Constituent Assembly. Secondly, a pledge was given that the Constituent Assembly would not interfere with the monarchical form of government in the Indian States. And, thirdly, an assurance was given that the question of territorial readjustment, which had assumed such a tremendous significance with reference to Indian Provinces (Groups A, B and C)—division, as well as integration—would not arise with reference to the States. However, Pandit Nehru said: "I can concede territorial boundaries being changed for economic reasons, for facilitating governmental purposes, etc., but any such territorial readjustment, we are quite clear, should be made with the consent of the parties concerned, and not be forced down." In other words, it was agreed, as a result of the joint consultations of the Negotiating Committee of the Constituent Assembly and the States' Negotiating Committee, that even for the limited purpose of participation by the States in the Constituent Assembly, the existing structure of Princely India would not be altered—a proposition which naturally could not be presumed to have the consent of the *Praja Mandal* in any individual State. However, even these self-denying ordinances on the part of the representatives of the Provinces in the Constituent Assembly,

and the sacrifice of the democratic principle, had not persuaded *all* the States to come into the Constituent Assembly, even for the limited purpose of discussing the basis on which the States should function in the Union Centre. For, participation in the Constituent Assembly does not, even by the longest chalk, mean adhesion to the Indian Union.*

PRECEDENTS OF CONSTITUTION ACT

It is here that some of the precedents available to us in the Constitution Act become very valuable, in so far as they indicate the manner in which the States might, by and large, have ultimately to decide to come into the Indian Union. Sections 5 and 6 of the Constitution Act deal in an exhaustive manner with the accession to the Federation of the States. While it is true that Federation as envisaged in the Constitution Act is no longer tenable, and that we have marched a good distance away from mere Federation under the Crown—though initially the Indian Union will only have Dominion Status—it is clear that at various points the scheme of Federation adumbrated in the Constitution Act, and the possible series of arrangements which must emerge from present discussions for the participation of States in the Indian Union, overlap each other. (It is gratifying for us to record here that, after this inquiry was completed and the MSS was set up in type, the debate in the British Parliament on the Indian Independence Bill conclusively proved our basic contention that, whether one (particularly the Princes) likes it or not, the Constitution Act still supplies the plinth on which the constitution of the Indian Union, or of Pakistan, must be erected. The Act has no validity in law, but its precedents cannot be ignored at all by constitution-makers today or tomorrow.)

* Announcing his acceptance of the Cabinet Mission Plan of May 16 1946, and his decision to send a delegation to participate in the Constituent Assembly of the Indian Union, the Maharajah of Mysore, in a message read to a press conference at Bangalore by his Dewan on June 17, 1947, observed as follows :

“On the constitutional proposals for the Federation that may emerge from the deliberations of the Constituent Assembly, and on the particular arrangements, agreements or conventions that may be decided upon with special reference to the conditions in Mysore, will depend the ultimate issue whether the State of Mysore should join such Federation or come to any other arrangements with the neighbouring areas.”

Under the Constitution Act, Federation would not have been promulgated unless at least the Princes of the States having an aggregate population of 50 per cent of the total population of all the States declare, through Instruments of Accession, their intention to come into the Federation. No such provision is needed now for the participation of States in the Indian Union, or for that matter in Pakistan. A period of twenty years has been set in under Section 6(7) for the establishment of Federation for the States to come into it, after which special procedure was laid down for the States which initially elected to stand out of the Federation. No such limit is envisaged in the discussions of the Negotiating Committee of the Constituent Assembly and the States' Negotiating Committee, even though the Union Powers Committee has laid down a maximum period of fifteen years for the incoming States to bring their administrative, fiscal and economic systems to the levels prevailing in the Provinces.

Under the Constitution Act, the King would have played a vital role, to the extent that he alone would be the authority for the promulgation of Federation as the Constitution for India. Today the Crown disappears completely, and the Constituent Assembly is the only sovereign body which is to lay down the basis of the Constitution, the terms on which the States are to participate in it, and the Treaty which should ultimately govern the liquidation of the Indo-British relations of the past two centuries.

Two other points of interest must be discussed here. What would be the character of the Instrument of Accession which rulers are to execute with reference to participation in the Indian Union, or in Pakistan? The Constitution Act lays down that the ruler should specify, in the Instrument of Accession binding his State to the Federation, the terms on which he would enter the Federation, and undertake the obligation "of ensuring that due effect is given within his State to the provision of this Act, so far as they are applicable therein by virtue of his Instrument of Accession." The Instrument of Accession shall specify the matters which the ruler accepts as matters with respect to which the Federal Legislature (the Constituent Assembly today) may make laws, and the limitation, if any,

to the power of the Federal Legislature to make laws for his State, and "the exercise of the executive authority of the Federation in his State." There is provision for supplementary Instruments of Accession to be executed by rulers "extending the functions which, by virtue of that Instrument, are exercisable by His Majesty or any Federal Authority in relation to the States." No Instrument of Accession will be deemed valid or accepted by the King, if its terms are inconsistent with the scheme of Federation embodied in the Act. Once an Instrument of Accession has been accepted by the King, "the validity of that Instrument or any of its provisions shall not be called in question," and the provisions of the Act, to the extent accepted in the Instrument of Accession, shall become applicable to the State. Actually, under Section 6(9), "all courts shall take judicial notice of every such Instrument and Acceptance."

If these provisions are any guidance to us, as regards the shape and substance of the Union Centre, it is clear that in the place of the King and Parliament the Constituent Assembly is the sovereign body to treat with the States. States willing to come into the Constituent Assembly and the Indian Union may come in at any time. States come into the Constituent Assembly and the Union Centre, subject only to the terms of the Instrument of Accession executed by each individual State, the presumption being that there would be a considerable degree of uniformity in the terms of the Instruments to be executed by rulers of the States who are willing to come in. The legislative and executive authority of the Indian Union must become exercisable in the States, and can be extended by supplementary Instruments of Accession on the part of rulers, if the need for such arises at any time in the future. The acceptance of supplementary Instruments would be by the Indian Union, which replaces the Crown as entombed in the Constitution Act, but the crux of the situation is that, once the States come into the Indian Union, they cannot opt out, a right which exists with the States only till the time when they stay out of the Union Centre. For, otherwise, vital decisions of policy, whether it be in relation to defence, communications, foreign affairs, taxation, commerce, etc., cannot be

aken by the Union Centre, if there is no guarantee that such of the States which agree to participate in it, at any given time, are bound by them, not only for the time being, but also in perpetuity. In other words, once the States start coming into the Indian Union, even as circumscribed by the Instruments of Accession of the Rulers, to that extent there is fixity and stability for the polity of India enveloping both Provinces and States, which are members integral to the Union Centre, or even for that matter Pakistan.

INSTRUMENTS OF ACCESSION

There are some half a dozen provisions in the Instrument of Instructions (as laid before Parliament by the Secretary of State for India in February 1935), in regard to the special responsibilities of the Governor-General with reference to the States, which have got to be examined here in some detail, though there is the assurance that almost everyone of these special provisions becomes inoperative the moment the Union Centre replaces the existing constitutional set-up, including the Crown.

Section XV reads as follows: "Our Governor-General shall construe his responsibility for the protection of any Indian State as requiring him to see that no action shall be taken by his Ministers, and no Bill of the Federal Legislature shall become law, *which would imperil the economic life of any State or affect prejudicially any right of any State heretofore or hereafter recognised, whether derived by treaty, grant, usage, sufferance or otherwise, not being a right appertaining to a matter in respect to which, in virtue of the Ruler's Instrument of Accession, the Federal Legislature may make laws for his State and his subjects.*" (Italics ours). It is clear that this provision has no meaning at all in the light of what a ruler of a State might do in his Instrument of Accession regarding the Union Centre. In other words, there would not be any agent of the Crown to look after the economic or other interests of a State *vis-a-vis* the Indian Union, for the simple reason that the Crown itself disappears completely from the picture.

The powers of the Governor-General to issue "directions to a Ruler of a Federated State" (Section XX), "to secure the

co-operation" of Federated States (Section XXI), to determine the methods relative to "the imposition of taxes" in Federated States (Section XXII), and to "satisfy himself that the results of all practicable economies and of all practicable measures for increasing the yield accruing to the Federation from other sources of taxation within the powers of the Federal Legislature would be inadequate to balance Federal receipts and expenditure on revenue account" (Section XXIII), which have been specifically indicated in the Instrument of Instruction, also become inoperative on the above showing. Section X of the Instrument of Instructions which vests the Governor-General with special responsibility "for safeguarding the financial stability and credit of the Federation", as well as that the institution of a budgetary or borrowing policy would not "seriously prejudice the credit of India in the money markets of the world, or affect the capacity of the Federation duly to discharge its financial obligations", is yet another example of a thing that was within the reach of Federation, and that would not be available to the Indian Union.

There is a curious lacuna in the Instrument of Instructions to the Governor-General which merits notice here. Sections XXIV and XXV of the Instrument deal with the powers of the Governor-General to determine "whether the Federation would or would not be justified in refusing to make a loan to a Province, or to give a guarantee in respect of a loan to be raised by a Province, or in imposing any conditions in raising such a loan or guarantee." This is a special responsibility of the Governor-General with respect only to Provincial borrowing—that it must necessarily be in conformity with the policy of the Federation, and it is a glaring omission that no reference was made to the borrowing policy of any State which might enter the Federation under the set-up of the Constitution Act. The question naturally arises as to what would be the position of a State entering the Indian Union, or Pakistan, with respect to borrowing policy, and the numerous problems involved in the raising of loans for the especial benefit of individual States?

In other words, will the Union Centre, or Pakistan, permit any member State thereof to pursue a borrowing policy totally unrelated to those which are in operation within their respect-

ive politics, leave alone the question of a possible conflict between the policy of the Union and the policy of the State concerned? Obviously, the answer is based upon the specific provision in the Instrument of Accession of the ruler of a State with respect to questions of this character. The initiative and competence of a State to pursue a borrowing policy, may be at complete variance with that of the Union Centre, are possible, unless they are specifically surrendered by the ruler concerned into the pool of Union polity. As we have noted elsewhere in this Chapter, it is quite conceivable that a state of chaos might ensue, at any rate during the initial period of life of the Indian Union, with respect to questions of high economic and financial policy, to the extent to which States do not subscribe on a uniform basis alongside of the Union Centre.

NEED FOR UNIFORM ACCESSION

It is necessary here to examine the broad implications of Sections 145 to 149 of the Constitution Act, which define the functions of the Crown Representative in his relations with individual States members of the Federation, regarding income-tax, immunities as a broad category, specific treaties between the Crown and the States with respect to military assistance on a two-channel basis (meaning thereby the duty of the States to supply military assistance to the Crown, and/or the obligation of the Crown to give protection to the States), and a host of other provisions. Obviously, the abolition of the Crown creates a gap in the administrative and political relationships between the States on the one part and the Union Centre on the other, unless it be that each individual State enters into a specific agreement covering all aspects of these questions facing the Union Centre. This is a proposition, as we have repeatedly pointed out, which is not feasible in the present circumstances, the reason being that it is the discretion of the ruler of a State to execute or not to execute an Instrument of Accession enveloping any or all these points.

It is, thus, that we come to the final proposition relating to the Union Centre *vis-a-vis* the States. There must be some method of arriving at the basis of an Instrument of Accession for and on behalf of the ruler of a State, which would answer

the requirements alike of the State entering the Union, and of the Union which accepts such entry. Who is to bring about this model Instrument of Accession is a point of considerable importance. Obviously, the Negotiating Committee of the Constituent Assembly and the States' Negotiating Committee must sit together, and work out details of such a model. In the prevailing chaos in the Princely Order, it is possible that the difficulties would become almost insuperable. It is conceivable that even if there are two Chambers of Princes, and even if there is more than one Constituent Assembly for the Indian Provinces, a platform of approach between the various warring elements can be brought together for the specific purpose of laying down the broad principles of this Instrument of Accession. Such a model Instrument must lay down the minimum conditions relating to defence, foreign affairs, communications, fiscal and economic policy, etc., which the rulers of States must undertake to adhere to, before they are admitted into the Union. (As these pages are being printed off, we learn that gigantic efforts are being made by representatives of both the States and the Provinces to see that a standard Instrument of Accession is evolved, to which every Prince wishing to enter the Indian Union might signify his assent. Such an Instrument must perforce be of a very general nature, enveloping such broad categories of subjects as defence, foreign affairs and communications. Most of the questions dealt with in this inquiry such as taxes on income, customs, excises etc. will have to be taken up at a later stage, possibly through supplementary Instruments of Accession, and a stand-still period covering the multitude of existing arrangements between the Paramount Power and the States is being agreed to.)

Once such a model Instrument of Accession is arrived at, naturally the question arises as to the Authority which is to enforce the observance of the conditions of the Instrument for and on behalf of the States. In other words, is the Union Centre, inclusive of such of the States which choose to go into it, competent to enforce the observance of the Instrument of Accession executed by the rulers? Competence of this character includes presupposition of the existence of a breach of observance on the part of the States, and an agency of sanctions

behind the proposed *regime*. This is a domain which is very delicate to tread, for the States and their *durbars* would bring in the question of their respective sovereignties. Much as we deplore a possible clash of the *bona fide* needs of the Union Centre and the respective sovereignties of the States, it is clear to us as crystal that, without a uniform method of entry of the States into the Indian Union, and the provision of sanctions for the observance of obligations undertaken by the States entering the Union, it is impossible for the Union to exist with any purposiveness. It is here that we bring ourselves to the position of disagreeing with the operative portion of the recommendation of the Interim Report of the Union Powers Committee of the Constituent Assembly, which postulated a period of fifteen years for the emergence of uniform practices, at any rate as far as fiscal and economic matters are concerned, on the part of the States entering the Union Centre. .

For the purposes of this Chapter, it is clear that there should not be any undue haste on the part of the Constituent Assembly to rope in as many States as possible and make them function in the Union Centre, without obtaining a prior guarantee that the incoming States would recognise their responsibilities on a uniform basis, and that there would be means at the disposal of the Union Centre to see that the obligations thus undertaken are enforceable. It is here that we lay special emphasis upon the provision of the Constitution Act, Section 6(9), which laid down the principle of judicial cognisance by Courts of Instruments of Accession executed by the rulers of States which enter Federation. In other words, the highest tribunal of the Union Centre must have power to take notice of an Instrument of Accession on the part of the ruler of a State which enters the Union, on a basis which is similar to the procedure relating to any justiciable dispute. This is what the White Paper of December 1931 (paragraph 117) said on this question: "If any provision of a law of a State is in conflict with an Act of the Federal Legislature regulating any subject which the Ruler of that State has by his Instrument of Accession accepted as a Federal subject, the Act of the Federal Legislature, whether passed before or after the making of the law of the State will prevail." Obviously, the right to move the Court in the case

of a dispute, rests equally with the Union Centre on the one part and the constituents on the other (States as well as Provinces), in respect of disputes as between the Union Centre and the Units forming the Union, as well as the Units *inter se*.*

It is clear that the rulings of the highest Court on disputed points cannot be merely advisory. Section 212 of the Constitution Act runs as follows: "The law declared by the Federal Court and by any judgment of the Privy Council shall, so far as applicable, be recognised as binding on, and shall be followed by, all courts in British India, and, so far as respects the applicability and interpretation of this Act or any Order-in-Council thereunder, or any matter with respect to which the Federal Legislature has power to make laws in relation to the State, in any Federated State." It is obvious that the States coming into the Union Centre must be on a par with the Provinces which are members thereof, in regard to the enforcement of the jurisdiction of the highest Court of the Union Centre, in disputes relating to the Instruments of Accession. In other words, States coming into the Union Centre shall accept the award of the highest Court of the Union Centre as mandatory, and today the question of appeal to the Privy Council does not arise at all. We are most anxious to avoid the situation, in the inter-war period, which faced the Permanent Court of International Justice, which had only power to deliver advisory opinions on disputes referred to it by the Council of the League of Nations in respect of member States of the League of Nations. One trite illustration which comes to our mind is that relating to the Austro-German Customs Union which was referred by the League Council to the Permanent Court in 1931. We consider that merely advisory opinions on the part of the highest

* The *Joint Parliamentary Committee Report* (Vol. I. paragraph 156) runs as follows :

"It would, we think, be very desirable that the Instruments of Accession should in all cases be in the same form, though we recognise that the list of subjects accepted by the Ruler as Federal may not be identical in the case of every State. Questions may arise hereafter whether the Federal Government or the Federal Legislature were competent in relation to a particular State to do certain things or to make certain laws, and the Federal Court may be called upon to pronounce upon them; and it would, in our opinion, be very unfortunate if the Court found itself compelled in any case to base its decision upon some expression or phraseology peculiar to the Instrument under review and not found in other Instruments."

Court of the Union Centre would not meet the requirements of the situation created by the accession of a State to the Union Centre.

An Instrument of Accession, by its very nature, is the equivalent of a solemn treaty between two high contracting parties, pledged to securing common ends which are mutually beneficial. Such a treaty must provide within its own framework sanctions for enforcement, in the event of non-observance or breach thereof. As regards the Provinces, in their relation with the Union Centre, such a question does not arise, but with respect to Indian States punctiliousness on the part of the rulers, about attributes of sovereignty they are supposed to enjoy, would definitely create complications for the Union Centre in the future, and as such they must be forestalled right at the beginning.

The presumption must be accepted by all the parties that, in the event of a breach of observance of contractual obligations, even as defined in the Instrument of Accession of a ruler, the highest Court of the land must have the enforceable right of adjudication. On top of this, the presumption must also be there that the Union Centre does necessarily possess the enforcement machinery, viz., the army, to secure observance by the States concerned of obligations which are established, so to speak, by the highest Court of the land.* We should not be misunderstood into stating that the Union Centre must coerce the States into participation, but we definitely insist upon the point that once the States enter the Union Centre, they would obtain treatment no more different than that available to Indian Provinces under the Union Constitution. Otherwise, even so much as the loose framework of a *zollverein*, insufficient as it is on points, would not be available to the Union Centre, for Princes in the panoply of their medieval glory might develop centrifugal tendencies which would destroy the very framework of the Union.

* Let us record here the point that in June 1947 it was reported that the Political Department had fined two Central India States for black-marketing activities !

INCIDENCE OF PARAMOUNTCY

There is no single categorised basis on which the treaties, engagements and *sanads* between 582 Indian States on the one part and the Paramount Power on the other have been arrived at in the historical period. Apart from this lack of uniformity and precision in regard to *all* rights and obligations *inter se* of the States and the Paramount Power, a definition of the rights of the same State in relation to the Paramount Power, and a subtraction therefrom, in order that the *regime* of the Paramount Power is made possible, has been attempted times out of number during the past two hundred years. It would be a futile attempt to plunge into the morass of the treaties, engagements and *sanads* listed by Aitchison, in addition to those which came into existence since the last edition of Aitchison was issued by the Political Department. But it is necessary for our purpose here to take a few samples of the *outer limits* under which treaties and engagements and *sanads* were contrived as between the Paramount Power on the one part and the States on the other. The following analysis of some of the treaties is purely illustrative in character, and, in more cases than not, deals with the extreme positions taken up by the Paramount Power with respect to the series of questions subsisting between itself and the States.

As regards Defence, the treaty between Kapurthala and East India Company of 1806 prohibits (Article I) the State from entering into relations with enemies of the Government of India, or from committing hostile acts. Under Article IV of the Proclamation No. I of 1809, Kapurthala is bound to render military aid, and supply provisions, etc., to meet the requirements of the army passing through its territories. The proclamation of 1809 also provides for the free passage of European goods required for the army passing through the State's territory. *Sanad* No. LXXI of 1859 confers upon Kapurthala certain estates in recognition of services rendered during the Indian War of Independence of 1857, under certain conditions, one of which is the rendering of military aid on requisition by the Crown. Agreement No. XXI of 1899 deals with discipline, etc., of Kapurthala Forces serving outside the

State boundaries. In 1923, the *darbar* of Kapurthala agreed to the reorganisation scheme of the Indian Forces of 1921.

In the sphere of communications the agreement No. XC of 1899 between the Faridkot State and the Crown offers a trite example. Under this agreement, the State assumed an obligation to furnish materials required for construction of rail roads, railway stations and imperial roads and purchase at current rates and to give land freely for the construction of railroads and imperial roads, (Cf. clause No. VIII of *Sanad* No. LXXIX of 1863). "Full and exclusive jurisdiction of every kind" was surrendered by the Bhagat State in respect of its lands occupied or to be occupied by the Simla Kalka Railway, according to Agreement No. LXVII of 1901. Almost everyone of the undertakings between the Crown on the one part and the States on the other, in the realm of communications, contains provisions for the surrender by the States concerned of the jurisdiction over railway property and over railway police, leave alone the supply of land and materials either free or at concessional rates.

The Postal Convention concluded between the Paramount Power and the Chamba State (No. XCV of 1896) provides for preferential treatment to the Paramount Power in regard to postal matters within the territorial limits of the State, involving, as protagonists of States put it, encroachments upon the sovereignty of the State. Under Article III, the State is required to sell and use within its territories Indian postal stamps, post-cards and embossed envelopes, though the same are overprinted with the words "Chamba State" for use of private individuals, and with the words "Chamba State" and "Service" for official use, and are supplied by the Paramount Power at the cost price. In other words, the State is debarred from printing its own postage stamps, post-cards and envelopes bearing its own coat-of-arms. The mutual exchange of correspondence, parcels and money orders between the post-office of the Provinces and the State Post are governed by the rules in force, for the time being, in the Indian Postal Guide. The State is under an obligation not to enforce rates of postage fees or commissions, on all classes of correspondence, on all parcels and on all money orders, which are in excess of the rates charged by

the Indian Post. Chamba has been deprived of its share of income in respect of foreign correspondence and parcels when posted within the State's territory. Postage can be prepaid only by means of Indian postage stamps not bearing the overprint "Chamba State". In the case of foreign correspondence and parcels addressed to any place in the State or unpaid or insufficiently paid, they shall, on payment of the tax thereon, be delivered to the Chamba Post, by the Indian Post, and the amounts thus collected shall be remitted to the Paramount Power. On the other hand, fully paid foreign correspondence and parcels addressed to any place in the State shall be delivered by the State Post free of all charges on account of postage.

With reference to transit duties, the treaty of 1833 (No. XXIX) between Bahawalpur and the East India Company is extremely interesting. Under this treaty, which opened traffic on the Indus and the Sutlej, a fixed tariff alone can be levied at only two places in the State's territory, viz. Mithankot and Hariki. Under subsequent arrangements between Bahawalpur and the East India Company, a toll on boats was substituted by tariff. Under the Agreement of 1843, No. XXXIV, these tolls were reduced by one half, and a scale of duty was fixed on merchandise in transit through the State by land. In 1847 the State remitted, at the instance of the Paramount Power, duties on boats passing through its territory. In 1855, when the Sind postal authorities proposed to establish a camel train through Bahawalpur, the *darbar* reduced the duty on goods passing by the inland route, in addition to consenting shortly afterwards to revised ferry rates on the Sutlej, reducing them to a reasonable remuneration. Under Article VI of Treaty No. XXIX of 1833, Bahawalpur agreed to fix ceilings to duties levied on merchandise in transit on the rivers Indus and Sutlej, and undertook *never* to increase or diminish the same, except with the consent of the Paramount Power. Under the Agreement No. XXXIV of 1843, the *darbar* undertook to keep in good repair *pukka* wells and caravansaries for the comfort of travellers from Bahawalpur to Sirsa, as well as to maintain a road along that route. Article III of Agreement XXX of 1835 provides for the stationing of British officers, with full control over the working of the agreement, in the matter of the

taxing of merchandise and the apportioning of the income accruing therefrom, between the Paramount Power on the one part and the State on the other. This, surely, is a point which the spokesmen of Bahawalpur claim to be an encroachment on the executive and fiscal sovereignty of the State, and on its free and inherent sovereign rights to impose taxation.

The Abkari and Opium Agreements between Baganappalle and the Paramount Power must now be examined as illustrative of the rights generally conceded by the States to the Crown. The Baganappalle Administration was taken over, between 1922 and 1929, by the Paramount Power owing to maladministration, and it is now complained that an agreement (No. XXXVIII) of 1924 was imposed upon the State, entailing restrictions upon the executive, legislative, and fiscal jurisdictions of the State. Under this agreement, the Madras Abkari Act was enforced within the limits of the State's territory. During the term of this Abkari and Opium administration of the State, an officer of the Paramount Power was invested with powers to enforce the principles and rates of taxation on and the selling prices of liquor, ganja, opium, etc., as they existed in the adjoining Madras district of Kurnool, thus bringing about the unity in the excise administration of the State's territory and the territory of the adjacent Indian Province. The State was only entitled to the net collections of the Abkari and Opium department within its territory. It was, however, provided that in case of a non-renewal of this agreement by the State, the Abkari and Opium administration shall be conducted on the following principles: the Abkari and Opium laws of the State and the rules thereunder must conform to those prevailing in the Kurnool District of the Madras Presidency; the rates of taxation on liquor, ganja, opium, etc., must be equivalent to those in force, for the time being, in the Kurnool District; the management of the State's revenue from these sources shall be such that they do not in any way injure the Abkari and Opium revenue of the Kurnool District.

As regards forests, the Chamba Agreement, already referred to with reference to postal matters, authorises the Paramount Power to invest the forest officers appointed by them in the Chamba forests with all or any of the powers of a magis-

trate, as prescribed in the Code of Criminal Procedure in force in Indian Provinces, to be exercised within the Chamba territory for the purpose of trial and punishment of offenders against the rules set forth in the Schedule annexed to the Agreement. The Agreement binds the ruler of Chamba to render every assistance required by the officer or officers authorised by the Paramount Power to exercise these powers, both for bringing to justice all persons committing offences against the rules, as for enforcing the judgments awarded against them. It is claimed by the *darbar* that even though the agreement was designed as a *lease*, the powers vested with the officers of the Paramount Power subtract from the judicial sovereignty of the Chamba State, in so far as jurisdiction over forest administration was removed from the competence of the State Administration. The protests from Chamba have led to an alteration of this agreement, but it is clear that the precedent involved in the compulsory taking over of the jurisdiction impinges heavily in its incidence upon Princely India.

There are hundreds of similar agreements with individual States which deal with a heterogeneous mass of other questions, like customs, salt etc., and in every one of these there is an "infringement" of the sovereignty of the States by the Paramount Power. Indeed, the incidence of Paramountcy had cost a tremendous lot to the States. Yet, it is a tragedy which flows out of the abolition of Paramountcy that these very States, which had accepted these encroachments willingly or under duress for two centuries, do not agree to do the same with reference to the Union Centre, even on the assurance that such a surrender alone can make their continued existence as entities possible.

REPOSITORY OF FINANCIAL MATTERS

We consider that the provisions of the Constitution Act, Part VII, in relation to the entry of the States into the Federation, especially delineating the special financial relationship between the Crown on the one part and the States on the other, are no longer valid today, for the specific reason that the Crown disappears from the scene and the States are left to stand high and dry, with only their voluntary decisions linking them to

the Union Centre. Such, indeed, is the implication of Sections 145 and 146 of the Constitution Act which make the Crown the repository of monies from the States, which are necessary for the discharge of the functions of the Crown, which today yields place to the Union Centre. The position indicated in Section 147, however, is vitally different, and comes into the general pool of precedents available to the Union Centre for the regulation of the relationships of the Union with the incoming States. It is quite true that "cash contributions" which States were habituated to pay to the Crown, might have to be remitted, when the Instrument of Accession of States under the Constitution Act was accepted by the Crown over a period of years. Such, again, is the position of privileges and immunities enjoyed by the States under the Crown. These questions are discussed at length in the next Chapter, and here we are only concerned with the constitutional position relating to them.

The abolition of the Crown, which is involved in the Quit India decision of His Majesty's Government, would automatically involve the wiping out of the vast group of arrangements relating to procedure and finance built up by the Political Department, since Lord Clive's "victory" at Plassey. The lists of cash contributions and privileges and of immunities, as mentioned in Section 147 of the Constitution Act, would become more or less inoperative. The Crown disappears from the political scene of India, without another agency automatically taking its place and becoming successor to it, in respect of the relations of States to the Union Centre, or for that matter Pakistan. Furthermore, the Instrument of Accession on behalf of any State, which should have obtained the consent of the Crown, whatever its provisions might be, has now to specify, on the volition of the ruler concerned, the manner in which all these and many more of the intricate questions, involving the relations of the States and the Union Centre or the States *inter se* and with the Provinces, are to be regulated.

Whether, and if so, how soon, any or all the States entering the Union Centre, or Pakistan, would agree to a uniform procedure in respect of these vital questions of finance cannot be stated with any degree of certainty today. Since the Political Department ceases to function as the *mahout*, exercising sup-

reme direction and control over the fortunes of the States, it is clear that a certain amount of anarchy would enter into the attitude of the States in their projected relationships, including possibly abandonment of relationships, with the Union Centre. We should not be misunderstood as suggesting that the Political Department, or the dozen Regencies as they exist in India today, should continue. On the contrary, our anxiety is to demonstrate, and put beyond any shadow of doubt, the fact that since the Constituent Assembly is sovereign only with reference to Indian Provinces; since the States are perhaps more functionally sovereign than the Constituent Assembly itself; and since each individual State must, of its own accord, come to a decision as to a serried phalanx of items on which it is prepared to surrender its prerogatives into the common pool of the Union Centre; it is clear that there would be the maximum amount of confusion in the delineation of the relationships between the Union Centre on the one hand and the heterogeneous mass of States on the other.

We might as well illustrate this proposition a little further. It might be the question of the personal salute of a ruler which might become the stumbling block to the functioning of a State inside the Union Centre. If the Viramgam Customs cordon is to be abolished and the Union Centre is to propose the taking over of sea customs generally, not only the future of the States of Kathiawar and Cutch and other maritime States becomes definitely involved, but the entire Union *regime* of sea customs is in peril. If land customs are taken over, Kashmir might certainly throw the spanner into the works of the Union Centre. In all certainty, the Nizam would insist on his pound of flesh with respect to his demand for egress to the sea both to the East and the West, leave aside the unbridled recognition of his sovereignty over Berar. Later in this book we would show the manner in which the application of income-tax, excise, and other taxation measures would put the Union Centre almost at the mercy of each individual State, which in its own discretion has to agree to, or reject suggestions made for, the evolution of common fiscal system for all of the unionised territories.

Such, again, is the implication of Section 198 of the Constitution Act, which runs as follows: "If and in so far as His

Majesty's Representative for the exercise of the functions of the Crown in its relation with the Indian States may entrust to the Authority [the Statutory Railway Authority] the performance of any functions in relation to Railways in an Indian State *which is not a Federated State*, the Authority shall undertake the performance of those functions." (Italics ours). What would happen if the Nizam does not come into the Union Centre, to the Railway system connected with, or passing through, his territories? Perhaps, the position of Bhopal is more intricate in this regard than that of the Nizam's Dominions. The Crown would not be there to instruct the Statutory Railway Authority of the future—and some such Authority must come into existence, not necessarily on the lines indicated in the Constitution Act—and the Union Centre cannot possibly impose a *regime* of administration upon any State which elects to stay out of the Union.

If the threat of the Dewan of Travancore, to keep that State out of integral relationship to the rest of the country, becomes a fact, even the establishment of something like the Virangam customs cordon round the State territory would not solve the stupendous problem of sea customs which is likely to be created for the Union Centre.* As we have said earlier,

*It is difficult to pursue here the tortuous course of controversy which the Dewan of Travancore has raised on the question of the sovereignty and independence of Travancore after the lapse of Paramountcy. Gandhiji, Pandit Nehru, Sir Alladi Krishnaswami Iyer, Sir N. Gopalaswami Iyengar and Mr. Pattom Phanu Pillai (on behalf of the Travancore State Congress) have all entered the lists with Sir C. P. Ramaswami Iyer in this regard. Dr. B. R. Ambedkar argued that since the Indian Union and Pakistan become Dominions under the plan of June 3, 1947, the Crown cannot divest itself of its Paramountcy!

While the controversy drags on, the Dewan of Travancore has called for a fight between his Maharaja and the people of the State. On June 20, 1947, a press note was issued by the Travancore Government appointing a Delhi Representative of the State, meaning thereby an Envoy to the Indian Union. The very next day, the following press *communiqué* was issued from Trivandrum: "As a result of personal discussions and correspondence between Mr. Jinnah and the Dewan of Travancore, the Dominion of Pakistan, on its establishment has agreed to receive a representative of Travancore and to establish relationship with this State which will be of mutual advantage. In pursuance of this decision, the Travancore Government have nominated Rajyaseva Pravina Khan Bahadur Abdal Karim Sahib, retired Inspector-General of Police, Travancore, as Representative of Travancore State in the Dominion of Pakistan, and he will take charge of his duties from the date on which Paramountcy lapses and Travancore becomes independent."

The Maharaja of Travancore, in a broadcast to his people on July 18, 1947, declared: "Travancore will realise its destiny as a Sovereign

since under the 'existing procedure relating to the entry (including possible non-entry) of the States into the Union Centre, or Pakistan, and in the absence of the exercise by another body of the direction and control of the Crown which lapses, a position very nearly analogous to that prevailing in medieval times might eventuate in this country in the immediate future. Indeed, it would be important for the Constituent Assembly, as at present constituted, or even for a later edition of the Constituent Assembly in which *all the States* agree to function, to tie up the loose ends of problems of polity and administration involved in the liquidation of the Indo-British connection of the past two centuries.

INCIDENCE OF SOVEREIGNTY

We have said enough to show the complexity of the problems involved in the unionisation of the Provinces and the States, with the reference to the Union Centre, as much as with reference to Pakistan. We deplore sincerely the lack of provision for automatic entry of the States into one single Indian Union or more than one single Indian Union. We deplore, again, the lack of suitable criteria on the basis on which the States are to come into the unionisation schemes. Furthermore, we deplore the lack of uniformity for the entry of the States, and the lack of a compelling authority behind such entry.

The interim report of the Union Powers Committee of the Constituent Assembly has laid down a maximum period of fifteen years, during the course of which such of the States as come into the Union Centre are to bring up their administration and other practices into line with those of the Provinces. The following is a relevant quotation from this report: "We realise that, in the matter of industrial development, the States are in varying degree of advancement, and conditions in British India and the States are in many respects dissimilar. Some of the above taxes* are now regulated by agreements between the

State, working in close collaboration with the rest of India in all matters of common concern."

*The taxes referred to are customs, including export duties; excise duties; corporation tax, taxes on income other than agricultural income; taxes on the capital value of the assets, exclusive of agricultural land, of individuals and companies; taxes on the capital of companies; duties in respect of succession to property other than agricultural land;

Government of India and the States. We, therefore, think that it may not be possible to impose a uniform standard of taxation throughout the Union all at once. We recommend that uniformity of taxation throughout the Units may, for an agreed period of years after the establishment of the Union, not exceeding fifteen, be kept in abeyance and the incidence, levy, realisation and apportionment of the above taxes in the States Units shall be subject to agreements between them and the Union Government. Provision should accordingly be made in the Constitution for implementing the above recommendation."

We agree that at the time when the Union Powers Committee drafted its report, and especially in the light of the knowledge that Britain was getting ready to quit India, no other recommendation could have been possible. But it is clear that the proposed entry of the States into the Union Centre, or into Pakistan, would, under this proviso, become haphazard, and unequal in its incidence, *vis-a-vis* the position of the Provinces. In the realm of foreign affairs and international relations generally, and especially in regard to the implementation of international conventions, particularly of the International Labour Organisation, the utter untenability of the position relating to volition on the part of the States, to do or not to do a thing with reference to the Union Centre, become particularly apparent. Here we are content with re-stating the proposition that the conditions for the entry of the States into the Union Centre are purely one-sided, and that they put a premium on lukewarmness and recalcitrance on the part of even such of the States which agree to come into a unionised polity. It is difficult to write about the amount of friction which would eventuate from the lack of control over the entry of the States into the Union Centre on a basis which is not only uniform *intra se* of the States, but also from the lack of expedition with reference to the manner in which the Provinces are to be yoked to the States, in order that the chariot wheels of the Union run smoothly and swiftly.

It is obvious that once the Union Centre comes into being

estate duty in respect of property, other than agricultural land; and fees in respect of any of the matters in the list of Union powers, excluding Court fees, other than the Union Court.

as a result of the framing of a Constitution by the Constituent Assembly and the promulgation of an Indo-British Treaty, the *role* played by the Governor-General in the regulation of the affairs of the Federation, as envisaged in the Constitution Act, would be drastically altered or completely abolished. The Constituent Assembly on January 22, 1947, passed a resolution declaring the future Constitution of India to be a Sovereign Republic,* and it is the Constituent Assembly which becomes the supreme arbiter of the fortunes of the Union Centre, and of the States, for while the States which become unionised are bound by its acts, those which do not are affected by the consequences of those acts.

We, for our part, would envisage a definite period to lapse before such a Sovereign Union Republic comes into physical existence, though reports have gone forth to the effect that the Provincial Governors are resigning in August 1947, to be replaced by elected heads, and that the Governor-General would

* The following is the text of the Resolution :

“(1) This Constitution Assembly declares its firm and solemn resolve to proclaim India as an Independent Sovereign Republic and to draw up for her future governance a Constitution ;

(2) WHEREIN the territories that now comprise British India, the territories that now form the Indian States, and such other parts of India as are outside British India and the States as well as such other territories as are willing to be constituted into the Independent Sovereign India, shall be a Union of them all ; and

(3) WHEREIN the said territories, whether with their present boundaries or with such others as may be determined by the Constituent Assembly and thereafter according to the Law of the Constitution, shall possess and retain the status of autonomous Units, together with residuary powers, and exercise all powers and functions of Government and administration, save and except such powers and functions as are vested in or assigned to the Union or resulting therefrom ; and

(4) WHEREIN all power and authority of the Sovereign Independent India, its constituent parts and organs of government, are derived from the people ; and

(5) WHEREIN shall be guaranteed and secured to all the people of India justice, social, economic and political ; equality of status, of opportunity, and before the law ; freedom of thought, expression, belief, faith, worship, vocation, association and action, subject to law and public morality ; and

(6) WHEREIN adequate safeguards shall be provided for minorities, backward and tribal areas, and depressed and other backward classes ; and

(7) WHEREIN shall be maintained the integrity of the territory of the Republic and its sovereign rights on land, sea and air according to justice and the law of civilised nations ; and

(8) this ancient land attains its rightful and honoured place in the world and makes its full and willing contribution to the promotion of world peace and the welfare of mankind.”

be replaced by a President of the Indian Union, though nothing can be said at the moment about Pakistan, unless Mr. Jinnah declares himself to be its Sultan.* Actually, the assurances given by Pandit Nehru on behalf of the Committee of the Constituent Assembly which negotiated with the States' Negotiating Committee, concerning the continuation of monarchical form of Government in the States, seems to us to be a considerable impediment, at any rate for the immediate establishment of a Sovereign Republic of the Indian Union, which must obviously include within its framework a considerable number of States. Thus, the two issues involved in the work of the Constituent Assembly are clear. If a Sovereign Republic is to be created, the Indian Union would have to surmount almost insuperable difficulties involved in the perpetuation of monarchical government in the States which are, or become, members of the Union. On the other hand, if there is a time lag—and we definitely assume such a time lag—between the completion of the work of the Constituent Assembly and the inauguration of the future Sovereign Republic of India, the position of the Governor-General in relation to the executive authority of the Union Centre must be subject to radical alterations, in order that both the legislature and the executive, which must come to function in the name of the people of India, annex unto themselves the functions and prerogatives so far enjoyed, under the Instrument of Instructions, by the Governor-General and the Governors.

For nearly two centuries, the Indian Princes have continued to exist as the pampered darlings of British Imperialism. Their servility to the Crown has become notorious in the annals of world history. The States have for long centuries continued to dot the political and economic map of India as so many leprous patches, preventing integration of the life of four hundred million people. In theory the States are sovereign, at any rate internally, and their sovereignty is nothing other than medieval despotism. The Crown has sustained this despotism in the

*Mr. Jinnah has contrived to get himself designated as the Governor-General of Pakistan, while Lord Mountbatten continues to be the Governor-General of the Indian Union. When the promised Socialist Pakistan Republic is established, it is certain that Mr. Jinnah's designation as Chief Executive will certainly undergo a change!!

modern age. The economic depravity of the States must be traced to inaction and maladministration on the part of the rulers on the one part, and their condonation by the Crown, meaning thereby the Political Department at New Delhi on the other. Assertion of popular feeling inside the States has been ruthlessly suppressed all these long decades since the death of Maharaja Ranjit Singh, and, more often than not, the British bayonets behind the Princes must claim responsibility for this state of affairs. Is it not a fact that one of the operative clauses of a subsidiary alliance between an Indian Prince and the old East India Company *Bahadur*, of which the British Crown is the legal successor today, that the Prince concerned in the Treaty must be protected against aggression from without, as well as aggression (meaning thereby a demonstration of the will of their own subjects) from within? The Princes of India have for long thwarted the freedom movement with impunity. As we write, the Nawab of Bhopal and his henchmen are trying to cut Princely India into two portions, so that Hindu and Muslim among the Princely Order would find themselves ultimately ranged in serried phalanxes, so that the battles of Pakistan are fought with logic, if not to a decisive conclusion.

NO RIGHT OF SECESSION

We consider that the British Government had, even on the showing of Mr. M. A. Jinnah, broken faith with India and the people of India in the May 1946 Declaration, when the Cabinet Ministers were allowed to announce to the world that Paramountcy would be re-vested with the Princes, the moment the Constituent Assembly for the Provinces formulates its own Constitution, as well as the first principles of an Indo-British Treaty.* After the passage of one year since this Declaration

* In contradiction to the Congress stand on Paramountcy, Mr. M. A. Jinnah, declaring the attitude of Pakistan, said in a statement issued on June 17, 1947, as follows :

“ Constitutionally and legally, the Indian States will be independent sovereign States on the termination of Paramountcy, and they will be free to decide for themselves to adopt any course they like. It is open to them to join the Hindustan Constituent Assembly or the Pakistan Constituent Assembly, or to decide to remain independent. In the last case, they can enter into such arrangements or relationship with Hindustan or Pakistan as they may choose. In my opinion, they are free to remain independent if they so desire. Neither the British Government, nor any power or body can compel them to do anything contrary to their

was made, it is now abundantly clear that this re-vesting of sovereignty with the Princes is but the latest example of the principle of *divide et impera*, which has been the sheet-anchor of British colonial policy for nearly three centuries. Maharaja Ganga Singh of Bikaner, Maulana Mohammed Ali and others, who participated in the Federal Structure Sub-Committee of the First Round Table Conference, must have turned in their graves at this breach of faith on the part of Britain with the people of India, for having deliberately encouraged recalcitrance on the part of Indian Princes *vis-a-vis* the Union Centre, or for that matter Pakistan. Even that mild provision of Section 5 (2) (b) of the Constitution Act, which provides for the automatic inauguration of Federation, the moment States with an aggregate population of at least one half of the total States' population come into the Federation, is not there with us today. It is arguable and is argued that the Union Centre can come into being without one single State participating in it. It is also arguable and is argued here that quite a good number of Indian States, leave aside the sabre-rattling of the Dewan of Travancore and of Bhopal and Hyderabad for the time being, can successfully elect to stay out of the Union Centre, or even of Pakistan, for a definite length of time, imperilling the ultimate success of a polity and an economic system for the country as a whole, which the constitution-makers in this country and England were pledged to bring into existence.

In spite of numerous impediments in the way of the progressive realisation of a people's polity in India during the past one century in particular, thanks to the preservation of Princely India as a watertight compartment, Britain had seen to it that in all essentials, at any rate in the economic system, the States were brought more or less into line with the Provinces. An overall customs *regime* has been in operation, bringing in its train the benefits of a unified fiscal and economic system for the country as a whole. Especially during the seven

free will and accord, nor have they any power or sanction of any kind to do so. The British Government have made it clear that Paramountcy will not be transferred to any government or governments or authority that may be set up in British India, and that itself shows that Paramountcy cannot be transferred but is going to terminate. On its termination, the full sovereign status of the Indian States emerges."

years of the recent world war, the integration of the economies of the States with the economies of the Provinces has been brought to such a degree of precision, that all patriots in the country have come to visualise the eventual establishment of a unified economic system for these respective portions of a possible Indian Union Centre. The revesting of sovereignty with the Princes, and the lack of provision for their automatic entry into the Union Centre constitute, to our mind, a step analogous to Ulsterisation, which Britain practised with reference to Eire, in the sense that quite a number of Indian States can :

(1) thwart the establishment of a Union for the country as a whole by taking sides in the politics of Hindustan and Pakistan ;

(2) retard the pace at which either the Union Centre or Pakistan are to be brought into existence ;

(3) prevent the evolution of an economic, political and administrative system with respect to the Union Centre, or Pakistan, even as the showing of the interim report of the Union Powers Committee, which conceded a period of fifteen years for bringing the Indian States up to the standards of the Indian Provinces ; and

(4) threaten to secede from the Union, or Pakistan, at any future date, putting in permanent jeopardy the prospects of the Union Centre as formed, or of Pakistan.*

We cannot overemphasise the point that the lack of a binding provision with respect to Union membership in perpetuity, once a ruler of a State executes an Instrument of Accession on behalf of his State contracting into the Union, is a disaster. This leads us to the position that everything depends upon the scope and content of an Instrument of Accession, which cannot be left to the sweet will and discretion of the ruler of a State.

*The right of secession on the part of a State which comes into the Union Centre, or Pakistan proper, is a question which has been left undefined up to the moment. Does it mean that when once the Ruler of a State executes an Instrument of Accession and participates, on specified conditions, in the Union Centre or in Groups B or C, bind his heirs and successors in perpetuity, in respect of the continued participation of his State in the Union ? Do the States possess the right, for example, exercisable by Assam and N. W. F. P., which can get out of Group B or C after a period of ten years, even after they agree to participate in them ? We have no legal or other precedents to establish the juridical content of these posers with respect to the States, which are likely to participate in the Indian Union, or in Pakistan.

We have known instances where, in the British Dominions, the right to secession sought to be exercised by component units of a Federal Government had threatened to bring about a collapse of the polity of the Dominion concerned. The polity of the Indian Union must be organic and all-inclusive. The Union can wait for the coming in of all the States, but cannot afford to allow any State which enters, to get out of it, for the simple reason that secession, or threat of secession, would become a tremendous bargaining power in the hands of the rulers, who must be presumed to be ready to fight to the last ditch for the preservation of their powers and perquisites, since, as we have said earlier, the *mahout* of the Political Department will not be there to ride over them.

In other words, without a specific provision in the Instrument of Accession, which each ruler is expected to execute before his State is permitted entry into the Union, specifically binds his State to the Union *in perpetuity*, it is just as well that the State is not admitted to participation in the Union. This is the point which has got to be put beyond any shadow of doubt by the Negotiating Committee of the Constituent Assembly in its discussions with its opposite number from Princely India. In fact, every Indian Ruler must be notified in advance that admission means continued adhesion to the Union on behalf of his State in perpetuity.

The nuisance value of Princely India had long since been recognised in this country, and the only guarantee that the States, which are admitted, on terms, to an Indian polity, would not imperil the future security of the country is that the people of Indian States must be vested with the attributes of sovereignty. Such a process is under way, and to bar the emergence of a revolution inside of each State (and of this there are numerous indications today) it behoves Indian Princes to recognise the writing on the wall, and to trim their sails to the requirements of the popular will of their subjects.

CHAPTER II

JURISDICTION OF THE CENTRE

“The Federal Government will be the main point of contact between the Provinces and the Indian States which accede to the Federation. It will be the connecting link between all the constituent units as such ; and there must exist at the Centre a residuary and ultimate responsibility for the peace and tranquility of the whole of India.”

—Report of Joint Committee on Indian Constitutional Reform, Vol. I, Part 1, Paragraph 163.

LEGAL BASIS OF UNIONISATION—UNION BURDENS — CEDED TERRITORIES — CONTRIBUTIONS AND IMMUNITIES—COINAGE AND CURRENCY—POSTAL UNITY—MISCELLANEOUS CLAIMS — PRINCIPLES OF UNION FINANCE—FINANCIAL POSITION OF SELECTED STATES.

The Cabinet Mission Declaration, which laid down the basic structure of an Indian Union or Unions, and the enormous controversy which ensued during the past twelve months over its implications, is now of a purely academic character to the students of India's constitutional and fiscal history. Since, however, the British Plan of June 3, 1947, makes the Cabinet Mission Declaration the basis on which the States are to enter the Indian Union or Pakistan, it is clear that an examination must be made of the Declaration with reference to the jurisdiction of the Union Centre.

Speaking in the House of Lords on February 25, 1947, the Earl of Munster said: “What is the Centre in India? The Centre is the axis upon which the whole body-politic of India resolves. It is the sole authority for any number of vitally important subjects. Communications, including railways, foreign affairs and defence, financial matters (including Customs and Income-tax)—all these are the responsibilities of the Centre, and in the Cabinet Mission's plan of last May a scheme was devised, whereby the Centre would be responsible for much the same authority as it has today, and with power to raise the necessary finances.” Since the Earl of Munster spoke early this year, informed opinion in India has veered round to the view that we must have a Union Centre which is strong and self-supporting, and unionisation, even for purposes of Pakistan,

need not be there, if the co-ordinating government is to depend upon doles from the constituent Provincial and States units.

In paragraph 15 (1) and (4), the Cabinet Mission visualised the formation of a Union of India embracing both Provinces and States, dealing with foreign affairs, defence and communications, with necessary powers for the raising of the finances required for the administration of these subjects. It also laid down that the States, which enter the Union, will retain all the subjects and powers other than those conceded to the Union. In Section 101 of the Constitution Act of 1935, the Federal Legislature was precluded from making laws for a Federated State "otherwise than in accordance with the Instrument of Accession of that State and any limitations contained therein."

From the viewpoint of precedents, States entering the Union surrender only such of the powers and prerogatives which are specifically mentioned as surrendered in the Instrument of Accession binding them to the Union. Section 128 of the Constitution Act has some very interesting provisions in this regard. It was laid down that "the executive authority of every Federated State shall be so exercised as not to impede or prejudice the exercise of the executive authority of the Federation, so far as it is exercisable in the State by virtue of the law of the Federal Legislature which applies therein." It was further laid down that if it appeared to the Governor-General (who for our present purposes must be substituted by the Union Government) that the Ruler of any Federated State "has in any way failed to fulfil his obligations" under this provision, he may in his discretion, after considering such of the representations made to him by the Ruler in extenuation of his (the Ruler's) actions, issue such directions as are deemed necessary in the circumstances. There is also a provision regarding the reference of a dispute between a Federating State and the Federation (the Union Centre today), as to whether the executive authority of the Federation is exercisable in a State by the Federal Court in the exercise of its original jurisdiction.

Section 125 of the Constitution Act envisaged an agreement between the States which contract in and the Federation, and gave the Governor-General powers of inspection to ensure

that the administration of the law to which the agreement related is carried out in accordance with the policy of the Federal Government. Under this Section, again, it was stated that "all courts shall take judicial notice of any agreement made." The Instrument of Accession must necessarily be annotated in terms of these legislative provisions of the Constitution Act, which are valid precedents, and without which it is unthinkable that a Union Centre can come into existence, or function in an effective manner.

Section 124 (3) of the Constitution Act is very helpful, for it extends all Acts of the Federal Legislature to States which had agreed to come in, and imposes duties upon these States or officers and authorities thereof designated for the purpose by the Rulers of the States concerned.

Under Section 108 (1) (f) of the Constitution Act, it was laid down that the Federal Legislature shall not contemplate legislation which "subjects persons not resident in British India to greater taxation than persons resident in British India, or subjects companies not wholly controlled and managed in British India to greater taxation than companies wholly controlled and managed therein." The intention of the Parliament behind this provision was obviously to secure a favoured position for British nationals and commerce in India, but the wording of this provision is so general as to become automatically applicable to the States. In fact, the existing practice also confirms this view. The Central Legislature today, operating under the 1919 Act, has no jurisdiction over the States. At any rate, the Union Centre must be governed by the principle that legislation, especially in the fiscal sphere, cannot be such as will impose inequitable burdens upon the subjects of the States or companies incorporated in the States, the assumption being that subjects of the States, and the companies incorporated therein do, for the time being, business in both the States' territory and the Provinces.

LEGAL BASIS OF UNIONISATION

The legal basis of the Federal Constitution envisaged by the Joint Parliamentary Committee was set out as follows: "It is clear that, in any new Constitution in which autonomous

Provinces are to be fully united under the Crown, not only can the Provinces no longer derive their powers and authority from devolution by the Central Government, but the Central Government cannot continue to be an agent of the Secretary of State. Both must derive their powers and authority from a direct grant by the Crown. We apprehend, therefore, that the legal basis of a reconstituted Government of India must be, first the resumption into the hands of the Crown of all rights, authority and jurisdiction in and over the territories of British India, whether they are at present vested in the Secretary of State, the Governor-General, or in the Provincial Governments and Administrations; and second, their redistribution in such a manner as the Act may prescribe between the Central Government on the one hand and the Provinces on the other. A Federation of which the British Indian Provinces are the constituent units will thereby be brought into existence.”* Clearly, this interpretation of the legal basis of Federation is untenable today. The Constituent Assemblies of the Indian Union and of Pakistan are sovereign in character, and there is no longer any need for cession by the Crown of sovereignty to the Provinces. It is only in the case of the States, which wish to participate in the Indian Union or Pakistan, that they must legally and factually divest themselves in regard to a categorised list of items, of portions of sovereignty which becomes vested in them on the passing of Paramountcy, as we have seen in the preceding Chapter.

UNION BURDENS

Whether the States come into the Indian Union or not—and this holds good for Pakistan also—the change-over from the existing political relationship of India with Britain transfers burdens to the Union which had long since been regarded as “Imperial Burdens”. Under this category, services were rendered to the States, for which the tax-payer in the Indian Provinces has till now paid ungrudgingly. These burdens will have to be shouldered by the Union Centre as long as the States stay out of the Union, and recovery of monies is only possible

**Report of the Joint Committee on Indian Constitutional Reform (Session 1933-34), Volume I, Part I, paragraph 153.*

on the entry of the States, on terms which will be their own, and not those of the people of the Union from the Provinces.

The Sub-Committee which was appointed to investigate certain facts relating to the economic and financial relations between the Provinces and the States (Nind Committee) classified, in 1930, a list of heads of expenditure incurred by the Government of India, and to which, apparently, the States did not make any contribution, and from which the States obviously received benefits of considerable value (pages 30-68 of the Report). These burdens vary from revenue collection charges relating to customs etc., to Pilgrim Departments at Indian Ports and at Jeddah and other ports in Arabia. The following is a summary of these heads:

High Commissioner for India.

Agent of the Government of India in South Africa.

Port quarantine measures.

Central agricultural and veterinary research.

Central medical research.

Lady Hardinge Medical College and Hospital.

College of Forest Institute at Dehra Dun.

Agency service to Malay and Ceylon.

Meteorology.

Railway Board.

Net loss incurred on strategic Railways.

Army, marine and military work.

Standing Committee of the Chamber of Princes and the Chamber.

Chiefs' Colleges.

League of Nations.

Costs of representation abroad and in India.

Pilgrim Departments at Bombay, Karachi, Calcutta and in Jeddah and Iraq, and the Vice-Consulate at Jeddah.

Aden.

Foreign and Political Department Secretariat.

North-West Frontier Province, including Baluchistan, and Political Agencies in Tribal Areas.

British Agency in Kabul.

Maintenance of Afghan refugees in India.

Military Adviser staff of Indian States Forces.

Civil Works.

Political Agencies in Indian States.

Watch and Ward expenditure on the North-East Frontier, including Expenditure in connection with backward tracts.

Expenditure in England and exchange.

Revenue collection charges.

Some of the items of expenditure, as listed above, whose aggregate annual cost was estimated by the Nind Committee at Rs. 65½ crores, are today out of the picture, e.g., Aden. There are other items of expenditure incurred by the Government of India which have become really gigantic in character, compared to those listed by the Nind Committee of 1930. One has to go through the entire gamut of activities of the External Affairs and Commonwealth Relations Department of the Government of India, to estimate the importance of the Services rendered to the States, and the expenditure incurred in this behalf from out of the general revenues of the tax-payer in the Provinces.

What happens to such of the States which elect to stand out of the Union Centre under any or all of the above heads, and their variations, today? It is clear that expenditure on heads of activities, which the Nind Committee have so laboriously analysed, will have to continue in one form or another, and will be shouldered by the revenues of the Union Centre. Obviously, the Union Centre cannot sell information on meteorological conditions on a metered basis to any or all the States interested in civil aviation. Obviously, again, the Union Government will refuse to shoulder burdens on *Haj* for its Muslim nationals especially in the knowledge that, for the sake of making possible Mr. Jinnah's theocratic States to the east and west, the country has been cut up, at enormous loss to the Indian Union.

During war-time there is the well-known practice that if countries A and B are neutral, and C and D are belligerents, A and B, for courtesy's sake and on payment of expenditure incurred, look after the interests of C in D and of D in C, in order that "civilised life" might be carried on even during the emergency. We cannot bring ourselves to believe that, if some

of the land-locked States, and even for that matter, maritime States, remain out of the Union Centre, the Government of the Union would "hold the baby" for them, in regard to the heterogeneous mass of items of expenditure listed by the Nind Committee, and in particular in the sphere of international relations. Trade treaties, extradition, Indians overseas, the U. N. O. and a host of other subjects are there, which have got to be looked after in common and are paid for in common. It will be a sight for the gods alone to see Bhopal strutting across the international sphere in all the panoply of the Ruler's newly acquired sovereignty! It will also be a fantastic proposition that the Union Government should negotiate with the congeries of States for contributions towards services discharged in common for the country as a whole, and especially for allocating expenditure on an agreed basis, between itself on the one part and States which elect to stay out of the Union on the other, for the discharge of the services involved. This is yet another illustration of the imperative need for integration than division, for common effort than separation, of the interests and activities of Provinces and States today.

CEDED TERRITORIES

The question arises as to what would happen to the territories ceded by some of the States to the Paramount Power in the historical period, once sovereignty becomes revested with the States concerned. The Davidson Committee distinguished between the voluntary surrender of sovereignty over certain tracts by States on the one part, and the formal transfer of territories by States to the Paramount Power on the other. The Davidson Committee also distinguished between a cession of sovereignty and a cession of jurisdiction. For example, the territories ceded by the Nizam of Hyderabad is an illustration of the vital importance of the abolition of Paramount Power which is now proposed, in so far as its implications to the Centre are concerned. Territories were ceded to the Paramount Power by the States in the historical period, in order that the former gave protection and ensured immunity to the latter, both from external aggression and, possibly, internal revolt.

What would happen if there is either an inter-statal war between two States, or internal commotion in any single State, once Paramountcy is abolished? In either case, the political security and even the economic system of the Union Centre, or of Pakistan, would become imperilled, for today there cannot be any localisation of trouble arising out of a violation of people's liberties, and there is a growing consciousness everywhere of the essential unity of the peoples of the States and the Provinces. We recall the classical illustration of the revolt of the Meos some ten years ago in the Alwar State, when the Political Department persuaded the Government of India to place troops at the disposal of the Ruler of Alwar for the suppression of the revolt. As we write, a similar recrudescence of trouble from the Bharatpur Meos in the Gurgaon District has brought us face to face with the proposition that under no circumstances can a State be allowed to remain in isolation, on the specious plea that such isolation is justifiable because the Ruler becomes sovereign the moment the Paramount Power ceases to exist.

We are not here attempting to lay down the methods for the re-regulation of relations *inter se* of the States on the one part, and of the States and the Union Centre on the other. It is rather difficult to estimate at the moment what exactly would be the extent of financial adjustments arising out of the recommendations of the Davidson Committee, which dealt with this question exhaustively in 1932. After arguing the *pros* and *cons* involved in the commutation of cash contributions and tributes paid till then by some of the representative States to the Paramount Power, the Davidson Committee arrived at the following set of recommendations (paragraph 163) :—

(In Lakhs of Rupces)

State	Estimated value in treaty of cession.	Present Central Revenue (Gross)	Provincial		Annual compensatory credits recommended.
			Present Revenue.	Expenditure.	
Hyderabad	71.81	63.52	183.4	173.32	Nil.
Baroda	22.98	47.91	56.11	68.91	22.98
Gwalior	10.03	30.26	51.55	58.21	11.78
Sangli	1.10	.40	2.76	2.57	1.10

The Davidson Committee recommended that in respect of the ceded territories of the four States, *viz.*, Baroda, Gwalior, Indore and Sangli, an annual credit of an aggregate amount of some Rs. 40 lakhs should be allowed in respect of ceded territories, as compensation to the States concerned. In the case of the Nizam of Hyderabad, the value of territories which were ceded by his predecessors was estimated at Rs. 23 lakhs a year, the Davidson Committee recommended that no such credit should be allowed to that State, since the Nizam had then asked that the military guarantee (obviously of protection against external aggression and internal commotion), for which the territories were ceded, should continue in existence. At page 60 of the Davidson Committee Report, the following very eloquent paragraph occurs: "We recommend that the annual credits which we have proposed should become effective in the adjustments with the States in question *pari passu* with the reduction of contributions to be paid by the Provinces to Federal revenues."

Taking the case of the Nizam of Hyderabad as the *cause celebre* among the numerous cases which are certain to crop up in this field, the moment the Paramount Power vanishes into thin air, we have to pose the question: What would be the fate of the Union Centre, or of Pakistan, if the States (1) demand retrocession of the ceded territories, on the plea that sovereignty is indivisible and that they must get back what they gave to the Paramount Power in bygone years; (2) demand cash credits recommended by the Davidson Committee Report from the Union Centre, or from Pakistan, and reject intervention on the part of either of the independent polities in the future; and (3) demand retrocession, and still ask for protection?

The third proposition is not really as fantastic as it looks on the face of it. This is exactly the proposition of the Nizam of Hyderabad today. He wants his corridors to the east and to the west, in addition to a rendition of complete sovereignty over Berar. It is true that these and other questions involved in a few of the ceded territories and the financial adjustments, as recommended by the Davidson Committee, can only be disposed of in the individual Instruments of Accession of the rulers concerned. In other words, the initiative and sanctions for a

future *regime* enveloping these questions definitely pass into the hands of the Rulers, and the Negotiating Committee of the Constituent Assembly or Assemblies will be powerless. This is where, we repeat again, the Paramount Power have done the greatest possible injustice to the people of India, by promising to quit India and creating, in the same breath, numerous Ulsters, which will destroy the very concept of a common polity and governance for the country as a whole.

**Tributes paid by the Indian States to the Government of India
(1930)**

	Rs.
Mysore	24,50,000
Baroda	3,75,000
Central India States (Bhopal—Rs. 1,61,290)	5,45,000
Gwalior	33,000
Rajputana States (Jaipur Rs. 4,00,000 ; Kotah Rs. 2,34,000)	11,27,000
Cochin	2,00,000
Travancore	7,96,000
Western India States (Bhavanagar Rs. 1,28,000)	7,68,000
Bombay States	1,46,000
Punjab States (Mandi Rs. 1,00,000)	1,33,000
Cooch Behar	68,000
Benares	2,19,000
Bihar & Orissa States	96,000
Central Provinces States	2,41,000
Manipur	5,000
Grand Total ..	72,00,000

CONTRIBUTIONS AND IMMUNITIES

The abolition of Paramountcy brings the country, at any rate as far as States are concerned, face to face with a category of miscellaneous financial problems, which has got to be taken in hand and disposed of before the Union Centre and Pakistan are formed on the basis of adhesion of the States. A comprehensive financial settlement must be arrived at as between the Union Centre on the one part and the Provinces and the States on the other. The legatees of the East India Company had, in the historical period, taken recourse to a series of expedients, both in the realms of polity and finance, which has led the vast majority of the States into obligations and reliefs, which sometimes cut across each other, and which sometimes leave the States, at any rate some of them, high and

dry, making them pay for real and imaginary protection given to them by the Paramount Power. Once Paramountcy ceases, and sovereignty becomes vested with the Princes, these cash contributions and immunities of States become automatically inoperative. In other words, the States will be under no obligation to make any supplication to any outside authority. On the other hand, the States, if they elect to remain outside the Union Centre, would, in theory at least, become completely independent of outside interference.

This, however, does not mean that there would not be the need for a readjustment of financial arrangements which had been in force during the *regime* of the Paramount Power, which it is now proposed to be abolished. The Union Centre must necessarily perform the functions of the Paramount Power, whether the States like it or not, and whether the States elect to come into or stay out of the Union. We have the classical illustration of the Butler Committee which proved that on the average figures of the inter-war period, States were accustomed to derive an aggregate of Rs. 4½ crores a year on import and export duties only. It will become a fantastic proposition that, if all the States, or the majority of them, elect to stay out of the Union, they have to be allowed to continue a *regime* of export and import duties (which in terms of the parlance known to the Provinces are the equivalent of octroi or transit duties). In other words, the polity and economy of India cannot be allowed to be cut up by the States which, under the Cabinet Declaration, become vested technically with powers of sovereignty.

On the same token, the contributions so far made to the Crown by the States and the immunities received, not necessarily in exchange for contributions made in the case of every individual State among the 582 on the political map of India today, must also cease eventually, as much as the assurance must be there that the Union Centre will take over—admittedly on the basis of voluntary adhesion by the States to the Union—the powers of the Crown in all their various ramifications and manifestations.

It is here that we should examine in some detail the various types of contributions made by the States to the Crown,

for they have got to be commuted once States become unionised. According to the Davidson Committee (paragraph 42), there are seven categories of contributions made which have got to be distinguished one from the other. There are contributions made by States in acknowledgment of suzerainty of the Paramount Power, very commonly imposed by treaties embodying an obligation to aid or protect on the one side, and to give subordinate co-ordination on the other. Secondly, there are contributions and commutation of obligations for the provision of States' "Contingent Force" or other form of military assistance. Thirdly, there are contributions for the maintenance of a British "Subsidiary Force" on the soil of States' territories. Fourthly, contributions are fixed on the creation or restoration of a State, or on a re-grant or increase of territory, to a State. Fifthly, there are contributions for special or local purposes, such as the maintenance of local corps, police, etc. Sixthly, there are contributions acquired by conquest or lapse of the original recipient State. And, finally, there are contributions acquired by treaty.

The following rather elaborate list of these various types of contributions has been prepared by us on the basis of the welter of figures given in the Schedules to Appendix III of the Davidson Committee Report:

Contributions imposed or negotiated by British Government, in acknowledgment of suzerainty, including obligations to aid and protect on the one side, and to give subordinate co-operation on the other, are as follows :

	Rs.		Rs.
Bundi	40,000	Kotah	1,31,250
Jaipur	4,00,000	Cochin	1,00,000
Sirohi	6,881	Mysore	24,50,000
Udaipur	2,00,000	Porbundar	15,000

Contributions imposed or negotiated by British Government in commutation of obligations for the provision of a State "contingent force" or other form of military assistance :

	Rs.		Rs.
Bhopal	1,61,290	Jaora	1,37,127
Indore	Nil	Dewas Senior and Junior	28,475

Contributions imposed or negotiated by British Government for maintenance of a British "Subsidiary Force."

	Rs.	
Cochin	1,00,000	
Travancore	3,81,456	(Treaty of 1795)
do.	4,01,655	(Treaty of 1895)

Contributions imposed or negotiated by British Government fixed on the creation or restoration of a state, or on a re-grant or increase of territory (including annual payments for grants of land on perpetual tenure and for equalisation of the value of exchanged territory):

Rs.			Rs.		
Jhalawar	30,000	Bilaspur	8,000		
Lawa	225	Bashahr	3,945		
Ajaigarh	7,014	Jubbah	2,520		
Bihat	1,400	Kumharsain	2,000		
Charkhari	8,584	Nalagarh	5,000		
Panna	9,955	Beghal	3,600		
Indore	5,285	Balsan	1,080		
Cutch	82,253	Bhajji	1,440		
Bhavnagar	52,000	Bija	124		
Manipur	5,000	Dhami	720		
Cooch Behar	67,701	Kuthar	1,000		
Benares	2,49,387	Kunihar	180		
Kapurthala	Nil	Mailog	1,440		
Chamba	2,307	Mangal	72		
Mandi	1,00,000	Tarooh	288		
Suket	11,000				

Contributions imposed or negotiated by British Government for special or local purposes, such as the maintenance of local corps, police, etc.

Rs.			Rs.		
Jodhpur	1,15,000	Jhabua	1,271		
Kotah	2,00,000	Barwani	3,390		
Tonk	5,000	Ali Rajpur	1,271		
Udaipur	Nil	Kolhapur	96,000		
Indore	Nil			(for Infantry)	48,000
Dhar	6,602			(for Residency)	8,75,000
		Baroda			

Contributions imposed or negotiated by British Government by conquest or lapse of the original recipient:

Rs.			Rs.		
Travancore	13,519	Vankaner	17,422		
Shahpura	10,000	Limbdii	44,128		
Paldeo	117	do.	43		
do.	125	Rajkot	18,991		
Sangli	24,575	Wadhwan	25,922		
Bhor	4,687	do.	87		
Jath	11,247	Jasdan	7,694		
Phaltan	9,600	Virpur	3,418		
Mudhol	2,672	Kotda Sangani	10,189		
Ramdurg	3,089	Jetpur	50,262		
Cambay	21,924	Kotharia	948		
Bansda	153	Gavridad	1,011		
Dharampur	9,000	Pal	1,253		
Malpur	430	Lodhika	1,287		
Ranasan	3	Bantwa	29,642		
Junagadh	28,394	Lakhtar	6,763		
Nawanagar	50,312	do.	124		
Bhavnagar	153	Sayla	15,001		
Porbandar	21,202	Chuda	6,324		
Dharangadhra	40,671	do.	143		
Morvi	9,263	Muli	7,501		
Gondal	49,096	Bajana	7,880		

JURISDICTION OF THE CENTRE

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	Rs.		Rs.
Bajana	58	Rai Sankli	556
Patdi	3,219	Jhunjhunwada	11,073
do.	2,682	Dudhraj	1,102
Vanod	1,953	Jhampodad	138
Rajpur	2,412	Talsana	913
Anandpur	715	Munjpur	603
Vana	3,715	Bhadvana	998
Tavi	313	Kessaria	278
Gadhka	643	Devalia	467
Mehgani	3,412	Bhathan	641
Vasavad	766	Jhamar	464
Shahpur	464	Bhalala	474
Bhadwa	1,394	Palali	357
Rajpura	2,932	Kherali	678
Kotda Pitha	4,850	Vadod	1,252
Khirasra	2,366	Gundiala	1,408
Amreli	1,621	Laliad	362
Vadali	246	Bhoika	1,759
Vivra	149	do.	99
Sisang Chandi	720	Khambhavl	730
Kankasiali	84	Gedi	1,200
Mahuva	120	Kantharia	1,491
Kanpur Ishvaria	230	do.	89
Bhaldoi	204	Darod	366
Dhrafa	3,706	Jakhan	242
Satudad	1,466	Kamalpur	776
Kurundwad	9,619	Sahuka	519
Jamkhandi	20,841	Bhalgamda	1,400
Miraj Senior	12,558	Karol	703
Miraj Junior	6,412	Vanala	396
Akalkot	14,592	Untdi	498
Amrapur	511	Ankevalia	1,300
Mulila Deri	1,279	Khandia	806
Chotila	652	do.	13
do.	25	Samla	959
Mevasa	445	Chanchana	318
Bhimora	307	Chalala	971
Chobari	154	do.	73
Sanosra	186	Karmad	140
Bamanbore	76	do.	59
Ramparda	75	Dasada	12,968
Bhadli	1,101	do.	74
Kariana	850	Paliad	907
Khambhala	406	Matra Timba	290
Itaria-Chadala	252	Bharejda	94
Akadia	129	do.	32
Nilvala	511	Sudamada-Dhandhalpur	2,381
Kamadhia	377	Sejakpur	316

Fixed Contributions

	Rs.		Rs.
Athgarh	2,800	Mayurbhunj	1,068
Athmallik	480	Narsingpur	1,456
Baramba	1,398	Nayagarh	5,525
Baud	800	Nilgiri	3,900
Daspalla	661	Pal Lahra	267
Dhenkanal	5,099	Ranpur	1,401
Hindol	551	Talcher	1,040
Keonjhar	1,710	Tigiria	882
Khandpara	4,212		

Fluctuating Contributions

	Rs.		Rs.
Bastar	18,000	Chhuikhadan	12,000
Kalabandi	16,000	Kawardha	30,000
Khairagarh	80,000	Nandgaon	80,000
Bonai	2,700	Changbhakar	150
Gangpur	10,000	Jashpur	2,000
Korea	750	Surguja	3,500
Udaipur	1,200	Bamra	7,500
Sarangarh	4,500	Patna	13,500
Raigarh	5,500	Rairakhol	2,000
Sakti	1,500	Sonpur	12,000

Contributions originally paid to another state, but subsequently acquired by the British Government by assignments from the original recipient.

	Rs.		Rs.
Balasinor	9,706	Bhavnagar	75,657
Kotah	94,252	Jodhpur	98,000
Kotah	9,252	Bundi	80,000
Ratlam	42,000	Sailana	21,000
Kheibipur	11,134	Amjhera	34,019
Lunawada	9,230	Sant	5,385
Partabgarh	Nil	Indore	660
Banswara	17,500	Dungarpur	17,500
Ali Rajpur	Nil		

It will be extremely difficult to keep track of remissions and suspensions of contributions from the States as listed above, since the Davidson Committee reported on this question. The broad position today is that payments made by States in excess of five per cent of their gross revenue have been remitted to the extent of the excess, under the powers conferred by Section 146 of the Constitution Act, and that payments made by States which were attached to larger States in 1943 have been altogether remitted. We, however, are in a position to build up a list of such remissions and suspensions with respect to a few States, and this illustrative table is appended below. It is clear that a fresh enquiry must be held by the Union Centre, in conjunction with the States, to determine the extent of these contributions, *minus* suspensions and remissions, in order to establish a list of credits and debits which must precede the complete reorganisation of claims and counter-claims as between Provinces and States participating in the Union.*

*Since the above was written, it is understood that the Political Department, before it was superseded by the Indian States Department under Sardar Patel, completed the revision of these lists of contributions etc., bringing the information up-to-date, and that it is more than likely that they will be made available to the public.

State	Contributions according to Davidson Report	Amount remitted or suspended since Davidson Report	State	Contributions according to Davidson Report	Amount remitted or suspended since Davidson Report
Jaora ...	1,37,127	76,200	Kotda-Sangani ...	10,189	2,680
Sailana ...	21,000	6,000	Limbdi ...	44,171	13,600
Mysore ...	24,50,000	5,13,500	Mengani ...	3,412	1,280
Manali ...	1,00,000	44,200	Nilvala ...	511	250
Kotah ...	4,34,720	2,05,800	Rajpura ...	2,922	1,560
Bundi ...	1,20,000	49,600	Satudad ...	1,466	520
Tonk ...	5,000	5,000	Sayla ...	15,001	7,000
Partabgarh ...	36,500	8,850	Manipur ...	5,000	5,000
Udaipur ...	2,00,000	66,000	Chhuikhadan ...	12,000	6,300
Jodhpur ...	2,13,000	1,15,000	Kawardha ...	30,000	16,500
Sirohi ...	6,881	6,881	Khatragarh ...	80,000	53,363
Bhadwa ...	1,394	460	Benares ...	2,49,387	1,23,000
Jhunjhunwada ...	11,073	4,940	Nandgaon ...	80,000	53,363

The Davidson Committee recommended that fluctuating tributes should be stabilised at their present levels, and that the conditions attached to certain other tributes already remitted should be removed or relaxed. The Committee further recommended that the securities representing the amounts paid for capitalised tributes should be returned *pari passu* with the remission of annual payments. The Committee also recommended that the remaining payments should disappear, at least *pari passu* with the income-tax contributions from the Provinces, but that a moiety should be extinguished at the latest within ten years from Federation, and the whole within twenty years. Finally, the Committee recommended that immediate relief should be given to the States by the remission of the amount of any contribution which is in excess of five per cent of the total revenues of the State which pays it.*

The Committee estimated that the immediate relief recommended by them would amount to Rs. 12 lakhs a year, and that the net amount, excluding this sum of Rs. 12 lakhs, but including contributions in respect of local corps which will rank for remission, will not exceed Rs. 63 lakhs a year. The Com-

*On this question, the Joint Parliamentary Committee wrote (Vol. I, paragraph 263): "We do not think it necessary to review the intricate adjustments discussed [by the Butler Committee] and it is sufficient to say that we endorse the main principles on which the Report is based, and in particular the gradual abolition over a period of years (corresponding to the period during which it is proposed to defer the full assent to the Provinces of a share of the taxes on income) of any contribution paid by a State to the Crown, which is in excess of the value of immunities which it enjoys."

mittee also estimated that, if the savings resulting from disbandment of the local corps are set off against the remissions, the total net cost to Government will be Rs. 69 lakhs a year. We will take the question of Defence and police force of the States and their cost in a later Chapter, but we estimate that the total net cost to the Federal Government from these proposals would, if all the Indian States come into the Union, be not merely Rs. 69 lakhs a year, on the present prices. It must necessarily be more than double or even treble this amount today.

It is clear that the finances of the Union cannot be saddled with charges arising out of the abolition of Paramountcy and the re-vesting of sovereignty with the States before they come into the Union Centre. The vast majority of the States must perish if they elect to remain in isolation as sovereign territories. There would be a thousand and one ways in which the economies and finances of individual States become integrated with those of Provinces. It is presumed by us that the vast majority of the smaller States would become administratively merged into larger units for purposes of coming into the Union, and it is not our purpose to investigate the manner in which such merger *inter se* of smaller States should be wrought, for such an investigation is obviously completely outside the scope of our enquiry. Assuming that the vast majority of States, whether it be the Central India States, the Kathiawar States, the Eastern States Agency States, the Sinla Hill States, etc., merge into larger units for purposes of adhesion to the Union (even though the arrangement is that each individual Prince shall execute an Instrument of Accession for his own State!), the presumption would continue to exist that numerous financial adjustments would have to be made *inter se* of the Union Centre and the incoming States.

It would be clearly unthinkable that the States should pay monies, as analysed above, in recognition of the suzerainty of the Union Centre. But it is equally clear that they have to contribute to the Union fisc on a basis which is equitable, easily ascertainable and equally easily enforceable. Where there is no income-tax, land customs, etc., in the States, it is obvious that a block contribution must be determined from out of the reve-

nues of the States concerned for payment to the Union Centre, before the State in question is allowed adhesion to the Union. This contribution has got to be arrived at by an expert mixed committee, composed of representatives of the Union Centre and the State in question, and its recommendations must become enforceable before the State in question can be permitted to participate in the *regime* of the Union Centre. We hesitate to lay down the lines of approach for the financial participation of the States, but it is clear to us that a system of contributions must continue to exist, though not necessarily in terms of the *regime* of the East India Company, which has been the basis of the contributions so far levied and collected by the Crown from the States as listed above.

COINAGE AND CURRENCY

The currency and coinage rights of the States, in so far as they are presumed to exist as a particle of sovereignty, when once sovereignty becomes re-vested with the rulers, are bound to create a considerable amount of difficulty to the fortunes of the Union Centre, as of Pakistan. Right through the historical period, princes and potentates, small and big, always maintained their right to issue coins, if only for ceremonial purposes. To a greater or lesser extent, some of the States today possess coinage rights of varying degrees of significance, from the State of Pudukottah minting a copper coin of the value of 1/20th of an anna, to the Nizam who has his own gold coins (the *ashrafi*) and currency notes of the value of Rs. 100/-.

We have attempted to analyse, to the best of our information, the currency and coinage rights in existence in some of the major States of the country, and we tabulate below the results obtained.

The States fall into several categories for the purposes of our examination of the limitations which may reasonably be conceded in connection with Unionization :

1. States like Mysore, Benares, etc., which definitely surrendered all currency rights.

2. States like Baroda, Bikaner, etc., which are bound by agreements for a period of years to refrain from minting State currency.

3. States like Orchha, Jaipur, Udaipur, etc., which are under no treaty obligations not to mint currency, and which in fact, until recent years, did mint silver rupees, etc. In recent years, the minting of silver rupees has been stopped voluntarily, and the British Indian rupee circulates side by side with the old State coins.

4. Travancore has not given up any rights, but has actively exercised its rights only in respect of coins of the value of half-rupee and less. It has notified the impending issue of State rupees years ago, but has not issued them so far. (Travancore has voluntarily made the British Indian rupee legal tender in the State).

5. States in which British Indian currency freely circulates, the State currency being dead or only in very partial circulation, even though the Rulers have not definitely abandoned their rights. This is the case of a very large number of States.

6. Hyderabad which exercises full currency rights.

7. States which exercise the right actively only in respect of copper coin, the rest of the rights having been either surrendered or voluntarily allowed to remain in abeyance.

GWALIOR

Mints *paisas* (copper coins), and gold *butkis* intended only for ceremonial purposes.

No silver coinage.

BARODA

Used to mint and circulate silver and copper coins, but resigned this right in 1900, on condition that the State should have the right to reopen it after 50 years with the consent of the Government of India, and that copper coins should be retained. (But even copper coins have ceased to be struck).

No silver coinage; but copper coinage in the form of pice and pies (now extinct).

CAMBAY

Closed the mint for 50 years in 1901, on the same conditions as Baroda.

CUTCH

Exercised her coinage rights.

Under silver coinage are to be found:

- (1) Five *koree* piece (*Panchia*)
- (2) Two and a half (*Adhia*) *Koree* piece.
- (3) *Koree* (*Koree*)
- (4) One half *Koree* (*Adadhium*).

Under copper coinage we find:

- (1) *Trambio* coin
- (2) *Dokdo* coin
- (3) One and half *Dokdo* coin (*Dhinglo*)
- (4) Three *Dokdo* (*Dhabu*).

TRAVANCORE

Mints silver and copper coins, which are issued and circulated:

Silver coinage:

- (1) Half rupee = 7.86 annas.
- (2) Quarter rupee = 3.93 annas.
- (3) *Fanam* = 2.25 annas.

Copper coinage:

- (1) *Chuckram* = 6.74 pies, but values at 6 pies.
- (2) Half *chuckram* = 3.37 pies.
- (3) Quarter *chuckram* = 1.685 pies.
- (4) *Cash* = 0.42 pice.

Travancore has maintained its own currency from very remote times, and the existing State Mint was established as early as 1789-90.

All these seven coins are declared legal tender within the State, each of the silver coins to the extent of rupees two and each of the copper coins to the extent of rupee one.

INDORE

Does not exercise coinage rights. In 1902 the State agreed to close the mint for silver coins for the next 50 years, and thereafter not to coin silver without the consent of the Government of India, and the British Indian rupee was adopted as legal tender. As regards copper coinage, the right does not seem to have been exercised after 1902.

Only under copper coinage, there is *hali*.

ORCHHA

Exercises the right. The *darbar* has converted a large proportion of its currency into British Indian rupees, and they are widely used in the State.

Under silver coinage are:

- (1) *Gajashahi* coin. (At present, however, this rupee circulates locally at a depreciated value).

Copper coins (only locally).

ALWAR

Does not exercise any right. But some of the silver rupees struck in the time of Maharaja Mangal Singh are still in circulation, and are also legal tender, being equivalent to the British Indian rupee.

HYDERABAD

Gold coins:

- | | | |
|---------------------------------------|---|-------------------|
| (1) The <i>ashrafi</i> (Rs. 29) | } | Not legal tender. |
| (2) Half <i>ashrafi</i> (Rs. 15) | | |
| (3) Quarter <i>ashrafi</i> (Rs. 8) | | |
| (4) One-eighth <i>ashrafi</i> (Rs. 5) | | |

Silver coins:

- | | | |
|------------------------------|---|---------------|
| (1) The <i>Osmania</i> Rupee | } | Legal tender. |
| (2) Half rupee | | |
| (3) Quarter rupee | } | Token coins |
| (4) One-eighth rupee | | |

Nickel coins:

- (1) One anna coin.

Copper coins:

- (1) Half anna
- (2) Two pies
- (3) One pie

Paper currency:

- | | | |
|-------------------------|---|---------------|
| (1) One-rupee notes | } | Legal tender. |
| (2) Five-rupee notes | | |
| (3) Ten-rupee notes | | |
| (4) Hundred-rupee notes | | |

The Hyderabad Government Mint was founded in 1855-56, and the method of hand manufacture of coins

continued up till 1892-93. The demand later became so great that production had to be continued by machinery.

DUNGARPUR

Does not exercise any right. Dungarpur minted only a few gold coins in 1917 for ceremonial and charitable purposes.

Copper coins minted before 1904 are still in circulation to some extent among the Bhils of the State.

BUNDI

Exercises the right.

Under silver coinage:

- (1) The *Kattarshahi* or half rupee.
- (2) Half rupee.
- (3) Quarter rupee.

Under copper coinage, pice only.

JAIPUR

Exercises the right. Mints gold mohars (*Akheyshahi mohar*) coined on demand by individuals who require it for ceremonial and ornamental purposes.

Under silver coinage—*Akheyshahi* rupee.

Under copper coinage—2 pice and 1 pice coins.

JODHPUR

Exercises the right. Only Gold *mohars*, half *mohars* and one-fourth *mohars*, which are not legal tender and minted on demand for ceremonial presentation or ornaments.

Under copper coinage: Only pice, but even this is falling out of circulation.

UDAIPUR

Exercises the right.

Under silver coinage: Udaipur or Chitoori rupee, 8 anna, 4 anna and 2 anna pieces.

Under copper coinage: *Dhingla*.

BIKANER

Does not exercise the right. The State agreed to close the mint for 30 years in 1893 under an agreement, and no fresh agreement has been entered into.

The Butler and Davidson Committees, which investigated this question, have laid down two important principles which must be examined here. The Butler Committee wrote (paragraph 94): "We are strongly of the opinion that the multiplication of different currencies in India is hostile to the best interests of the States and the country as a whole." They also wrote: "The advantages of the Imperial currency are so obvious that we do not consider that there is a substantial claim to any relief, but some allowance might be made on this question in any financial settlement that may be made with individual States or groups of States."

There are two passages in the Report of the Davidson Committee which are of value to us, particularly in view of the fact that a retrocession of sovereignty to the States is bound to create a new situation, in which the "Royal Mint" of a prince or princeling in India might become a new menace to be reckoned with by the Union and by the constituent units of the Union, leave alone such of the States which elect to contract out of the Union. The Davidson Committee wrote (paragraph 409): "It is sufficient here to remark that the revival of the mints which have been closed in the past, or the minting of coins by States which have hitherto exercised the right, would be even more inconsistent with Federation, than any system of dividing among federating units the profits accruing from control of Federal currency." They further wrote (paragraph 412): "We suggest that in any case where the reopening of mints or the continued issue of metallic currency may be considered inimical to the interests of the Federal currency, efforts should be made to arrange, by negotiation, that such operation should be confined within purely nominal limits, or to the production of coins intended for ceremonial as opposed to currency purposes."

These, again, are principles which are unexceptionable, and have got to be fitted into any discussion of currency and coinage rights of the States as they exist today, or they might rear their heads in future *vis-a-vis* the fiscal and currency policies of the Union, or of Pakistan.

At the time when the Davidson Committee enquired into this question (1931), it was estimated that the Nizam alone

had notes in circulation of the value of Rs. 9 crores, and that on the basis of population or of active note circulation, the loss to Federal revenues from the circulation of the coins and currency of the Nizam was approximately Rs. 70 lakhs a year. We regret we have no information relating to the present-day volume of the coins and currency of the Nizam in circulation, but the estimates of the Davidson Committee are illustrative of the importance to the Union Centre of reservation, within the meaning of the recommendations of the Butler Committee, of the right to coinage and currency on an overall basis.

Apart from the losses to Union revenues involved in the exercise by the States of currency and coinage rights on an extensive basis, there is the cognate question of the supposed claim of the States to a share in the profit made by the Government of India under the head "coinage and currency", which the Federal Finance Committee of the Round Table Conference estimated in 1931 to be Rs. 380 lakhs a year. The Davidson Committee were unwilling to recommend that the States have a right to share in the profits accruing to the then prospective Federation, which is the equivalent of our Indian Union, from this Head, and wrote (paragraph 408): "Nevertheless, whatever the profits, we are unable to recommend the acceptance of any scheme for the distribution among prospective Federating Units, in as much as 'coinage and currency' is a prospective Federal subject, and any profit thereon should accrue to the Federal Government, in the direction of whose currency policy the States should have the opportunity of exercising their due share of influence."

We have known, in the past, instances where the States, when prices of silver fell, urged the Government of India, of their own volition, to demonitize the coins which they minted in their own individual territories, and the Butler Committee drew pointed attention to the case of at least one Indian State which profited through manipulation of its own currency to such an extent that trade was brought to a standstill. The days are long since gone past when the greater the variety in coinage and currency in circulation in different territories, the greater is the picturesqueness of the patterns of India! In fact, we hold strongly to the view that one of the points for

negotiation by the Negotiating Committee of the Constituent Assembly of the Union should be the question that the States should surrender outright the right to coinage and currency, if only for the reason that this year silver has been more or less demonitized, and that it was decades ago that gold coins of the Government of India were, so to speak, in effective circulation. Day by day the country is marching forward to a system of currency and coinage which is token in character, and there would not be any opportunity for any of the States to melt coins for purposes of obtaining profits out of such a transaction, or to debase its currency system in a manner which puts in jeopardy the economy of the Union.

Obviously, the Nizam would constitute a headache to the Union Centre, now that he had elected to become sovereign, by virtue of the extensive character of currency rights exercised by him so far. We, however, feel that the Union Centre has, in the event of the Nizam being forced by political and economic circumstances coming into the Union in the future, to negotiate a financial settlement through a fixed contribution to him under this head. It is just as well that the rights exercised by him are taken over by the Union Centre, in order that one single currency and coinage system is to pervade the length and breadth of the country. If, however, the Nizam elects to stay permanently out of the Union, it is clear that the most stringent possible type of currency regulations must come into force through a cordon round his territories, so that black-market transactions as between the *Hali-Biji* currencies are prevented. If the Nizam stands out of the Union, his currency and coinage will become foreign currency and coinage, and the Government of the Union Centre will have to enforce its own rights of exchange, so that profiteering is prevented on the trade passing from the territories of the Union into the territories of the Nizam and *vice versa*. Such, again, will be the case of other States which declare their independence.

It appears to us a trifle ridiculous on the part of any of the States, e.g. Travancore, that they should claim today sovereign attributes of currency and coinage, because they elect for the time being to stay out of the Union Centre, when even

mittees recommended the abolition of these rights, and rejected the claim of the States to a share in the profits accruing to the Government of India under this head. We have argued this point at some considerable length, in order to give an additional illustration of the manner in which, while the States become under the British proposals completely sovereign, the Union Centre, or even Pakistan, would be kept widowed of power in essential questions of this character. Forty-eight federating units pay homage today to one single dollar bill of Uncle Sam, and we know that the erstwhile autonomous Mexican and Red Indian territories honour this bill in the U.S.A. today. The days for a multiplicity of effigies on coinage and currency inside a single country are definitely gone, if only for the reason that it is ruled out by the inexorable necessity for national parity for world currencies, and that the fiscal and currency policy of the country in question as a whole demands the abolition of these so-called attributes of medieval sovereignty which some of the States, in the first flush of their freedom away from Britain, might choose to demand. Otherwise, there would be chaos in the economic and fiscal spheres, with the Nizams, the Bhopals and the Travancores and a host of other States cutting across the integral unity of the country, from which only disaster would ensue.*

POSTAL UNITY

The postal and telegraph unity of India has been one of the arrangements which the East India Company and, later on, the British Crown had been very zealous to secure, for it had always been maintained that the efficiency and security of postal and telegraph services, as much as railway communications, are matters of Imperial concern. In other words, the preservation of control over communications has always been considered by the British Government to be a question of stra-

* With uncanny precision, if precision it can be, Sir C. P. Ramaswami Iyer continues to get into trouble, by seeking to define the position of his "independent" Travancore. In a statement from Trivandrum on July 18, 1947, he said: "The State will be perfectly prepared to harmonise its import regulations with the rest of India. It will also be ready to enter into an agreement with the rest of India on the rates of export duties to be levied. However, the States will continue to levy import duties and retain customs. Travancore will also retain her right to issue her own currency".

tegic or military security, with the result that, despite obvious and numerous mistakes committed, there is in existence today something like an overall unity of the postal and telegraph systems, enveloping both the Provinces and the States.

The services of the Indian post office are enjoyed by States in common with the Provinces, though fifteen States have their own Postal Departments and are outside the postal union of the country as a whole. Of these fifteen States, five States have conventions with the Indian Post Office and work in co-operation with it. As for the balance of the remaining ten States, the greater part of the correspondence between the States is carried by the local post office, while the branches of the Indian Post Office exist at most of the important places and carry correspondence across the States' frontiers. In most of the Convention States, the Indian Post Office exists only on territories which are British in jurisdiction, such as the Residency areas, railway stations, etc. The State postage stamps of the five Convention States are valid for correspondence to any part of India, but not to overseas, while the stamps of the remaining ten States are not valid anywhere outside their respective boundaries.

According to the Davidson Committee, (paragraph 386), there are five questions on which the States and the Government of India have so far been unable to reach agreement on the issues involved:

(1) There is a belief in the States that the Indian Posts and Telegraphs Department is a revenue-yielding department, and that the Government of India make a profit out of its administration. The deficits of the Department of Posts and Telegraphs during the five years 1929-30 to 1933-34 were respectively as follows: Rs. 62 lakhs; Rs. 133 lakhs; Rs. 94 lakhs; Rs. 41 lakhs; and Rs. 52 lakhs. All the sections of the Department *viz.*, the post office, telegraphs, telephones and the radio, showed deficits in all these years, except that the telephones showed small surpluses of Rs. 2 lakhs and Rs. 3 lakhs in the years 1932-33 and 1933-34 respectively. It will be seen that the impression of the States, when the Davidson Committee reported, was not valid, and that, as such, there could be no "claim" on their part for a share in the surplus profits of the Govern-

ment of India from the administration of this Department, which did not exist at all. The Davidson Committee wrote (paragraph 388) that, since they were bound to approach this question from the federal standpoint, they were "unable to regard with sympathy any claim for a share in the alleged profits of the Posts and Telegraphs Department."

• Since the Davidson Committee reported, the financial position of the Posts and Telegraphs Department was altogether different. The successive deficits of the earlier years were converted into more or less successive magnificent surpluses, what with the lifting of the Great Depression and increases in the rates charged by the Department for services rendered. The position is illustrated by the following figures: 1934-35, Rs. 38 lakhs; 1935-36, Rs. 47,000; 1936-37, Rs. 15 lakhs; 1937-38, Rs. 57 lakhs; 1938-39, Rs. 19 lakhs; 1939-40, Rs. 90 lakhs; 1940-41, Rs. 125 lakhs; 1941-42, Rs. 341 lakhs; 1942-43, Rs. 452 lakhs; 1943-44, Rs. 903 lakhs; 1944-45, Rs. 1,025 lakhs; 1945-46, Rs. 1,131 lakhs; 1946-47 (revised estimates), Rs. 478 lakhs; and 1947-48 (budget estimates) Rs. 422 lakhs.

The war-time activities of the Government of India were responsible for this "surplus bulge" in the accounts of the Department, which after all, are only paper entries. The thing to be noticed, however, is in relation to the precipitate decline in the surpluses during the past two years, and detailed examination has shown us that in the budget estimates for the current financial year there is provision for a deficit of Rs. 11 lakhs against the post office. We consider that division of India into the Indian Union and Pakistan would mean further losses of revenue to the Government, and there cannot be any question that the people would tolerate the continuance of the high rates and surcharges for services rendered by this Department, which cannot be run on any basis other than that of a public utility. We are, however, convinced that this question lends itself for examination *de novo*, from which the States can obtain satisfaction.

Finances of the Postal Department.
(In Thousands of Rupees)

	1929-30	30-31	31-32	32-33	33-34	34-35	35-36	36-37	37-38	38-39
Post Office	-21,47	-62,09	-51,37	-6,07	-11,08	24,33	21,99	27,34	47,78	35,28
Telegraphs	-35,21	-61,27	-37,65	-33,47	-38,96	-7,88	-33,36	-29,93	-16,39	-37,77
Telephones	1,09	-1,95	-6,00	2,28	2,73	23,67	14,98	19,79	28,10	21,05
Radio	-6,85	-8,18	1,18	-4,62	-4,02	-2,18	-3,14	-2,66	-2,24	42
Total	-62,44	-1,33,49	-93,84	-41,88	-51,93	37,94	47	14,54	57,25	18,98
	1939-40	40-41	41-42	42-43	43-44	44-45	45-46	46-47 Revised	47-48 Budget	
Post Office	53,68	43,53	1,41,13	2,92,53	4,02,93	4,34,20	4,83,79	21,03	-11,14	
Telegraphs	-2	37,45	1,10,43	83,24	2,28,88	3,45,10	3,57,83	2,44,42	2,03,92	
Telephones	35,46	42,29	88,02	76,95	2,68,95	2,51,16	2,93,78	2,21,27	2,35,26	
Radio	48	1,53	1,05	-1,03	1,81	-5,81	-4,63	-9,07	-6,40	
Total	89,60	1,24,80	3,40,63	4,51,69	9,02,57	10,24,65	11,30,77	4,77,65	4,21,64	

(2) The States protest that under the existing departmental regulations they were required to give a cash guarantee in respect of remunerative post offices opened for their administrative convenience, and argue that no such demand should be enforced without first giving them allowance for all admittedly unremunerative offices within their territories.

(3) The States object to the Indian Posts and Telegraphs Department carrying on banking operations through the postal savings banks, and to the issue of cash certificates. The substance of the complaint is that these cash operations are competitive with those of similar institutions, other than postal institutions, run in or by the States. The Posts and Telegraphs Department, according to the Davidson Committee Report (paragraph 391), admitted that "it would be a new and unjustifiable principle of political practice to hold that the Paramount Power is entitled to carry on these transactions in States against the wishes of the Rulers, and, in some cases, in competition with the Durbar's own local arrangements. We are prepared, therefore, to arrange for their complete cessation in the territories of any State, which definitely asks for it." Thus, this dispute was put beyond the pale of controversy.

(4) There is wide resentment against the operation of mail robbery rules, under which the States can be required by the Government of India to make good any losses which are sustained by the Indian Posts and Telegraphs Department from robbery of mails in transit through States' territories. The Davidson Committee accepted the recommendations of the Butler Committee, which asked for an improvement in the police and security administrations of States, in order that reasonable safety of life and property and protection of routes over which mails are carried are ensured. The Davidson Committee held (paragraph 393) that the States were not entitled under this head to any financial compensation.

(5) Many States which are in receipt of grant of free service stamps complain that these are inadequate to their needs, while others who do not enjoy this privilege demand the grant thereof. The Butler Committee (paragraph 101) wrote that "service stamps are given in certain cases on no apparent principles." It is clear that these claims of the States to free

service stamps are based upon an anachronism which had better be dispensed with, both in the interests of all the States *inter se*, as well as of the Indian Posts and Telegraphs Department. It is also clear that there cannot be any continuance of the grant of free service stamps for the States, enjoyed today by 27 States, at a cost, estimated by the Davidson Committee, of over Rs. 4 lakhs a year, once the Indian Union, or even Pakistan comes into existence. The Davidson Committee held that "no method has been discovered whereby the profit or loss for providing postal facilities in any particular area can be assessed" (paragraph 398), and that if the accounting system used by the Indian Posts and Telegraphs Department were applied by those States which possess postal systems, the effect, in all probability, will be the conversion into deficits of the surpluses or the so-called revenue resources of these States under this head.

We cannot exaggerate the dictum of the Davidson Committee (paragraph 396) that there is "a widespread tendency towards cessation of postal unity" among the States today. It is true that States like Hyderabad, which have an extensive postal system and considerable revenue from the operation of the Postal Department, will, as pointed out by us, create a problem of considerable difficulty for the Indian Union. It is also true that the *anchal* system of Travancore and Cochin, which has been in existence from almost times immemorial, belongs to the category of residual problems in between the Union Centre and the States. It is equally true that the States consider the right to issue postal stamps, if not the running of a Postal Department, an essential attribute of their sovereignty, which under the British "Quit India" proposals will be re-vested with them. In all certainty, there will be considerable difficulty in the path of the Negotiating Committees of the States and of the Constituent Assembly in respect of a settlement of this problem. But it is clear that every obstacle to the creation of a new *regime* of postal unity for the Union Centre must be demolished, whatever the cost involved in the process.

The Union Centre must secure the abolition of this right of the States subject to two provisos. In the first place, the States which come into the Union must be permitted to obtain,

through payment on a commercial basis, their required quota of postal stamps, and for this no financial "contribution" need be made to the Union Finances. In other words, the States must be assured of adequate supplies of stamps for the use of people resident within their internal jurisdiction, and they must give the assurance that they would not profiteer on the sale of the stamps. We consider that this arrangement would not cause any loss to the Federal budget. A tremendous expansion of postal facilities has taken place in India during the past thirty years, involving great additional outlay on the services of this Department. The participation of all the States in a common postal *regime* would not, to our mind, add appreciably to this total cost of expanded services. Even if it does cost more, it is clear that the cost must be borne willingly by the Union finances. For, after all, the Postal Department is a public utility and, if properly managed, is bound to be run on a commercial basis. The costs of participation of, say, an additional five or ten per cent of the total population of India, represented by the people of the States which enjoy the postal privileges today, cannot be considered tragic under any circumstances, the only consideration being that the States which come into the Union must be presumed to be willing to surrender this attribute of their sovereignty.

The second consideration is that the States which are in the enjoyment of postal rights may be continued in them, so far as ceremonial purposes are concerned. We know occasions in the world where commemorative postal stamps are issued to celebrate the centenary of a State or of an institution. We do not see any reason why the *darbars* of States should be deprived of the opportunity of issuing ceremonial postal stamps, e.g., on the ascension of a Ruler to the *gadi*, or the birth of an heir-apparent. We are persuaded that the exercise of this "right" can be made possible by the Postal Department of the Union Centre, which can print and supply the same to the State concerned, on the payment of a commercial rate for the labour and expense involved. Beyond this, States participating in the Union Centre cannot have any other rights.

MISCELLANEOUS CLAIMS

There is a host of other claims on the part of the States which has got to be remembered in any delimitation of the relations between them on the one part and the Provinces on the other, for the purposes of the Union Centre. This includes claims in respect of railway lands owned by the Government of India in the States, and the question of jurisdiction thereon; claims arising out of civil stations and cantonments in the States; claims regarding *kadim inams*; and claims in regard to other miscellaneous cash contributions and immunities.

All these questions are bound to crop up when the Ruler of a State executes his Instrument of Accession relating to participation in the Union Centre. These claims can be reasonably settled on the basis of a mutual give and take policy, after a close scrutiny of financial implications involved therein. We cannot over-emphasise the point here that the prevailing time spirit in the country must be remembered in any examination of these claims and counter-claims, and the principle must be established beyond all shadow of doubt that simply because the Ruler of a State had, in the ages gone by, enjoyed a certain right, he has got to be permitted to enjoy it today, even though such a right becomes obnoxious in terms of modern social conscience, e.g., *begar*.

PRINCIPLES OF UNION FINANCE

Two broad principles of public finance emerge from the series of constitutional discussions which took place in this country during the past thirty years, and these should be disposed of before we can embark with any purposiveness upon our study of Union Finances. The Montagu-Chelmsford Report (paragraphs 205-6) advocated the redistribution of the financial resources of the Centre and the Provinces as then existed, including Burma, and arrived at the principle that, in view of greater resources being placed at the disposal of the Provinces, it was the duty of the Provinces to meet the incoming deficits of the Centre. Lord Meston and his colleagues, in their famous Award (paragraph 8), declared that, at any rate as far as ensuring the financial stability of the Centre was concerned, "doles and temporary assistance would be inconsistent

with the whole policy.”* The Butler Committee further wrote (paragraph 106): “While impressed with the need for great caution in dealing with a body so heterogeneous as the Indian Princes, so conservative, so sensitive, so tenacious of internal sovereignty, we find that our imagination is powerfully affected by the progress already achieved and by the possibilities of the future. To that future we can merely open a window.”

In fact, the basic principle of the Meston Award was that since, on the basis of the then prevailing financial estimates, a gross revenue of Rs. 18½ crores was being placed at the disposal of the Provinces, the impending deficits of the Centre, which in 1920-21 was calculated at about Rs. 10 crores a year, should be met from out of the proceeds of increased revenues which became a windfall for the Provinces. In fact, out of a gross total of Rs. 18½ crores of additional revenues made available to the Provinces, as much as Rs. 9.83 crores was detached as provincial contributions to the Centre, thus leaving only Rs. 8.67 crores as increased spending power for the Provinces. The Meston Award was based upon the principle of a flat rate of 60 per cent of these additional resources made available to the Provinces accruing to the Centre over a period of years, even though such a process had involved great injustice to Provinces like Madras, the U.P. and the Punjab which, in particular, had made contributions to the finances of the Centre far out of proportion to that made individually by the

* Paragraph 15 of the Meston Report runs as follows :

“The central government in the course of a political reconstruction gives to each of the local governments some, and to some local governments a very considerable, increase of spending power. Finding itself in a deficit as the result of this reconstruction, it withholds from each province a certain proportion of the increased resources which it is intended that that province should eventually obtain. The central government does not come in as raiding the hard-won surplus of a province; nor ought the central government to be represented, if our proposal be accepted, as the pensioner of the provinces. It can hardly be contended that a province, which has, at all events, decidedly improved its finances as a result of the change, has valid ground of complaint, if it does not obtain immediately the full increment which it may subsequently realise. In the cases of the provinces that gain most, it would hardly be possible for any such province to spend in the first year the whole of its suddenly increased resources; and if it were possible, it would be financially undesirable. We think therefore that this basis affords less scope for controversy and may be accepted as both more logical and more equitable than the plan of the Montagu-Chelmsford report.”

other Provinces. The following table indicates the implications of the Meston Award in this regard :

(In Lakhs of Rupees)

Provinces.	Increased spending power under new distribution of revenue.	Contributions as recommended by the Committee.	Increased spending power left, after contributions are paid.
Madras	5,76	3,48	2,28
Bombay	93	56	37
Bengal	1,04	63	41
United Provinces ..	3,97	2,40	1,57
Punjab	2,89	1,75	1,14
Burma	2,46	64	1,82
Bihar and Orissa ..	51	Nil	51
Central Provinces ..	52	22	30
Assam	42	15	27
Total ..	18,50	9,83	8,67

We are in complete agreement with the principle enunciated in the Meston Award, for to our mind the need for a strong Union Centre, at any rate in the financial sphere, is perhaps a greater necessity today than it was at any time in the chequered history of India, if only for the reason that a heterogeneous mass of States is expected to come into it. The Meston Committee wrote: "After the most careful scrutiny of their various peculiarities, we see no marked necessity for differential treatment *inter se*. In Madras and the United Provinces the windfall is so vast that it could not be employed profitably for several years. On the other hand, their revenues do not promise any remarkable elasticity, economy has been strictly practised, and considerable arrears of administrative progress are now due. In the Punjab also the windfall is large and balances are full, while here the revenues move upwards with marked ease. The position is less simple, for diverse reasons, in Bombay and Bengal. The former has attained a scale of expenditure far above the Indian average, and the pace of expansion of its revenues is distinctly higher than in any other Province. We believe that it could, without inconvenience, forego the greater part of its new resources

at the outset, and help the less fortunate provinces from its own abundant balances. But we hesitate to differentiate it prejudicially from the other richer provinces. Bengal, on the other hand, has a low scale of expenditure and an inelastic revenue; and it will receive only a very moderate start in its new financial career. But its size, intrinsic wealth and general economic possibilities prevented us from treating it more favourably than the other provinces in this category."

The principle enunciated by the Meston Committee, on a survey of the financial position prevailing in 1920-21, which is of exceptional importance to us in our enquiry, is that the economic and administrative set-up, at any rate of the Provinces, is one single compact whole, and that it is inevitably indivisible in character. When the Davidson Committee reported in 1932, there was then the prospect of the States coming into Federation under the Constitution Act, and a similar principle was laid down for the participation of States in a common all-India polity. The Davidson Committee wrote (paragraph 448): "It is not irrelevant to observe that the States who enter Federation will be called upon to share with the provincial units in the cost of subsidising the deficit provinces, which will stand in very much the same relation to the Federal Government as those States which enjoy immunities and make no corresponding contributions in return." We will revert later to an examination of these immunities, and the need for off-setting them against contributions from the Centre on an agreed basis, between the resources of the Provinces on the one part and those of the States participating in the Union Centre on the other.

It is, however, necessary for our purposes here to examine the radical departure from the principles laid down in the Meston Award and by the Davidson Committee, which are involved in the Niemeyer Award of 1936, with respect to financial readjustments between autonomous Provinces to be and the Federal Centre. The emphasis had by then shifted from the financial equilibrium of the Centre to the financial equilibrium of the Provinces. Sir Otto Niemeyer posed the question (paragraph 9): "The present position of the Provinces and their contrasted positions *inter se*, both of which fall under the

objective of starting the Provinces, on the occasion of Autonomy on 'an even keel' . . . How far, in actual fact is each province now solvent and is likely to remain solvent—a matter which cannot be judged on one year only?" Sir Otto Niemeyer then dealt with the comparative efficiencies of administration in the various Provinces, the levels of taxation prevailing in them, and the firmness with which public finances were managed by provincial administrations, and arrived at the conclusion that central grants-in-aid, in addition to a division of the pool of residual income-tax, should be there in order that the financial stability of the Provinces was ensured. We will take up this question again in some detail in the next chapter dealing with taxes on income, and our purpose here is only to contrast the broad tendencies in public finance which have invaded India during the past thirty years.

Our conclusion is that if the States are to participate in the Union Centre, they can only participate on the basis of a stable and equitable financial system both for the Centre and the participating units, which obviously include Provinces as well as States. If the States do not accept this viewpoint, it is just as well as that they do not come into, or are not allowed to come into, the Union Centre. In other words, the States must be prepared to throw their resources into the common pool of the finances of the Union Centre in the same manner in which Provinces bind themselves to participate, and no other claim is possible. For the purposes of the Union Centre, as much as for the individual purposes of the component parts of the Union, there cannot be two sets of standards in the financial sphere.

It was, as pointed out earlier, estimated by the Butler Committee that the export and import duties levied by the Indian States for purposes of financing their administrative activities in 1928-29, were of the order of Rs. 4½ crores of rupees a year. Present estimates must definitely treble, if not quadruple, the yield from this considerable source of revenue for the States. The Butler Committee further argued that when the Provinces adopted discriminating protection, revenue from maritime customs rose from Rs. 5 to Rs. 50 crores a year in 1921-22, and that the States were not at all consulted.

Actually, the imposition of a protective tariff by the Indian Legislature in the inter-war period meant a double customs duty on States. Similar, again, is the case with disputed and disputable points relating to income-taxes, corporation taxes, excise, the railway system, coinage and currency, etc., etc., which have got to be settled in advance of the formation of the Union Centre.

It is against this general canvas that our thesis of Union Finances is built up, viz., that the States, which declare their willingness to participate in the Union, must come in on the basis of throwing their resources into the common pool in all matters relating to finance, at any rate as far as the Union finances are concerned. Considerations of sovereignty of Rulers cannot be allowed to stand in the way of the fulfilment of this dictum. Even without participating in a governance for the country as a whole, they have willingly, or otherwise, surrendered considerable moieties of their rights and powers into a common pool which had become necessary for the country as a whole, at the behest of the Paramount Power. The obvious examples are the series of arrangements between the Provinces and States as regards the Postal Department and the Railway communications, and the surrender of powers in relation to excises and participation in a common pool through division of resources (*e.g.*, matches, *vanaspati*, etc.)

With nation-wide plans of economic and reconstruction development, involving thousands of crores of rupees of expenditure, leave alone the imperative and inescapable necessity for the creation of a strong financial Centre for the Union, there is no other option to the Princes who are prepared to execute Instruments of Accession on behalf of their States for participation in the Union. By the very nature of the political map of India today, the States are landlocked, at any rate the overwhelming majority of them. They cannot hope to survive in isolated economic and political existence like Luxemburg or Switzerland. No sensible person in India talks of coercion of the States into participation in the Union Centre, but the prospect ahead is clear, viz., that smug isolation cannot secure the preservation of the dynasties of the Rulers concerned, a point on which even Pandit Jawaharlal Nehru gave an assur-

ance to the Negotiating Committee of the Princes on behalf of the Constituent Assembly. Either the States participate in the Union Centre on a par with the Provinces on questions involving finance, communications, defence and foreign policy, or they do not. The acceptance of this principle is vital to the subject-matter of our inquiry.

The Percy Committee (otherwise known as the Federal Finance Committee of the Round Table Conference), in its report published in 1932, laid down (paragraph 92): "We have found, as a matter of fact, that the Federal Government will not have at its command, at the outset of Federation, large reserves wherewith to satisfy claims, whether of the Provinces or of the States, which the Government of India have hitherto found themselves unable to meet. This fact has a bearing on the problem of equalizing burdens as between all units of the Federation. The principle of equality is accepted by all sections of opinion. It is not our function to interpret that principle. We can only report that, on the facts as we have found them, the Provinces will have for some time to contribute in one form or another, a considerable sum of their income-tax receipts towards the finances of the Federal Government." The Davidson Committee (paragraph 439) laid down the same principle in the following manner: "In an ideal Federal system there would no doubt be complete uniformity, if not equalisation, of burdens and of benefits, and Federal Constitutions seek to give effect, so far as possible, to this principle. But the circumstances in which an Indian Federation has to be created are, in the true sense of the word, unique, and present features which no framers of any Federal Constitution have hitherto had to take into account."

What is the meaning of this principle of equality as between the Provinces and the States which are members of the Union? How can this principle be applied to the heterogeneous mass of items of revenue and expenditure, particularly those relating to the States, for which there are hardly any yardsticks of measurement? What will be the basis on which the resources of the States are to be yoked to the needs of the Union Centre? What, again, will be the basis on which such of the States which surrender valuable items of revenue to the

Union Centre, in order that there is not only uniformity but administrative cohesion in financial matters, will recoup their losses? Finally, in case of non-observance of voluntary undertakings by a State, even in terms of the Instrument of Accession executed by its Ruler, what will be the consequences? We can project this line of reasoning almost without limit, but for our present purposes, however, an examination must be made of the principles which must subsist behind the participation in the Union Centre of Provinces and States which are unequal in their size and resources.

Provinces and States are not capable of comparison, even assuming for our purposes that the smaller States will eventually merge into sizeable groups or affiliate with bigger States, as the States' Merger Scheme sought to do in 1943. The following two tables show the manner in which Provinces and some of the major Indian States compare with each other, in respect of territories and population.

Area and Population of Provinces

Name.	Area in square miles.	Population	Name.	Area in square miles.	Population.
Bombay ...	76,443	2,08,50,000	C. P. ...	98,575	1,68,14,000
Madras ...	1,26,166	4,93,42,000	Sind ...	48,136	45,35,000
Bengal ...	71,442	6,03,07,000	Assam ...	54,951	1,02,05,000
Punjab ...	99,089	2,84,19,000	Orissa ...	32,198	87,29,000
U. P. ...	1,06,247	5,50,21,000	N. W. F. P.	14,263	30,38,000
Bihar ...	69,745	3,63,40,000			

Area and Population of Selected States

Name.	Area in square miles.	Population.	Name.	Area in square miles	Population.
Kashmir ...	82,258	40,22,000	Baroda ...	14,243	34,55,000
Bahawalpur ...	20,000	15,00,000	Cambay ...	392	97,000
Patiala ...	5,941	19,36,000	Nawanagar ...	3,791	5,04,000
Kapurthala ...	661	3,78,000	Bhavnagar ...	2,961	6,18,000
Gwalior ...	26,008	40,06,000	Kolhapur ...	3,229	10,92,000
Rampur ...	894	4,77,000	Bhopal ...	6,918	7,85,000
Jaipur ...	15,601	30,41,000	Rewa ...	12,803	18,20,000
Bikaner ...	23,317	12,93,000	Dholpur ...	1,173	2,87,000
Jodhpur ...	36,120	25,56,000	Hyderabad ...	82,330	1,63,39,000
Udaipur ...	1,045	1,18,000	Indore ...	9,934	15,14,000
Bharatpur ...	1,972	5,76,000	Mysore ...	29,458	73,29,000
Mayurbhanj ...	4,243	9,91,000	Travancore ...	7,661	60,70,000
Cooch Behar ...	1,318	6,40,000	Cochin ...	1,480	14,23,000

The first principle of public finance, according to modern standards, is the securing of the maximum social advantage of

the community, which unfortunately for the Union Centre, as a beginning, comprises of two complements of people with varying standards of ideas, living and comfort, as between the Provinces and the States. Additionally, the equation between public opinion and government which subsists today in the Provinces is missing in the States, with the result that there are bound to continue in our midst, for a considerable period of time, two standards of public finance in relation to the social will. There is no escape from this really inconvenient proposition. We can only hope for the resurgence of a political conscience on the part of the peoples of the States, which will be sufficient to batter down autoeracy wherever it exists, and which will make possible the emergence of conditions in the States which will become comparable to those prevailing in the Provinces in the fullness of time.

But the Union Centre cannot wait for such a consummation, before States are admitted into participation in the governance of the country. The Joint Parliamentary Committee (Vol. I, paragraph 249) have no doubt observed as follows: "It will be wiser to base the division upon the financial and economic needs of the Federation and the Units. Nor is it likely that any disequilibrium between British India and the States which result from such a method of treatment would be of a serious character." But the problems of the Union Centre are as much of the morrow as they are of today, and perhaps their immediate importance far outweighs that of any long-range consideration. How can the principle of equality of burdens, in other words, equality of sacrifice, be applied to the revenue resources of States and those of Provinces for purposes of the Union Centre? Surely, there cannot be any quantitative point in the sharing of financial burdens by the States and the Provinces. For one thing, the States are such a heterogeneous mass, with varying standards of administration and varying sources of income. The *per capita* taxation in the Provinces (1944-45 figures) varies from Rs. 2.7 in Bihar to Rs. 14.1 in Sind, and even progressive States like Mysore and Baroda cannot stand comparison with Bihar in the field of taxable capacity. In other words, we cannot apply the "rule of three" for the division either of the assets or of the revenues of the States, in

order to make them share equally with the Provinces in the burdens which have got to be imposed by the Union Centre for purposes of federal or confederal governance of the country, or of the territories involved. The principle of equality in the allocation of burdens between the Provinces and the States can only have a relationship to the incidence of those burdens on the respective units forming the Union.

The Percy Committee (paragraph 93) have brilliantly expounded this point, and we cannot improve upon it. They wrote: "It is doubtful whether a jealous comparison of relative burdens offers a sound basis for a successful partnership. Each partner in a new enterprise must bring something substantial into the common pool, and may expect to derive solid advantages from the partnership commensurate with his contribution; but, if those conditions are fulfilled, the partners will be unwise to insist on a meticulous equality. They will probably find it best to take their associates as they are. Similarly, a new Federation may find, at the commencement of its existence, that the conception of maintaining the *status quo* in non-essentials is a better guide to policy than any ambitious ideals of equality or unity." The Provinces have administrative unity, and a tax system which is more or less uniform in its incidence. Two centuries of common rule have created conditions which make their polity and economy integral to a common governance. More than everything else, the Provinces are not, as Indian States are, subject to the personal whims of autocratic Rulers, who can make and unmake decisions without the consent of the people.

All these conditions are slowly passing in the States. It is quite likely that the growing pressure of public opinion and, more than that, the impact of ideas from without, might secure, within a reasonable period, the emergence of a social conscience in the States, and the gradual diminution, to the vanishing point perhaps, of the prerogatives which Rulers enjoy today. However, the administrative and tax systems of Provinces and States vary to such an extent that we cannot possibly bring about, at any rate overnight, conditions of equality as between Provinces and States. Even an orthodox revolutionary in politics has got to reckon with this solid fact, however much ugly

it is, and however inconvenient it will be, at all events, from the viewpoint of the Union Centre.

What will be the practical utility of the imposition of a tax on income, leave alone a corporation tax, in the Simla Hill States or the Eastern States Agency? Arguing *contra*, what sources of revenue will replace the abolition of salt tax, as in the Provinces today, in such of the States which have a plentiful supply thereof? Pursuing the same strain of argument, what will replace the sources of revenue from maritime customs in Kathiawar States and Travancore, and of land customs in the case of Kashmir? Who will be responsible for the opium policy of Malwa States, unless it be that these States come into the Union Centre and willingly surrender their rights of sovereignty. In all certainty, the majority of the States, which are only specks on the map of geographical India, would demand compensation for the abolition of *begar*, because *begar* is an important element in the Public Works policy of the States concerned.

We have said enough to demonstrate the fantastic character of the problems involved in the inevitable increases in the expenditure of the incoming States on the one part, and those of the Provinces on the other, for purposes of the Union Centre. It sounds attractive to talk about the need for throwing everything into the common pool, and for taking out of the common pool on the basis of the principle, "each according to his needs". On this question the following is the weighty opinion of the Joint Parliamentary Committee (Vol. I, paragraph 249): "British India is mainly concerned with the aggregate of the States' contributions and immunities, and not with their uneven incidence as between the States *inter se*. The States, however, must enter the Federation as separate units, and a balance-sheet will, therefore, be required in the case of each individual State."

To our minds, in view of the vast divergence of the fiscal systems of the States, in comparison with that prevailing in the Provinces, the pooling and sharing thereof, for purposes of the Union Centre, cannot become feasible, until the States admit the principle of budgetary scrutiny on the part of the Union authorities. In other words, the Union Centre must be enabled to comprehend the character and extent of revenues available

to the States, before it could decide, obviously with the consent of the *durbars*, the manner in which those resources could or should be ear-marked to meet: (1) the specific requirements of the individual State concerned, and (2) the requirements of the Union Centre itself. Today the budgets of the States are, to say the least, of indifferent value to students of public finance, and do not help in a proper determination of revenue and expenditure. We have attempted to analyse the budgets of some prominent States, and summarise the results in the accompanying tables:

Revenues of Selected States.
(In thousands of rupees.)

State.	Year.	Total.	Land Revenue.	Customs.	Excise.	Income-tax.	Stamps.	Forests.	Communica-tions.	Commer-ce & Industry.	Tele-graphs.
Kashmir	1944-45	4,63,95	68,08	1,06,21	8,86	12,30	10,58	1,05,87	15,38	88,14	2,85
Bahawalpur	1944-45	1,68,33	56,02	Nil	8,82	12,15	4,84	18,45	54,00	.....	.....
Kapurthala	1944-45	35,90	9,65	.....	11,79	3,79	2,73	.....	11	.....	.....
Gwalior	1942-43	3,20,43	.....	.....	.....	.....	.....	.....	.....	.....	.....
Rampur	1943-44	84,24	34,76	.....	17,64	.....	1,66	72	37	10	89
Jaipur	1942-43	1,96,96	57,84	23,05	13,75	.....	4,32	1,56	23,36	2	1,34
Bikaner	1943-44	2,10,98	32,34	19,80	23,36	4	1,76	5	79,21	1,72	.....
Jodhpur	1937-38	1,68,85	.....	.....	.....	.....	.....	.....	.....	.....	.....
Udaipur	1945-46	4,49	84	.....	1,30	5	3	1,61	.....	.....	.....
Bharatpur	1944-45	64,98	26,08	.....	25,33	.....	1,46	90	.....	.....	.....
					(includes customs also).						
Mayurbhanj	1944-45	46,98	12,78	.....	3,30	3,45	98	13,55	.....	68	.....
Cooch Behar	1943-44	70,76	23,39	.....	3,11	2,29	3,28	41	5,06	2	.....
Baroda	1944-45	4,34,26	1,02,64	20,28	74,27	74,17	3,28	18	23,20	1,15	.....
Cambay	1943-44	12,41	3,67	3	1,93	.....	78	.....	64	.....	.....
Nawanagar	1943-44	1,10,15	47,32	19,36	.....	.....	1,49	.....	21,97	.....	1,36
Kolhapur	1943-44	1,15,08	17,76	.....	16,39	7,77	4,50	1,16	5,12	46	11
Bhavnagar	1942-43	80,23	29,70	5,81	.....	.....	1,40	40	6,15	.....	.....
Bhopal	1941-42	90,27	.....	.....	.....	.....	.....	.....	.....	.....	.....
Hyderabad	1938-39	8,92,64	2,96,43	1,11,26	1,96,11	.....	17,38	12,04	1,41,22	2,53	14,05
Indore	1943-44	2,83,27	77,46	31,99	31,60	.....	6,07	13,79	.....	76,06	.....
Mysore	1944-45	10,01,38	1,31,24	.....	1,66,17	1,73,37	26,25	64,97	.....	1,45	.....
Travancore	1944-45	6,11,25	42,66	89,04	1,45,69	1,12,76	35,51	52,16	16,76	19	1,44
Cochin	1942-43	1,70,60	12,29	27,75	48,63	31,37	6,52	12,11	15,00	18	.....

Expenditure of Selected States.
(In thousands of rupees.)

State.	Year.	Total.	Military.	Agriculture.	Public Works.	Edu- cation.	Justice	Com- merce & Indus- try.	Co- ope- ration.	Central Admi- nistration.	Com- muni- cations.	Civil List.
Kashmir	1944-45	4,22,80	89,69	2,14	18,57	34,22	5,90	24,06	1,50	26,46	35,52	22,72
Bahawalpur	1944-45	....	18,47	44	1,48	3,67	4,61	....	....	7,08	91	6,19
Kapurthala	1944-45	25,09	4,01	....	3,80	2,02	49	....	....	....	....	2,80
Gwalior	1942-43	2,22,15	....	....	....	....	....	....	....	....	....	....
Rampur	1943-44	81,73	12,51	41	2,09	4,86	1,04	1,35	2	3,06	7,39	17,19
Jaipur	1942-43	1,44,84	27,16	....	16,18	8,25	2,94	32	....	7,47	7,07	13,62
Bikaner	1943-44	1,39,66	8,59	19	13,13	6,14	8,72	62	3	9,11	32,00	21,77
Jodhpur	1937-38	1,30,36	....	....	....	....	....	....	....	....	....	....
Udaipur	1945-46	3,91	....	1	1,25	24	13	....	....	25	....	37
Bharatpur	1944-45	64,28	4,29	....	8,07	2,39	80	....	1,06	1,67	....	4,00
Mayurbhanj	1944-45	37,07	....	34	4,41	1,89	85	76	....	7,47	....	....
Cooch Behar	1943-44	49,28	3,19	22	6,15	1,97	30	1,86	....	28	2,33	4,75
Baroda	1944-45	3,73,78	27,50	10,17	32,19	42,30	5,93	1,67	77	26,67	....	23,00
Nawanagar	1943-44	1,08,19	5,02	32	2,00	3,34	67	....	....	1,52	10,36	13,17
Cambay	1943-44	10,24	56	....	89	96	21	....	....	72	....	1,00
Bhavnagar	1942-43	83,59	4,31	18	14,05	5,78	1,94	....	....	2,78	....	8,28
Kolhapur	1943-44	75,77	9,73	1,24	19,35	8,16	2,16	22	17	3,96	....	7,55
Bhopal	1941-42	84,03	....	....	....	....	....	....	....	....	....	....
Hyderabad	1938-39	8,90,59	89,24	7,55	14,65	93,95	24,67	3,92	4,67	46,95	78,86	69,54
Indore	1943-44	1,91,84	18,27	....	11,02	11,17	5,51	5,12	....	3,56	....	11,00
Mysore	1944-45	11,22,60	30,00	6,53	49,71	84,19	12,43	3,70	1,69	19,05	40,35	23,00
Travancore	1944-45	6,11,25	23,48	2,49	4,78	69,33	17,41	99	1,22	9,47	59,92	20,17
Cochin	1942-43	1,44,39	1,99	1,72	12,59	20,83	3,08	1,17	32	2,32	21,25	8,60

It will be seen that in addition to *suppressio veri*, if not *suggestio falsi*, the budgets of the States are not amenable to comparison with the usual financial statements of governments the world over. Apart from the much-vaunted fixing of the principle of privy purse, which does not find itself in evidence these days even to the extent of the supposed fixing, the resources suppressed from these budgetary statements of the States, in so far as they relate to the private fortunes of the Princes, will, on proper scrutiny, be adjudged by any impartial tribunal to bear a considerable proportion to the total resources of the States. This is the reason why we attach the greatest possible importance to the principle of budgetary scrutiny by the Union Centre of the finances of the States, especially in view of the fact that the Union Centre, both in respect of the Legislature and the Executive, *does* have representatives of the States thereon. If this principle is not accepted, there cannot, to our mind, exist a Union Centre, at all events in a financial sphere, capable of comprehending the States.

The development of the resources of the States becomes the next important point to be tackled by the Union Centre. In the last Chapter dealing with Reconstruction Finance, we will deal with the manifold aspects of this problem but, for our present purposes, it is clear that the Union Centre must have powers to tap resources wherever they exist, obviously with the consent of the States concerned. The abolition of an item of revenue, which is obnoxious in terms of modern public finance, would mean the ultimate creation of a new head of revenue, and the development generally of the resources of the States legitimately merges in the functions of the Union Centre. For, otherwise, there will be the yoking together in the financial sphere of unequal partners, and, however much we deprecate the immediate use of a common financial yard-stick for Provinces and States, it is clear that the Union Centre must not be prevented from functioning at all in the financial sphere even at the outset of the Union polity.

The incidence of taxation as between the Provinces and the States belonging to the Union must be comparable in character, though not commensurate in all respects. Just as the Government of India, in order to make provincial autonomy

workable, assumed burdens on behalf of deficit Provinces (*e.g.* Niemeyer grants-in-aid), the Union Centre, as we have repeatedly pointed out, must assume responsibilities for the financial stability of participating States, and must, more than everything else, ensure a common incidence of expenditure, so that social services available to Provinces and States become comparable in character, and make possible the creation of a commonalty, which becomes indivisible as between Provinces and States, and whose needs must prevail over those of Princes and potentates.

We unreservedly endorse the dictum of the Davidson Committee regarding the need for approximation of credits and debits arising out of the income and expenditure positions of the Provinces and the States for purposes of the Union Centre. The Davidson Committee wrote (paragraph 443): "We do not, however, intend to suggest that a State which enters Federation can continue in the enjoyment of privileges or immunities which are definitely inconsistent with the Federal ideal, and at the same time claim remission of tribute or other contributions on the ground that these are of a feudal character, or are unknown in other federations. We recommend, therefore, that, whenever it is proposed to remit a contribution of this kind, the value of any privilege or immunity from ordinary Federal burdens shall be set off against the proposed credit and no remission or payment made unless the credit exceeds the debit, and then only to the extent of the balance. In one case only we do not recommend the application of this principle, namely, that of cash contributions in excess of five per cent of the revenue of a State. The remissions which we have recommended in this case are intended to be immediate, that is to say, prior to Federation, so that no question of 'credits' and 'debits' arises in regard to them."

There is no escape from the need for a surrender of contributions which States were accustomed to pay to the Paramount Power, and while the Union Centre can presume to take up the position of the Paramount Power after Britain quits India, there is no known method which the Union Centre can adopt to bring the States to a position where these contributions become payable to the finances of the Union Centre, barring of

course the declaration of war and the consequent compulsion of recalcitrant States. In the same manner, the immunities enjoyed by the States in respect of items of taxation must also be surrendered by them. Just as the finances of the Government of India become chargeable to contributions which are intended to secure financial equilibrium and stability in some of the deficit areas among the Provinces, the finances of the Union Centre must become equally chargeable to the extent needed for ensuring financial stability in the States which are members of the Union. On the same token, the resources of the States, in so far as they are chargeable to subserve the purposes of the Union Centre, must become available to meet the requirements of Provinces. In other words, the economic and financial unity of Provinces and States, which are members of the Union, becomes the only axis on which the Union Centre can ever hope to function. If this proposition is not accepted, it is just as well that States are not permitted to share the privileges of a common Centre for the country.

CHAPTER III

TAXES ON INCOME

“ Even if the argument were completely sustainable, it would not be conclusive on the question whether or not the community as a whole in India was entitled to tap this source of revenue, as it must in fact tap other sources of revenue of unequal provenance among the different parts of India. No source of revenue, whether Customs, Excise or Income-tax, can in fact in any country be derived equally from all parts of the country alike, rich and poor, industrial and agricultural.”

—Para 22 of *Sir Otto Niemeyer's Report*, dealing with the divisibility of Jute Export Duty.

CENTRAL DEPENDENCE ON INCOME-TAX— STRUCTURE OF TAXES ON INCOME—INCOME- TAX IN SELECTED STATES—DIVISION OF RESI- DINARY INCOME-TAX—DEFICITS OF THE CEN- TRE—SUBVENTIONS AND DIVISIBLE POOL OF INCOME-TAX—EXISTING ARRANGEMENTS WITH STATES.

The Federal Legislative List (VII Schedule of the Constitution Act, 1935) enumerates the following heads of revenue for the Federation, which must serve our present purposes, as the starting point of discussion in respect of Central taxes:

<i>Item</i>	<i>Description</i>
44 ..	Duties of customs including export duties.
45 ..	Duties of excise on tobacco and other goods manufactured or produced in India, except: (a) Alcoholic liquors for human consumption; (b) Opium, Indian hemp and other narcotic drugs and narcotics; non-narcotic drugs; (c) Medicinal and toilet preparations containing alcohol or any substance included in sub-paragraph (b) of this entry.
46 ..	Corporation Tax.
47 ..	Salt [The abolition of Salt Tax in the Indian Provinces has created a new situation relative to the rights of the States to levy and collect salt tax.]
48 ..	State Lotteries.
54 ..	Taxes on income, other than agricultural income.
55 ..	Taxes on the capital value of assets, exclusive of agricultural land of individuals and companies; taxes on the capital of companies.

- 56 .. Duties in respect of succession to property other than agricultural land.
- 57 .. The rates of stamp duty in respect of bills of exchange, cheques, promissory notes, bills of lading, letters of credit, policies of insurance, proxies and receipts.
- 58 .. Terminal taxes on goods or passengers carried by railway or air; taxes on railway fares and freights.
- 59 .. Fees in respect of any of the matters in this list, but not including fees taken in any court.

The above is a very comprehensive list of the powers of taxation by the Federal Centre as envisaged in the Constitution Act. There are, however, numerous points which are likely to crop up immediately the States enter the Union Centre, not only on the basis of the reservations made by the Constitution Act, but also relative to that large sector of disputed and disputable rights *inter se* of the Union Centre, the Provinces and States, which has emerged in the discussions relating to a Federal polity for Provinces and States during the past ten years in particular.

There is, for example, the reservation of Section 139 of the Constitution Act which lays down that the Corporation Tax shall not be levied by the Federation in any Federated State until ten years have elapsed from the establishment of the Federation. We presume that some similar reservation will be made, allegedly in the interests of the States, in the Instruments of Accession which the incoming Rulers are to execute before they are admitted to participation in the Union Centre. The Constitution Act lays down that any Federal Law providing for the levying of Corporation Tax shall contain provisions enabling the Ruler of any Federated State, in which the Tax would otherwise be leviable, to elect that the tax shall not be levied in the State, but that in lieu thereof there shall be paid by the State to the revenues of the Federation a contribution, as near as may be equivalent to the net proceeds which it is estimated would result from the tax if it were levied in the State. It was further provided that, where the Ruler of a State so elects as aforesaid, the officers of the Federation shall not call for any information or returns from any Corporation in the State, but

it shall be the duty of the Ruler thereof to cause to be supplied to the Auditor-General of India such information as he may reasonably require to enable the amount of any such contribution to be determined. Under the Act, any Ruler, who is dissatisfied with the determination of the amount of contribution payable by his State to the Federation in any financial year, may appeal to the Federal Court which has the power to adjudicate the dispute, with the added provision that the decision of the Court is final.

We cannot persuade ourselves to endorse the position defined in this section of the Constitution Act with respect to the Corporation Tax, in so far as the powers and functions of the Union Centre are concerned. The Constitution Act was framed at a time when the States were able to flourish in isolation from the general economy of the country as a whole. Disparities in taxation in the Provinces and the States have led to the colossal migration of industry from the former to the latter in recent years. This is a proposition which cannot be tolerated in the future. It may be argued that a reasonable time must elapse before the fiscal systems of the States are brought into line with that of the Union and of the Provinces. But it is clear that this ten-year period of exemption, as envisaged in the Constitution Act for the imposition of the Corporation Tax in the States, cannot be admitted for purposes of the Union Centre.

Section 138 of the Constitution Act annotates item No. 54 of the Federal Legislative list of the VII Schedule with respect to taxes on income, other than agricultural income, to the extent that "a prescribed percentage of the net proceeds in any financial year of any such tax . . . shall not form part of the revenue of the Federation, but shall be assigned to the Provinces and to the Federated States, if any, within which that tax is leviable in that year, and shall be distributed among the Provinces and those States in such manner as may be prescribed." It is to be assumed that the "rules as may be prescribed by or under the Federal or Provincial laws" relating to Estate Duties, also fall under the same category. We shall presently deal with the principles of the Niemeyer Award with respect to the Provinces under this head, and at the moment we will

proceed with an examination of the applicability of this provision of the Act to the States.

In the first place, it was provided that the percentages originally prescribed under this sub-section of the Act shall not be increased by any subsequent Order-in-Council of the Crown. Secondly, the Federal Legislature, which is the equivalent of the Union Centre, was invested with power to "increase the said taxes by a surcharge for Federal purposes, with the proviso that the whole proceeds of such surcharge shall form part of the revenues of the Federation. Thirdly, it was provided that, notwithstanding anything said so far, the Federation may retain out of the monies thus assigned to Provinces and States (a) in each year of a prescribed period such sum as may be prescribed; and (b) in each year of a further prescribed period a sum less than that retained in the preceding year by an amount, being the same amount in each year, so calculated that the sum to be retained in the last year of the period will be equal to the amount of each such annual reduction. It was also provided that neither of the periods thus prescribed shall be reduced by subsequent Orders-in-Council, and that the Governor-General, in his discretion, may, in the second prescribed period, direct "that the sum to be retained by the Federation in that year shall be the sum retained in the preceding year, and that the second prescribed period shall be correspondingly extended." Provisions are there in the Act for consultations between the representatives of the Federal, Provincial and State Administrations. Finally, the Act provides that "where an Act of the Federal Legislature imposes a surcharge for Federal purposes under this Section, the Act shall provide for the payment by each Federated State, in which taxes on income are not leviable by the Federation, of a contribution to the Revenues of the Federation, assessed on such basis as may be prescribed, with a view to ensuring that the contribution shall be the equivalent, as near as may be, of the net proceeds which it is estimated will result from the surcharge, if it were leviable in that State, and the State shall become liable to pay that contribution accordingly."

Sir Otto Niemeyer, in paragraph 36 of his Report, has annotated the implications of this provision of the Constitu-

tion Act as follows: "If at any time any State comes into the Federal Income-Tax, and thus qualifies for a share in the residual tax, a minor adjustment will have to be made", with reference to his allocations from the divisible pool of income-tax to Provinces, which we will examine presently. He further stated: "But it would be desirable that such adjustment, which could no doubt be arranged in connection with the Act of Accession, should not involve an alteration in the above percentages, but should rather operate to effect the total to which the percentages apply, just as it may not operate to increase the initial amount of that total."

CENTRAL DEPENDENCE ON INCOME-TAX

We must straightaway dispose of one of the outstanding points relating to the structure of Central revenues as it has developed during the past quarter of a century. The accompanying table, which we have built up from official statistics, is extremely revealing.

Principal Heads of Central Revenue.
(In lakhs of rupees)

YEAR.	TAXES ON INCOME		CUSTOMS		EXCISE	
	Total	% of revenue	Total	% of revenue	Total	% of revenue
1920-21	22,19	16.4	31,90	23.6	20,44	15.1
1921-22	18,74	28.9	34,41	53.1	..	..
1922-23	18,00	24.9	41,35	57.2	..	..
1923-24	18,24	24.5	39,70	51.9	..	..
1924-25	16,03	21.3	45,75	60.9	..	..
1925-26	15,92	10.5	47,78	31.4	..	..
1926-27	15,72	20.6	47,38	48.9	..	..
1927-28	15,07	19.7	48,21	63.3	..	..
1928-29	16,70	21.1	49,28	62.3	..	..
1929-30	16,71	20.9	51,28	63.4	..	..
1930-31	16,00	21.5	46,81	60.4	..	..
1931-32	17,49	22.8	46,44	60.4	..	..
1932-33	17,97	21.6	51,95	64.0	..	..
1933-34	17,13	22.4	47,16	61.6	..	..
1934-35	17,55	21.7	52,67	65.1	..	..
1935-36	17,07	20.7	54,11	65.8	..	..
1936-37	15,34	16.6	53,58	66.9	..	..
1937-38	12,70	16.9	43,11	57.3	7,66	11.8
1938-39	13,74	18.4	40,51	54.4	8,66	11.6
1939-40	14,20	17.4	45,88	56.4	6,53	8.0
1940-41	17,63	22.6	37,30	48.9	9,49	12.2
1941-42	25,01	25.3	37,80	39.4	13,15	13.3
1942-43	43,46	34.6	25,12	12.0	12,79	10.1
1943-44	58,37	33.9	26,57	15.5	24,94	14.5
1944-45	81,09	31.8	39,77	15.9	38,14	14.8
1945-46	73,55	26.4	73,61	26.0	46,36	16.4
1946-47 (R.E.) ..	57,60	21.2	87,50	32.3	42,79	15.8
1947-48 (B.F.) ..	59,70	21.7	93,00	33.8	40,93	14.9

From the above analysis, it is clear that taxes on income have come to assume increasing importance to the Central revenues since 1921, at various places outstripping customs as the mainstay of the Government of India in the financial sphere. When the full weight of the excess profits tax was felt, as in the recent war years, taxes on income have become the most outstanding item of Central revenues. The decline in the overall importance of customs, which had been the main source of Central revenues in the historic period, is impressive. There is a recovery in the percentages of customs revenue to the gross Central revenues since 1945-46, because of the sudden opening of the flood gates for imports, which could not come into the

country at all, except on government account, during the war years. We consider that the broadening of equity in principles of taxation would make taxes on income more and more fundamental as the principal axis of the financial structure of the Union Centre, and the added weight of death or estate duties would further heighten this importance. *Per contra*, customs are bound to decline as the predominant source of Central revenues in the future, even though we consider that India might remain a net importing country, in terms of balances of trade, for a decade or more. Our reasoning is based on the knowledge that imports into India in the future would be mostly capital goods, while the country would bounce forward each year towards reaching the goal of self-sufficiency. Excises also are likely to oust customs as one of the principal resources of India. The sum total of this gigantic process of the fiscal revolution, which is now under way, is that the former structure of revenues, with customs, taxes on income and excises following one another, in the descending order of importance, would be replaced by a new gradation, with taxes on income at the head of percentages and customs at the bottom, the middle position being occupied by excises.*

It is on this basis that we argue the point that taxes on income constitute a subject of finance on which the Union Centre cannot have any compromise, even if such a compromise might be suggested in the interests of the States which are likely to participate in it, or in Pakistan. It is time that the States are notified that unearned increments will not be allowed to continue with their former impunity, and that the incoming socialisation of productive activity and income in this country would make it imperative on the part of the Union Government to undertake a steeper, as well as a wider system of taxes on income. There is no escape from this fundamental proposition, which becomes the pith of our argument in this Chapter. It is clear that, for the purposes of the finances of the Union Centre, the States must be brought into a Central pool more or

* We have not included in the above key table on Central taxes the yields of corporation taxes, which, if added to actual taxes on income, would completely vary the relative importance of taxes on income, customs and excises to the Government of India. This is, however, done in a later section of this Chapter.

less on a par with the Provinces. We say more or less advisedly, for the reason that economic, commercial and financial conditions in the vast majority of the States today are not comparable with those prevailing in the Provinces. And yet we cannot over-emphasise the point that whatever might be the initial time lag left, even on the showing of the Interim Report of the Union Powers Sub-Committee of the Constituent Assembly, the target must be reached and reached very soon indeed, in order that the fiscal conditions in the Provinces and the States which become members of the Union Centre must approximate to each other. During the past ten years in particular, there has been a tremendous amount of evidence accumulated to the effect that tax evasion, at any rate as far as the Government of India was concerned, has been aided by the States which screen operators from the Provinces by making it possible for them to take their monies away into the States. Additional to this, there is also the argument, which is valid in our opinion, that a good many of the States today are becoming increasingly highly industrialised, and that with this progression of industry and commerce in the States, a new financial code must come into operation within their territorial limits, which satisfies the basic canons of public finance, at the same time bringing them into line with the Provinces. These are days for big commercial and industrial combines, and the dictum laid down by Lord Goschen, a former Chancellor of the Exchequer in Britain, more than half a century ago, that income cannot be localised, is applicable today and tomorrow.

STRUCTURE OF TAXES OF INCOME

We must take notice of the disparities in the existing system of taxation in the Provinces and the States. For this, we must bring into juxtaposition the respective rates of taxes on income prevailing in these two categories of territories in the country today. The following is an extract from the Finance Act of 1947-48 of the Government of India.

RATES OF INCOME-TAX

A. In the case of every individual, Hindu undivided family, unregistered firm and other association of persons not being a case to which paragraph B of this Part applies—

	<i>Rate</i>
1. On the first Rs. 1,500 of total income	Nil.
2. On the next Rs. 3,500 of total income	One anna in the rupee.
3. On the next Rs. 5,000 of total income	Two annas in the rupee.
4. On the next Rs. 5,000 of total income	Three and a half annas in the rupee.
5. On the balance of total income.	Five annas in the rupee.

• Provided that—

(i) no income-tax shall be payable on a total income which, before deduction of the allowance, if any, for earned income, does not exceed Rs. 2,500;

(ii) the income-tax payable shall in no case exceed half the amount by which the total income (before deduction of the said allowance, if any, for earned income) exceeds Rs. 2,500;

(iii) the income-tax payable on the total income as reduced by the allowance for earned income shall not exceed either

(a) a sum bearing to half the amount by which the total income (before deduction of allowance for earned income) exceeds Rs. 2,500 the same proportion as such reduced total income bears to the unreduced total income, or

(b) the income-tax payable on the income so reduced at the rates herein specified—

whichever is less.

B. In the case of every company and local authority, and in every case in which under the provisions of the Indian Income-tax Act, 1922, income-tax is to be charged at the maximum rate—

	<i>Rate</i>
On the whole of total income.	Five annas in the rupee

RATES OF SUPER-TAX

A. In the case of every individual, Hindu undivided family, unregistered firm and other association of persons, not being a case to which any other paragraph of this Part applies:

	<i>Rate, if income wholly earned.</i>	<i>Rate, if income wholly unearned.</i>
1. On the first Rs. 25,000 of total income.	Nil.	Nil.
2. On the next Rs. 5,000 of total income.	Two annas in the rupee.	Three annas in the rupee.
3. On the next Rs. 5,000 of total income.	Two and a half annas in the rupee.	Three and a half annas in the rupee.
4. On the next Rs. 10,000 of total income.	Three annas in the rupee.	Four annas in the rupee.
5. On the next Rs. 10,000 of total income.	Four annas in the rupee.	Five annas in the rupee.
6. On the next Rs. 10,000 of total income.	Five annas in the rupee.	Six annas in the rupee.
7. On the next Rs. 10,000 of total income.	Six annas in the rupee.	Seven annas in the rupee.
8. On the next Rs. 15,000 of total income.	Seven annas in the rupee.	Eight annas in the rupee.
9. On the next Rs. 15,000 of total income.	Eight annas in the rupee.	Nine annas in the rupee.
10. On the next Rs. 15,000 of total income.	Nine annas in the rupee.	Ten annas in the rupee.
11. On the next Rs. 30,000 of total income.	Ten annas in the rupee.	Ten and a half annas in the rupee.
12. On the balance of total income.	Ten and a half annas in the rupee.	Ten and a half annas in the rupee.

B. In the case of every local authority—

Rate

On the whole of total income Two annas in the rupee

C. In the case of an association of persons being a co-operative society, other than the Sanikatta Salt-owners' Society in the Bombay Presidency, for the time being registered under the Co-operative Societies Act, 1912, or under an Act of a Provincial Legislature governing the registration of co-operative societies—

Rate

(1) On the first Rs. 25,000 of total income: Nil.

(2) On the balance of total income: Two annas in the rupee

D. In the case of every company—

Rate

On the whole of total income: Two annas in the rupee
and in addition, in respect of that part of the total income (as reduced by the amount of dividends payable at a fixed rate) which does not exceed the amount of dividends, not being dividends payable at a fixed rate, declared in British India in

respect of the whole or part of the previous year for the assessment for the year ending on the 31st day of March 1948, on the amount by which such part—

	<i>Rate</i>
(a) exceeds 30 per cent, but does not exceed 40 per cent, of the total income as so reduced.	Three annas in the rupee.
(b) exceeds 40 per cent, but does not exceed 50 per cent, of the total income as so reduced.	Five annas in the rupee.
(c) exceeds 50 per cent of the total income as so reduced.	Seven annas in the rupee.

Provided that—

(i) no additional super-tax shall be payable where such part is less than, or equal to, five per cent on the capital of the company;

(ii) where such part is more than five per cent on the capital of the company, the additional super-tax payable shall be reduced by the amount of additional super-tax which would, but for the provisions of clause (i) of this proviso, have been payable had such part been equal to five per cent on the capital of the company;

(iii) the additional super-tax shall be payable only by a company in which the public are substantially interested within the meaning of the *explanation* to sub-section (1) of section 23A of the Indian Income-tax Act, 1922, or a subsidiary company of such a company where the whole of the share capital of such subsidiary company is held by the parent company or by the nominees thereof.

Explanation.—For the purposes of this paragraph, - -

(a) the expression “capital of the company” shall be deemed to mean the paid-up share capital at the beginning of the previous year for the assessment for the year ending on the 31st day of March 1948 (other than capital entitled to a dividend at a fixed rate) *plus* any reserves, other than depreciation reserves and reserves for bad or doubtful debts, at the same date as diminished by the amount on deposit on the same date with the Central Government under section 10 of the Indian Finance Act, 1942, or section 2 of the Excess Profits Tax Ordinance, 1943;

- (b) the expression "dividend" shall be deemed to include any distribution included in that expression as defined in clause 6(A) of Section 2 of the Indian Income-tax Act, 1922, and any such distribution made during the year ending on the 31st day of March 1948 shall be deemed to have been made in respect of the whole, or part of the previous year;
- (c) where any portion of the profits and gains of a company is not included in its total income by reason of such portion being exempt from tax under any provision of the Indian Income-tax Act, 1922, the capital of the company, the total amount of dividends and the amount of dividends payable at a fixed rate shall each be deemed to be the proportion thereof that the total income of the company bears to its total profits and gains.

INCOME-TAX IN SELECTED STATES

The States today cannot, by any stretch of the imagination, be called progressive with reference to their fiscal systems. We have attempted to analyse the provisions of taxes on income in some of the principal States, in order to arrive at a tentative comparison between conditions prevailing in the Provinces and the States for the purpose of our argument, and it will be seen that the provision for taxes on income in the States is, to say the least, as yet primitive. The following is an illustrative analysis of the taxes on income in force in some of the major States today during the recent years.

KASHMIR

In the case of every individual Hindu undivided family, every unregistered firm and every other association of individuals other than a registered firm, the rate of income-tax to be paid on a total income of Rs. 2,000 or upwards, but less than Rs. 5,000 per annum, is 5 pies; where it is Rs. 5,000 or upwards but less than Rs. 10,000, 7 pies; where it is Rs. 10,000 or upwards but less than Rs. 15,000, 9 pies; where it is Rs. 15,000 or upwards but less than Rs. 20,000, 1 anna; and Rs. 20,000 or upwards but less than Rs. 45,000, 1 anna and 6 pies.

But when the total income of every company and registered firm is above Rs. 999 and under Rs. 45,000, the rate of income-tax is 1 anna and 6 pies in the rupee.

BAHAWALPUR

The rate of income-tax in the case of an individual, Hindu undivided family is 4½ pies in the rupee on a total income of Rs. 1,000 and upwards, but less than 2,000; 6 pies on Rs. 2,000 or upwards but less than Rs. 5,000; 9 pies on Rs. 5,000 but less than Rs. 10,000; 12 pies on Rs. 10,000 or upwards but less than Rs. 15,000; 16 pies on Rs. 15,000 but less than Rs. 20,000; 19 pies on Rs. 20,000 or upwards but less than Rs. 40,000; 25 pies on Rs. 40,000 but less than Rs. 1,00,000; and 30 pies on Rs. 1,00,000 and over.

The surcharge will be 15 per cent if the total income is Rs. 2,000 or more but less than Rs. 5,000; 40 per cent if it is Rs. 5,000 or more but less than Rs. 10,000; 40 per cent if it is Rs. 10,000 or more but less than Rs. 15,000; 50 per cent if it is Rs. 15,000 and over.

Super-tax:—The exemption limit is placed at Rs. 25,000. On the next Rs. 10,000, the super-tax will be 1 anna; on the next Rs. 20,000, 2 annas; on the next Rs. 70,000, 3 annas; on the next Rs. 75,000, 4 annas; on the next Rs. 1,50,000, 5 annas; on the next Rs. 1,50,000, 6 annas; and on the balance of total income, 7 annas.

In the case of a company, on the total income, the super-tax charged will be 24 pies.

Excess Profits Tax:—60 per cent.

PATIALA

In the case of every individual, Hindu undivided family, and other association of individuals, on the first Rs. 500 of the total income the income-tax rate is nil; the next Rs. 1,400 is liable to a tax of 6 pies; the next Rs. 3,000 is liable to a tax of 7 pies, the next Rs. 5,000, 14 pies; the next Rs. 5,000 is again liable to a tax of 22 pies; and the balance is liable to a tax of 27 pies.

If the total income does not go beyond Rs. 1,000, it is exempt from income-tax. But under no circumstances shall the income-tax payable exceed half the amount by which the total income exceeds Rs. 1,000.

But in the case of every company, on the whole of total income, the tax is charged at 30 pies.

Super-tax:—In the case of every individual, Hindu undivided family and other association of individuals, the first Rs. 25,000 of total income is exempt from income-tax; on the next Rs. 10,000, 12 pies; on the next Rs. 20,000, 18 pies; on the next Rs. 70,000, 24 pies; on the next Rs. 75,000, 36 pies; and on the balance of total income, 48 pies.

The whole of total income, in the case of every company, is liable to a Super-tax of 12 pies.

KAPURTHALA

The first Rs. 750 of the total income is exempt from income-tax. On the next Rs. 1,250, Rs. 2-9-8; on the next Rs. 3,000 Rs. 4-14-2; on the next Rs. 5,000, Rs. 13-0-4; on the next Rs. 5,000, Rs. 20-13-4; on the next Rs. 10,000, Rs. 26-0-8; on the next Rs. 10,000, Rs. 38-8-8; and on the balance Rs. 45. No Income-tax need be paid on a total income which does not exceed Rs. 1,000.

Neither Super-tax, nor Excess Profits Tax has been levied.

GWALIOR

Income-tax and super-tax have not been levied.

Excess Profits Tax, otherwise known as the War Profits Tax, is a special feature of Gwalior. Over and above the standard profits (one sixth of the profits or Rs. 18,000/- per annum, whichever may be greater) during a certain accounting period, the remaining profits are liable to a tax of Rs. 60 per cent of such excess, on the understanding that two-thirds of this tax is refundable within three years after the war is over, and that until that time to be blocked in the shape of war loans.

RAMPUR

In the case of every individual, Hindu undivided family, and any other association of individuals, on the first Rs. 5,000 of total income, there is no income-tax. On the next Rs. 5,000,

the income-tax is 9 pies; on the next Rs. 5,000, it is 1 anna and 3 pies; and on the balance of income, it is 2 annas.

Moreover, in the case of every company, under the Ranpur State Income-Tax Act of 1944, the income-tax is to be charged at the maximum rate of 2 annas.

Super-tax:—In the case of every individual, a Hindu undivided family and other association of individuals, on the first Rs. 40,000, the tax is nil; on the next Rs. 10,000, 1 anna; on the next Rs. 20,000, 2 annas; on the next Rs. 70,000, 3 annas; on the next Rs. 75,000, 4 annas; on the next Rs. 1,50,000, 5 annas; on the next Rs. 1,50,000, 6 annas; and on the remaining total income, 7 annas.

In the case of every company, the total income is liable to a tax of 1 anna in the rupee.

Excess Profits Tax has not been levied.

JAIPUR

Income-tax and super-tax have not been levied.

Excess Profits Tax was levied on 1st September, 1944. Since then, it was assessed at 60 per cent of the excess profits over the standard profits, the minimum being Rs. 36,000.

BIKANER

NIL

MAYURBHANJ

In the case of every individual, Hindu undivided family and other association of individuals, on the first Rs. 1,500 of the total income, nil; on the next Rs. 3,500, 7½ pies; on the next Rs. 5,000, 12 pies; on the next Rs. 5,000, 15 pies; on the next Rs. 5,000, 18 pies; on the next Rs. 5,000, 24 pies; and on the remainder, 30 pies.

No income-tax need be paid on a total income which does not exceed Rs. 2,000.

Irrespective of the amount of total income, a uniform rate of 30 pies in the rupee will be leviable.

Super-tax:—In the case of every individual Hindu undivided family, and any other association of individuals, on the first Rs. 25,000 of total income, no super-tax is leviable; on the next Rs. 10,000, 9 pies; on the next Rs. 20,000, 12 pies;

on the next Rs. 70,000, 24 pies; on the next Rs. 75,000, 36 pies; and on the remaining total income, 48 pies.

But in the case of a company, the super-tax leviable will be 9 annas in the rupee.

Excess Profits Tax:—This is leviable on 50 per cent of the income over and above the standard profits.

COOCH BEHAR

In the case of every individual, Hindu undivided family and other association of individuals the first Rs. 1,000 of total income is exempted; if the total income is Rs. 1,500 or more but less than Rs. 2,000, the tax will be 3 pies; if it is Rs. 2,000 or more but less than Rs. 3,000, the tax will be 3½ pies; if it is Rs. 3,000 or more but less than Rs. 4,000, 4 pies; if it is Rs. 4,000 or more but less than Rs. 5,500, 5 pies; if it is Rs. 5,500 or more but less than Rs. 7,000, 6 pies; if it is Rs. 7,000 or more but less than Rs. 9,500, 7 pies; if it is Rs. 9,500 or more but less than Rs. 12,000, 8 pies; if it is Rs. 15,000 or more but less than Rs. 20,000, 12 pies; if it is Rs. 20,000 or more but less than Rs. 25,000, 15 pies; if it is Rs. 25,000 or over, 18 pies.

If the total income is below Rs. 1,500, it will be exempted.

In the case of companies, the income-tax chargeable on the total income will be 18 pies in the rupee.

Super-tax:—When total income-tax is less than Rs. 20,000, there is no super-tax. Over and above this limit, it will be charged at the rate of 1 anna per rupee.

Excess Profits Tax:—This will be charged at 50 per cent of the excess over the minimum standard of Rs. 30,000.

BARODA

In the case of every individual, Hindu undivided family and any other association of individuals, on the first Rs. 2,500 of the total income, no income-tax will be charged; on the next Rs. 2,500, 6 pies; on the next Rs. 5,000, 9 pies; on the next Rs. 10,000, 1 anna; on the next Rs. 20,000, 1 anna and 6 pies; and on the balance 2 annas.

If the total income is Rs. 3,000 or less, no income-tax need be paid, and the income-tax shall in no case exceed half the amount by which the total income exceeds Rs. 3,000

In the case of every unregistered firm and other association of individuals, on the first Rs. 1,500 of total income no income-tax need be paid; on the next Rs. 3,500, 6 pies; on the next Rs. 5,000, 1 anna; on the next Rs. 5,000, 1 anna and 6 pies; and on the remaining income, 2 annas.

In the case of every company and registered firm, on the first Rs. 30,000, no super-tax would be levied; and on the remaining total income, the super-tax will be 1 anna in the rupee.

Excess Profits Tax:—Levied on a basis which is the equivalent of $66\frac{2}{3}$ per cent, by which the profits of the business exceed the minimum standard of profits. This levy was introduced from August 1, 1943 and covered the profits made upto March 31, 1946.

BHAVNAGAR

In the case of every individual, Hindu undivided family, and other association of individuals, on the first Rs. 1,500 no income-tax need be paid; on the next Rs. 3,500, 3 pies; on the next Rs. 5,000, 6 pies; on the next Rs. 5,000, 12 pies, and on the remaining total income above Rs. 15,000, 18 pies.

No income-tax shall be payable when the total income does not exceed Rs. 2,400, and it shall in no case exceed half the amount by which the total income exceeds Rs. 2,400.

In the case of every company and registered firm, income-tax will be paid at the rate of 18 pies in the rupee on the total income.

Super-tax:—In the case of every individual, Hindu undivided family and other association of individuals, the first Rs. 25,000 is exempted from taxation; on the next Rs. 25,000, 6 pies in the rupee; on the next Rs. 50,000, 12 pies; on the balance above Rs. 1,00,000, 18 pies.

In the case of every company the first Rs. 25,000 of total income is liable to a tax at the rate of 3 pies in the rupee; on the next Rs. 25,000 at the rate of 6 pies and on the balance above Rs. 50,000, 12 pies.

Excess Profits Tax:—This ceased to be operative on profits arising after 1-11-1945.

KOLHAPUR

In the case of every individual, Hindu undivided family and other association of individuals, the first Rs. 1,500 is exempt

from taxation; on the next Rs. 3,500, 9 pies income-tax, and 6 pies surcharge; on the next Rs. 5,000, 1 anna and 3 pies income-tax, and 10 pies surcharge; on the next Rs. 5,000, 2 annas income-tax, and 10 pies surcharge; on the next Rs. 5,000 annas income-tax, and 1 anna and 6 pies surcharge and on the balance of the total income, 2 annas and 6 pies income-tax and 2 annas surcharge.

But in no case on a total income of Rs. 2,000 need income-tax be payable, and in no case should it exceed half the amount by which the total income exceeds Rs. 2,000.

In the case of every company, on the whole of the income the income-tax rate will be 2 annas and 6 pies in the rupee, and the surcharge would be 2 annas in the rupee.

Super-tax:—In the case of every individual, Hindu undivided family and other association of individuals, the first Rs. 25,000 will be exempted from super-tax and surcharge; on the next Rs. 10,000, 1 anna in the rupee super-tax and 1 anna in the rupee surcharge; on the next Rs. 20,000, 2 annas super-tax and 2 annas and 6 pies surcharge; on the next Rs. 70,000, 3 annas super-tax and 2 annas and 6 pies surcharge; on the next Rs. 75,000, 4 annas super-tax and 3 annas surcharge; on the next Rs. 1,50,000, 5 annas super-tax and 3 annas surcharge; on the next Rs. 1,50,000, 6 annas super-tax and 3 annas surcharge; and on the remaining total income, 7 annas super-tax and 3 annas and 6 pies surcharge.

In the case of every local authority, on the whole of total income, 1 anna super-tax and 1 anna surcharge.

In the case of an association of persons, being a registered co-operative society, on the first Rs. 25,000, there will not be any super-tax or surcharge; on the balance of the total income, 1 anna super-tax and 1 anna surcharge.

In the case of every company on the whole of the total income, 2 annas in the rupee as super-tax and no surcharge for the same.

Excess Profits Tax:— $66\frac{2}{3}$ per cent of the excess profits.

BHOPAL

In the case of every individual, Hindu undivided family and other association of individuals, when the total income is

Rs. 1,500 or more but less than Rs. 2,000 the income-tax will be 2 pies in the rupee; when it is Rs. 2,000 or above but less than Rs. 5,000, 3 pies in the rupee; when it is Rs. 5,000 or more but less than Rs. 10,000, 6 pies in the rupee; when it is Rs. 10,000 or more, 9 pies in the rupee.

In the case of every company and registered firm when the total income will be Rs. 15,000 or more, 18 pies in the rupee.

INDORE

Industrial Tax:—On the first Rs. 50,000, 18 pies per rupee; and on profits over Rs. 50,000, 30 pies in the rupee.

HYDERABAD

The State does not levy any income-tax or super-tax. But an Excess Profits Tax had been levied for the years 1941-42, 1942-43 and 1943-44, and was withdrawn as from the 6th October, 1945.

For the year 1941-42, 20 per cent was taxed, 10 per cent of the deposit being returnable with interest, and for the years 1942-43, 1943-44 and 1944-45, 40 per cent was taxed, and 20 per cent of the deposit was returnable with interest.

MYSORE

In the case of every individual, Hindu undivided family, and other association of individuals, on the first Rs. 1,500, no income-tax need be paid; on the next Rs. 3,500, 5 pies; on the next Rs. 5,000, 9 pies; on the next Rs. 10,000, 15 pies; on the next Rs. 20,000, 24 pies; on the next Rs. 20,000, 36 pies; on the balance of total income, 42 pies. But no income-tax need be paid if total income does not exceed Rs. 2,400; and in no case, shall the income-tax exceed half the amount by which the total income exceeds Rs. 2,400.

In the case of every company, the first Rs. 1,500 shall be exempted; on the next Rs. 3,500, 24 pies and on the balance, 42 pies.

Super-tax:—In the case of individuals, on the first Rs. 30,000 no super-tax need be paid; on the next Rs. 30,000, 18 pies; on the next Rs. 40,000, 27 pies; on the next Rs. 50,000, 36 pies; and on the balance 48 pies.

In the case of a Hindu undivided family, and other association of individuals, the first Rs. 50,000 of the total income shall be exempt; on the next Rs. 10,000, 18 pies; on the next Rs. 40,000, 27 pies; on the next Rs. 50,000, 36 pies and on the balance, 48 pies.

In the case of every company, on the first Rs. 1,500 no super-tax; on the next Rs. 3,500, 18 pies; next Rs. 5,000, 27 pies; on the next Rs. 10,000, 36 pies; and on the balance 42 pies.

Excess Profits Tax:—Levied at 60 per cent on the profits in excess of the standard profits, the standard being Rs. 36,000.

TRAVANCORE

In the case of every individual, Hindu undivided family and other association of individuals, when the total income is less than Rs. 2,000, no income-tax need be paid; when the total income is Rs. 2,000 or more, but less than Rs. 5,000, 10 *cash* in the rupee shall be paid; when it is Rs. 5,000 or more but less than Rs. 10,000, 13 *cash* in the rupee; when it is Rs. 10,000 or above but less than Rs. 15,000, one *chukram* and two *cash* in the rupee; when total income is Rs. 15,000 or above but less than Rs. 20,000, one *chukram* and eight *cash* in the rupee; when Rs. 20,000, or above but less than Rs. 30,000, two *chukrams* and four *cash*; when Rs. 30,000 or upwards but less than Rs. 40,000, three *chukrams*; when Rs. 40,000 or more but less than 50,000, three *chukrams* and eight *cash*; when Rs. 50,000 or more but less than Rs. 75,000, three *chukrams* and ten *cash*; when above 75,000 but less than Rs. 1,00,000, three *chukrams* and twelve *cash*; when total income is Rs. 1,00,000 or more, four *chukrams*.

Surcharge:—No surcharge need be paid when the total income is less than Rs. 2,000; when total income is Rs. 2,000 but less than Rs. 5,000, 5 *cash* in the rupee; when total income is Rs. 5,000 or more but less than Rs. 10,000, six and a half *cash*; when it is Rs. 10,000 or more but less than Rs. 15,000, nine *cash*; when it is Rs. 15,000 or more but less than Rs. 20,000, twelve *cash*; when it is Rs. 20,000 or more but less than Rs. 30,000, one *chukram* and two *cash*; when it is Rs. 30,000 or more but less than Rs. 40,000, one *chukram* and eight *cash*; when it is Rs. 40,000 or more but less than Rs. 50,000, one

chukram and twelve *cash*; when it is Rs. 50,000 or more but less than Rs. 75,000, one *chukram* and thirteen *cash*; when it is Rs. 75,000 or more but less than Rs. 1,00,000, one *chukram* and fourteen *cash*; when the total income is Rs. 1,00,000 or more, two *chukrams*.

In the case of every company or registered firm, two *chukrams* in the rupee shall be paid.

Super-tax:—In the case of every Hindu undivided family and other association of individuals and every individual, on the first Rs. 20,000 of total income, no super-tax need be paid and no surcharge; on the next Rs. 15,000, one *chukram* and twelve *cash* in the rupee for super-tax and fourteen *cash* in the rupee as surcharge; on the next Rs. 20,000, three *chukrams* and eight *cash* in the rupee as super-tax and one *chuckram* and twelve *cash* as surcharge; on the next Rs. 70,000, five *chuckrams* and four *cash* as super-tax and two *chuckrams* and ten *cash* as surcharge; on the next Rs. 75,000, seven *chuckrams* super-tax and three *chuckrams* and eight *cash* surcharge; on the next Rs. 1,50,000, eight *chuckrams* and six *cash* as surcharge; on the next Rs. 1,50,000, ten *chuckrams* and eight *cash* as super-tax and five *chuckrams* and four *cash* as surcharge; and on the balance of total income, twelve *chuckrams* and four *cash* as super-tax and six *chukrams* and two *cash* as surcharge.

In the case of every company, on the total income two *chuckrams* and ten *cash* in the rupee as super-tax and no surcharge.

Excess Profits Tax:—It was 60% on the excess profits, the minimum being Rs. 36,000.

COCHIN

In the case of every individual, Hindu undivided family and other association of individuals, the income-tax on the first Rs. 1,500 is nil; on the next Rs. 3,500 is 8 pies; on the next Rs. 5,000 is 12 pies; on the next Rs. 5,000 is 18 pies. on the balance is 24 pies. But no income-tax shall be payable on a total income which does not exceed Rs. 2,000, and shall in no case exceed half the amount by which the total exceeds Rs. 2,000.

In the case of every company, the income-tax on the whole income is 24 pies.

Super-tax:—In the case of every individual, Hindu undivided family and other association of individuals, on the first Rs. 25,000 no super-tax shall be levied; on the next Rs. 10,000, 8 pies; on the next Rs. 20,000, 16 pies; on the next 70,000, 24 pies; on the next Rs. 75,000, 32 pies; next Rs. 1,50,000, 40 pies; on the next Rs. 1,50,000, 48 pies; and on the balance, 56 pies.

In the case of every company, on the whole of total income 12 pies shall be paid. No super-tax on a total income shall be payable which shall not exceed Rs. 25,000, and the super-tax shall in no case exceed half the amount by which the total income exceeds Rs. 25,000.

Excess Profits Tax:—On the first Rs. 36,000, no excess profits tax need be paid; on the balance, 60 per cent.

An examination of the above analysis of income-tax in some of the prominent States shows that, whereas the practice prevailing in the Provinces has been faithfully copied, the incidence is lighter than in the case of the Provinces. The following table will illustrate this point:

Income-tax Yields in some Selected States.

(In Rupees.)

Kashmir	12,30,000	(1944-45)	Baroda	74,17,000	(1944-45)
Bahawalpur	12,15,000	(1944-45)	Cambay	Nil	(1943-44)
Kapurthala	3,79,000	(1944-45)	Nawanagar	Nil	(1943-44)
Patiala	Nil	(1944-45)	Bhavnagar	Nil	(1942-43)
Gwalior	Nil	(1944-45)	Kolhapur	7,77,000	(1943-44)
Rampur	Nil	(1943-44)	Bhopal	12,000	(1941-42)
	(Since introduced)		Rewa	Nil	(1944-45)
Jaipur	Nil	(1943-44)	Dholpur	Nil	(1944-45)
Bikaner	Nil	(1944-45)	Hyderabad	Nil	(1944-45)
Jodhpur	Nil	(1944-45)	Indore	Nil	(1943-44)
Udaipur	5,000	(1945-46)	Mysore	1,73,37,000	(1944-45)
Bharatpur	Nil	(1944-45)	Travancore	1,12,76,000	(1944-45)
Mayurbhanj	3,45,000	(1944-45)	Cochin	31,36,000	(1942-43)
Cooch Behar	2,29,000	(1943-44)			

Note:—Information for more recent years is not available for all these States, though the figures quoted above are from the *latest* available administrative report of each State concerned. We know that Rampur, for example, has recently introduced income-tax, but we are unable to obtain the actual yield from this source of revenue.

As we write, the Finance Minister of Gwalior has stated, in his budget statement for 1947-48, that his Government might

have to impose taxes on income, sooner or later. He argued the point that policies in the neighbouring areas, *e.g.*, the U.P. in regard to prohibition etc., would have repercussions upon the income from existing sources in the State, with the result that the quest for alternate sources of incomes becomes an urgent necessity. Indeed, we have reason for the belief that every State, whether it comes into the Union or Pakistan, or elects to remain independent and isolated, would feel, sooner than most people expect, the need for new sources of income, in addition to increasing yields, through deeper incidence, from existing ones. Once the feudal set-up of the Paramount Power is broken up, and windows are opened out into the so far hermetically sealed territories of the States, items of expenditure would crop up which would make many a former *dewan* of the Princes turn in his grave. The upsurge of the people of the States, in hot pursuit of their long-suppressed liberties, would compel the *durbars* of the States to ear-mark, not merely Rs. 18,000 as Gwalior has done for 1947-48 in respect of *Harijan* uplift, but lakhs of rupees for the amelioration of this and other categories of people, who today demand their right to education, medical relief and employment—to mention only a few of the pressing needs of the country. Existing heads of expenditure, *e.g.*, the Rulers' privy purse, military and police, etc., would be drastically cut down, and new heads would be instituted, so that the commonalty of the people get vested with their rights.

Taxes on income have come to stay, and we may soon have the agricultural income-tax, which the existing Provincial Governments are unable to stomach as yet. The imposition of death duties, the abolition of the *zamindari* system, through a system of compensation to the non-cultivating land-owners and the re-vesting of the tillers of the soil with their halcyon rights to property; the abolition of the salt tax, for which India has fought for nearly half a century; the introduction of prohibition, and a host of other developments of today, definitely give notice to the States that their greatest task is the redrafting of their fiscal systems, in which the social need is recognised through an incidence of taxation, in which the unearned incre-

ment gives place to the theory of the greatest good of the greatest number.

DIVISION OF RESIDUARY INCOME-TAX

We must now examine the Niemeyer Award on the division of residual income-tax between the Centre and the Provinces. We have already commented on the point that, in contra-distinction to the stand taken by the Meston Committee, the anxiety of Sir Otto Niemeyer was more to ensure the financial stability of the Provinces than that of the Centre. Despite what Sir Otto Niemeyer said regarding the need to prevent Provinces being tempted "to mortgage in advance these prospective additional revenues," his anxiety was to arrive at a divisible pool of residual income-tax, which will ensure the financial stability of the Provinces. He rejected considerations like the extent of population, the period of residence, the origin of income, etc., as criteria for determining specific portions of the divisible pool to which Provinces become entitled. He argued as follows (paragraph 33): "It cannot be said that any of the proposed bases have any particular scientific validity, or satisfy in any appreciable degree the ideal but practically unascertainable test of capacity to pay. The mere accident of place of collection, as has frequently been pointed out in previous discussions on this subject, is clearly as unsuitable guide. The residence of the individual, though it may be a convenient practical dividing line for purposes of avoiding double taxation between separate political units, is not in itself a very scientific criterion, particularly in a Federation, and in fact in India gives results (of necessity partly estimated) too suspiciously near those of collection to inspire much confidence." Sir Otto Niemeyer finally argued that, even supposing that it was practicable to ascertain how and where particular portions of the income of a prospective assessee have originated, federal integration of territories involves more of consideration of benefits and incidence pertaining to any Federal financial pooling, in which the weal of the community as a whole becomes involved, than of the respective rights or otherwise of contending parties becomes the ultimate yard-

stick of measurement. So far as the States are concerned, the same principle remains valid with equal force.

The following are the Niemeyer percentages of the Provincial share of 50 per cent of the residual taxes on income :

<i>Province.</i>	<i>Percentage.</i>
Madras	15
Bombay	20
Bengal	20
United Provinces	15
Punjab	8
Bihar	10
Central Provinces	5
Assam	2
North-West Frontier Province	1
Orissa	2
Sind	2
	100

Later in this Chapter we have argued the position relating to the Niemeyer proposals on grants-in-aid which the Provinces have come to enjoy from out of the Central revenues during the past ten years, and here we come to a final consideration of taxes on income arising both in the Provinces and the States which agree to participate in the Union Centre.

Income must be considered to be indivisible, whether it arises in the Provinces or in the States for the purposes of Union Finance and taxation. Like in the case of the Provinces, the tax collecting machinery of the Union Centre must, in principle, have access to sources of income in the States participating in the Union. Whether delegation of powers from the Union Centre to the finance departments or other tax collecting machinery of the States is the more easy expedient, at any rate for an initial period of years, until the States bring their fiscal and taxation systems into line with those prevailing in the Provinces, is a point which need not be debated here at length. In all certainty, it would be administratively convenient for the Union Centre, during the initial period, to invest the States with powers for the collection of income-tax for and on behalf of the Union Centre, even on the assurance that there will be a divisible pool available for the States concerned to meet their own expenditure requirements. We are, however, strongly of the opinion that the provision of Section 138(3) of the Constitution

Act, which gives the option to a State to pay a prescribed amount, in lieu of the Federal enforcement of a surcharge on taxes on income, should not become the permanent basis for adjustment of incomes of the component units of the Union. Such permanent option to the States is unthinkable in character, and we strongly deprecate any principle which tends to operate unjustly as between the Provinces and the States, the advantage being with the latter.

The analysis of taxes on income which are either in force or on the statute book of a representative list of States, which was given earlier in this Chapter, shows the essential inequalities of the taxation structure of the Provinces and the States. We concede the point that the States are backward economically, and that their taxation systems *might* become regressive in character, until vast schemes of reconstruction and development are taken in hand. Our anxiety is that there must be a progressive acceleration of administrative efficiency, economic development, and fiscal justice in the States, which have got to participate on an equal basis with the Provinces in the fiscal *regime* of the Union Centre. The creation of a divisible pool of residual income-tax in which the States are to participate, cannot become an argument, at a later stage, for States to advance the claim that, since they have surrendered a portion of the tax, which would have been theirs, had they not come into the Union, they must be entitled to an automatic scale of relief, on the plea that their budgetary requirements demand such grants-in-aid or subventions from the finances of the Union Centre. We have repeatedly pointed out that the economy of the Union Centre must be integral, both to the Provinces and the States, and that the weal of the community, both in the Provinces and the States, remains an indivisible whole.

Just as the Davidson Committee observed, while the States must of necessity shoulder the responsibility for meeting the requirements of deficit Provinces, the Provinces, as well as the Union Centre, must, in a similar way, come to the rescue of deficit States, once the polity of the Union Centre gets going. In this place, our anxiety is not merely to distinguish between general obligations undertaken by Provinces and States, even

within the meaning of the recommendations' of the Davidson Committee, but to show that agreement on the surrender of Federal or Union surcharges to the Centre cannot be an argument for receipt by the States of proportionate relief from Central finances. Thus, we cannot endorse the following dictum of the British White Paper of December 1931 (paragraph 141) : "The Powers of the Federal Legislature in respect of the imposition of taxes on the income or capital of companies will extend, but not until the expiry of ten years from the commencement of the Constitution Act, to the imposition of taxes on companies in any State-member of the Federation. Any taxes so imposed will, if any State so elects, be collected directly from the State by the Federal Government and not from the company." To put it in other words, taxes on income must be obtained by the Union Centre on a uniform basis from the *peoples* of the Provinces and the States. There cannot be any adjustments between the *durbars* of the States and the Union Centre, for the result would be that mendicancy would become rampant in the States, the Union Centre would be obliged to give doles, and the intention behind the suggested financial settlement, in extension of the Niemeyer Award, would become nullified.

DEFICITS OF THE CENTRE

The abnormalities of the recent wartime finances of the Government of India, the Provinces and the States have been responsible for a fatal belief that the Atlas of the Centre can be asked to shoulder all and sundry of the responsibilities of governance over the people of the country as a whole. We regret that proper study has not been as yet devoted in this country to the relationship which ought to exist between Central, Provincial and Local finance, and we include in this statement the position of the States as well. There is an unjustifiable belief in the land that the Centre is capable of carrying any burden which can be passed on to its shoulders. Few people, including officials and economists, realise how grievous have been the responsibilities of the Centre, and how impossible it is becoming for the Centre to finance its ever-expanding activities and responsibilities from current revenue. More than

this, fewer still recognise the writing on the wall. The Union Centre might as well have its back broken, if steps are not taken to ensure its financial solvency. The experience of the past quarter of a century in this land, especially the tragic incidence of burdens on the Centre from the shift from the Meston to the Niemeyer Award, which was noticed by us in the preceding Chapter, is conclusive that Central finances are bound to remain for long in the doldrums, unless there is a complete overhaul of existing conceptions and arrangements in the financial sphere.

The tables on the next four pages show at a glance the financial implications of the budgets of the Centre during the past twenty-eight years:

TAXES ON INCOME

Central Government's Revenue
(In lakhs of rupees)

Heads	1920-21	1921-22	1922-23	1923-24	1924-25	1925-26	1926-27	1927-28	1928-29	1929-30	1930-31	1931-32	1932-33	1933-34
Customs	31,97	34,41	41,35	39,70	45,75	47,78	47,38	48,21	40,28	51,28	46,81	46,44	51,95	47,16
Excise (Central)	20,44	..	..	..	..	..	..	..	..	..	..	..	..	..
Excise (Provincial)	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Corporation Tax .. .. .	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Income-tax.. .. .	22,19	18,74	18,00	18,24	16,03	15,92	15,72	15,07	16,70	16,71	16,00	17,49	17,97	17,13
Salt	6,76	6,34	6,82	10,02	7,39	6,33	6,70	6,63	7,60	6,76	6,83	8,58	10,07	8,86
Opium	3,53	3,07	3,79	4,25	3,79	4,15	4,33	3,95	3,27	3,04	2,53	2,07	89	1,59
Land Revenue	31,97	..	..	..	..	..	..	..	..	..	..	..	..	..
Stamps	10,96	..	..	..	..	..	..	..	10,96	..	..	..	..	..
Other Heads	7,51	2,20	2,34	2,28	2,07	77,75	2,18	2,30	2,24	2,21	2,03	2,19	1,85	1,80
Total	135,27	64,77	72,29	74,48	75,04	152,19	76,31	76,16	79,09	80,04	74,21	76,77	82,75	76,54

UNION FINANCES

Central Government's Revenue—(Contd.)

(In lakhs of rupees)

Heads.	1934- 35	1935- 36	1936- 37	1937- 38	1938- 39	1939- 40	1940- 41	1941- 42	1942- 43	1943- 44	1944- 45	1945- 46	1946- 47 Revi- ed	1947- 48 Budget
Customs	52,67	54,11	53,58	43,11	40,51	45,87	37,30	37,89	25,12	26,37	39,76	73,61	87,50	93,00
Excise (Central) ..	..	..	..	7,66	8,66	6,53	9,49	13,15	12,79	24,94	38,14	46,36	42,79	40,93
Excise (Provincial) ..	..	..	38	21	26	25	26	32	38	48	70	89	1,05	1,05
Corporation Tax ..	..	..	..	1,88	2,04	2,38	4,14	11,66	31,40	51,28	83,65	75,73	69,53	75,89
Income-tax	17,55	17,07	15,34	12,70	13,74	14,20	17,63	25,01	43,46	58,37	81,09	73,55	57,60	59,70
Salt	8,00	8,43	8,81	8,39	8,12	10,86	7,67	9,19	10,91	8,33	9,29	10,20	9,10	1,00
Opium	72	61	48	51	51	47	47	64	75	80	1,04	99	1,50	1,40
Land Revenue .. ..	..	..	17	19	18	16	18	19	20	33	31	28	32	33
Stamps .. .. .	..	..	39	36	35	36	39	41	52	71	79	84	1,02	1,04
Other Heads	1,92	1,94	91	20	24	22	30	27	17	21	23	11	48	68
Total	80,85	82,17	80,05	75,22	74,61	81,30	77,85	98,76	125,71	172,01	255,01	282,73	270,87	275,01

TAXES ON INCOME

Central Government's Expenditure.
(In lakhs of rupees)

Heads.	1920-21	1921-22	1922-23	1923-24	1924-25	1925-26	1926-27	1927-28	1928-29	1929-30	1930-31	1931-32	1932-33	1933-34
I. On Revenue Account:														
Railways...	19,38	8,80	9,94	11,24	18,61	17,32	16,51	20,65	20,26	18,80	20,22	20,63	20,46	20,15
Irrigation...	7,02	14	13	15	22	20	15	17	21	29	35	21	21	4
P. & T. ...	9,44	14	17	9	7	-1,04	76	79	82	83	85	25	86	89
Currency & Mint ...	23	44	43	43	41	43	53	59	59	63	95	75	65	58
Defence Services ...	.....	59,53	54,14	46,47	43,85	47,22	47,65	43,70	45,23	44,72	44,54	43,71	39,27	38,86
Total (a) ...	231,28	96,64	89,91	88,09	90,57	93,20	95,30	91,59	92,77	93,31	97,04	95,18	87,61	84,03
II. Capital Expenditure:														
Railways...	25,89	9,40	8,57	10,90	7,03	11,77	18,82	18,62	15,67	13,28	7,50	4,07	-97	-3,11
P. & T. ...	.....	82	66	75	1,18	2,12	23	33	43	26	52	84	15	5
Defence ...	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....
Total (b) ...	27,81	11,42	11,15	13,46	9,59	16,60	21,08	20,28	17,03	14,87	11,40	5,86	-59	-1,69
III. Debts, Deposits and Advances:														
Floating Debt ...	.....	.....	40,62	19,47	2,12	.....	8,18	1,95	.....	.....	3,99	.....	45,18	2,84
Unfunded Debt ...	.....	.....	.....	.....	.....	2,09	.....	.....	.....	.....	9,68	.....	.....	.....
Permanent Debt ...	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....
Loans by Centre ...	.....	1	.....	3	1,23	8,92	5,89	7,77	12,72	7,20	10,97	.....	.....	11,46
Loans between Centre and Provinces ...	.....	6,38	.....	10,12	8,86	.....	.....	.....	.....	.....	.....	.....	.....	2,84
Remittances of Provl. Govts. ...	.....	1,05	9,59	23,10	.....	41,27	.....	.....	.....	39,67	.....	.....	32,31	.....
Deposits and Advances ...	.....	.....	.....	.....	.....	.....	1,66	-3,22	-3,09	2,09	3,10	.....	.....	.....
Total (c) ...	.....	7,46	50,21	52,73	12,21	52,28	15,73	6,50	9,63	49,23	27,74	80,97	83,33	20,23

Note:—(a) Includes expenditure on Debt Services, initial expenditure on new capital at Delhi, Civil Administration and miscellaneous items.
(b) Includes payments for discharge of Debentures, construction of irrigation, navigation, etc., pensions, etc.
(c) Includes transfer of cash between England and India and some other minor items.

UNION FINANCES

Central Government's Expenditure—(Contd.)

(In lakhs of Rupees)

Heads.	1934-35	1935-36	1936-37	1937-38	1938-39	1939-40	1940-41	1941-42	1942-43	1943-44	1944-45	1945-46 (Revised)	1946-47 (Budget)	1947-48 (Budget)
I. On Revenue Account:														
Railways...	19,83	19,58	20,57	29,90	29,98	29,74	35,59	37,00	53,63	42,38	46,12	34,42	31,10	37,95
Irrigation...	6	5	10	11	10	9	9	8	10	8	11	13	19	12
Public Works...	87	80	82	76	77	74	69	67	72	93	99	1,05	1,18	1,05
Post & T. ...	73	40	35	37	36	39	38	1,23	1,75	2,26	2,08	1,51	1,91	1,80
Currency & Mint ...	38,62	39,18	39,82	52,60	52,07	52,26	74,81	105,58	218,54	368,01	412,10	371,76	266,72	201,37
Defence Services ...	87,06	86,86	86,51	122,48	121,71	125,77	151,65	186,89	347,14	492,76	559,98	531,57	442,86	382,54
Total (a) ...	-1,21	97	-1,12	2,47	6,44	4,46	2,81	84	24,39	8,71	18,17	9,85	13,49	29,06
II. Capital Expenditure:														
Railways...	83	39	47	40	2,62	6	4,79	9	39	3,90	3,08	2,17	5,04	3,98
Public Works...	.....	.....	.....	.....	.....	.....	.....	.....	52,51	37,46	62,82	35,09	2,00	.....
Defence ...	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....
Total (b) ...	57	7,65	6	3,28	9,07	4,62	6,93	99	67,54	64,51	81,73	87,45	204,67	117,09
III. Debts Deposits and Advances:														
Floating Debt ...	4,89	23,21	3,59	155,83	221,81	249,48	263,89	461,01	904,63	860,01	898,00	283,27	277,37	280,00
Unfunded Debt ...	.....	.....	9,43	69,69	71,92	65,28	68,23	51,49	42,79	38,25	42,54	56,22	80,83	91,58
Permanent Debt ...	.....	12,13	-11,70	6,99	29,55	51,79	114,84	223,07	123,54	36,34	4,61	55,59	334,49	60,21
Loans by Centre ...	2,10	9,03	.....	86	80	65	1,55	1,45	6,86	14,89	13,78	5,12	20,58	37,71
Loans between Centre and Provinces ...	45,22	17,92	.....	189,89	184,05	255,26	480,44	792,91	1,316,66	1,793,86	2,087,57	1,965,69	729,86	488,89
Remittances ...	.....	.....	.....	96,72	84,92	103,61	156,19	213,26	3,904,05	401,27	574,88	402,75	443,41	289,88
Balances of Provincial Governments ...	-3,66	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....
Deposits & Advances ...	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....	.....
Total (c) ...	48,55	62,29	1,32	519,98	592,95	725,87	1,035,14	1,786,49	1,498,33	8,144,12	4,091,38	2,738,64	1,886,04	1,252,77

Note:—(a) Includes expenditure on Debt Services, initial expenditure on new capital at Delhi, Civil Administration and miscellaneous items.

(b) Includes payments for discharge of Debentures, construction of irrigation, navigation, etc., pensions, etc.

(c) Includes transfer of cash between England and India and some other minor items.

Fiscal and economic circumstances in any country vary from time to time, and introduce in their wake of each change a multiplicity of factors which affect the yields from sources of revenue, particularly customs, income-tax and excises. These factors necessarily contribute either to expand revenues or to contract them. The Central revenues in 1920-21, which were accounted for at Rs. 135 crores, were followed by a tremendous shrinkage in the following year to Rs. 65 crores. The effects of the First World War were by then over, and Central finances were re-adjusting themselves to normalcy. Additional to this, there was the complete disappearance of Central excises, which began in 1921-22, as a result of the Meston Award, under which there came into existence a completely new basis of financial relationship between the Centre and the Provinces.

Revenues of the Central Government kept a steady pace during the years 1921-22 to 1924-25, with Rs. 72 crores, Rs. 74 crores and Rs. 75 crores respectively. There was then a sudden jump of revenues to Rs. 152 crores, explained by the accession of Rs. 78 crores under miscellaneous heads, while the major, normal heads of revenue continued as before. The progress of revenues from 1926-27 was from Rs. 76 crores to Rs. 76 crores in 1927-28; Rs. 79 crores in 1928-29; Rs. 80 crores in 1929-30; Rs. 74 crores in 1930-31; Rs. 77 crores in 1931-32; Rs. 83 crores in 1932-33; and Rs. 77 crores in 1933-34. Later the position was as follows: 1934-35, Rs. 81 crores; 1935-36, Rs. 82 crores; 1936-37, Rs. 80 crores; 1937-38, Rs. 75 crores; 1938-39, Rs. 75 crores; 1939-40, Rs. 81 crores; 1940-41, Rs. 78 crores.

Then began the full impact of the wartime activities of the Government, which led to the abandonment of all considerations of public finance, with mounting taxation trying fugitively to chase mounting expenditure, which was met more out of loans than from revenues. The revenues of the Centre then had the astounding upward curve as follows: 1941-42, Rs. 99 crores; 1942-43, Rs. 126 crores; 1943-44, Rs. 172 crores; 1944-45, Rs. 255 crores; and 1945-46, Rs. 283 crores. Very naturally, the revised budget for 1946-47 showed a decline in revenues to Rs. 271 crores, but in the budget for the current financial year there was a slight recovery to Rs. 275 crores.

An analysis of the individual items of revenue for the Centre during the past quarter of a century would be interesting. Taking customs first, it will be noticed that there was a continuous annual rise in yields from Rs. 32 crores in 1920-21 to Rs. 51 crores in 1929-30. Then, owing to the Great Depression, customs dropped by Rs. 5 crores during each of the next two years. There was recovery to Rs. 52 crores in 1932-33, rising eventually to Rs. 54 crores in 1936-37. Then began the steady decline in customs yields, falling as low as Rs. 25 crores in 1942-43. There was a slight recovery in the following year, and in 1944-45 they rose to Rs. 40 crores. Once commercial imports were re-admitted, the behaviour of customs became extremely impressive, and the yield from this source netted to the Centre Rs. 74 crores in 1945-46, Rs. 88 crores in 1946-47 (revised estimates), and Rs. 93 crores in the current financial year. This extraordinary upward resilience of yields from customs must be traced to the sudden gush of imports, of which the country was starved during the preceding war years, and to the prevailing high prices of commodities the world over. The comment would not be out of place here that it would be an amazing thing indeed if customs could maintain their present yields in the coming years.

We can dispose of income-tax as a source of revenue in briefer space. From Rs. 22 crores in 1920-21, it dropped to Rs. 15 crores in 1927-28. Then began recovery, which persisted during the next eight years, with the yield oscillating round about Rs. 17 crores. In 1937-38 this head touched the all-time bottom of Rs. 13 crores, but rallied during the coming three years to Rs. 18 crores. Wartime increases in taxes of income had led to better and bigger yields in the following years, as hereunder: Rs. 25 crores in 1941-42; Rs. 43 crores in 1942-43; Rs. 58 crores in 1943-44; Rs. 81 crores in 1944-45. Then decline, as was inevitable, set in, with yields only netting Rs. 74 crores in 1945-46, Rs. 58 crores in 1946-47 (revised estimates) and Rs. 60 crores in the budget estimates for the current year.

The story of taxes on income would not be complete, if the yields of the corporation tax are not included in the gross totals. Beginning with less than Rs. 2 crores in 1937-38, this

head of revenue rose to Rs. 2 crores in 1938-39; Rs. 2 crores in 1939-40; Rs. 4 crores in 1940-41; Rs. 12 crores in 1941-42; Rs. 31 crores in 1942-43; Rs. 51 crores in 1943-44; and the extraordinary total of Rs. 83 crores in 1944-45. Then, there was a decline to Rs. 76 crores in 1945-46, and to Rs. 70 crores in the revised estimates of 1946-47, with a comfortable recovery to Rs. 76 crores in the current financial year. If taxes on income and the corporation tax are clubbed together—since they belong to the same species—as they should be, the almost complete domination of Central revenues by these two heads of revenue would become clear. In 1944-45 the combined yields of these two heads had the staggering proportion of 70 per cent to all sources of Central revenue, and in the current year (budget estimates) their percentage was as high as 53.

The following table indicates the surpluses and deficits of the Central Government during the past twenty-seven years:

Surpluses and deficits of Central Government

(In lakhs of rupees)

1920-21	..	..	..	-26,01	1934-35	..	..	36
1921-22	..	..	..	-27,65	1935-36	..	..	..
1922-23	..	..	..	-15,02	1936-37	..	..	- 1,79
1923-24	..	..	..	2,39	1937-38	..	..	....
1924-25	..	..	..	5,68	1938-39	..	..	- 64
1925-26	..	..	..	3,31	1939-40	..	..	....
1926-27	..	..	..	....	1940-41	..	..	- 6,53
1927-28	..	..	..	....	1941-42	..	..	- 12,17
1928-29	..	..	..	-31,54	1942-43	..	..	- 111,78
1929-30	..	..	..	27	1943-44	..	..	- 189,90
1930-31	..	..	..	-11,58	1944-45	..	..	- 160,55
1931-32	..	..	..	-11,75	1945-46	..	..	- 123,89
1932-33	..	..	..	1,55	1946-47 (R.E.)	..	..	- 45,28
1933-34	..	..	..	....	1947-48 (B.E.)	..	..	- 16,96

One valid impression from these figures is an almost fatalistic monotony of deficits, barring the few after the inauguration of the Montagu-Chelmsford Reforms, thanks largely to the Meston Award contributions to the Centre from the Provinces. The Meston Award had its use for a temporary period, and was particularly helpful to the Government of India in preparing to face the Great Depression. The Niemeyer Award has, on the contrary, launched Provincial Autonomy in 1937, with the die definitely cast in favour of the Provinces. The Second World War has shattered the finances of the Centre to an

extent which cannot be precisely estimated today. We postulate recurring deficits in the finances for the Union Centre for a period of years to come after the establishment of the Union, and no administration can run on successive deficits. In view of the fact that almost every administrative unit in India today, whether it be the Government of India, the Provinces or the States, have blue-prints ready for vast schemes of reconstruction, the principle must be established beyond doubt that reconstruction programmes must be generally financed from out of public loans, and that administrative budgets must find their basis in an approximation of routine annual expenditure to revenue, as an orthodox economist would suggest.

In other words, we strongly hold that there must be two budgets for the Union Centre, as much as for the Provinces and the States which are component parts of the Union. In the first place, there must be an annual administrative budget, which balances income and expenditure, and which does not go beyond the requirements of the ordinary day-to-day administration. Any surpluses arising from, or created out of, these annual administrative budgets would go into a common pool for development purposes, to be divided among the component units of the Union. Then we come to a long-term budget, for the Union Centre, for the Provinces and for the States, which would be concerned only with long-term projects of planning, involving vast amounts of capital and recurring expenditure. Here again, there must be a Union pool of finance for reconstruction and development purposes, and this is a question which we will take up in the last Chapter of this book.

SUBVENTIONS AND DIVISIBLE POOL OF INCOME-TAX

The principle behind the Constitution Act, which must necessarily supply the basic framework for the Union Centre, at any rate as far as financial questions are concerned, has been well stated by Sir Otto Niemeyer in paragraph 3 of his Report. He said that "it has been recognised that at the inauguration of Provincial Autonomy, each of the Provinces should be so equipped as to enjoy a reasonable prospect of maintaining financial equilibrium, and, in particular, that the chronic state of deficit into which some of them had fallen should be brought

to an end." In other words, the separation of Sind from Bombay and of Orissa from Bihar, and their constitution into separate Provinces, additional to the constitution of the North-West Frontier and Assam as Governor's Provinces, have been based upon the principle that the community in general in *all* the Provinces must contribute to the maintenance of the financial stability of these four provincial units which assumed their autonomy in 1937. These contributions took the form of Central subventions, and a share in the divisible pool of income-tax. Under the Niemeyer Award, the following annual grants-in-aid became available to the Provinces :

<i>Province.</i>	<i>Amount in lakhs.</i>	<i>Remarks.</i>
U. P.	25	For a fixed period of five years.
Assam	30	Additional to Rs. 7 lakhs in respect of Assam Rifles.
N. W. F. P.	100	Subject to reconsideration at the end of five years.
Orissa	40	With Rs. 7 lakhs additional in the first years, and Rs. 3 lakhs additional in each of the next four years.
Sind	105	For 10 years with Rs. 5 lakhs additional in the first year, then falling in a graduated manner to a point reached by the extinction of the Barrage Debt in a total period of 45 years.

The present position of grants-in-aid is revealed in the Budget Statement for 1947-48 as follows:—

Grants-in-aid to Provincial Governments.

(In lakhs of rupees)

	Actuals.			Revised.	Budget.
	1943-44	1944-45	1945-46	1946-47	1947-48
A. Grants - in - aid to Provincial Governments :					
A. 1—Assam	30.00	30.00	30.00	30.00	30.00
A. 2—N. W. F. P.	1,00.00	1,00.00	1,00.00	1,00.00	1,00.00
A. 3—Orissa	40.00	40.00	40.00	40.00	40.00
A. 4—Sind	1,05.00	.....	.....	.....	.....
Additional grants to Provinces :	3,25.00	7,00.00	8,00.00	.....	.....
Total ..	6,00.00	8,70.00	9,70.00	1,70.00	1,70.00

An adequate illustration of the ramifications of Central loans and grants to Provinces and States is supplied by the consolidated accounts of Central revenues and the Cotton Fund for 1943-44 and 1944-45, the latest available to us. These are distinguished under four heads: irrigational facilities, land clearance and improvement; manure for distribution; and seed multiplication and distribution, the grand total under all heads being some Rs. 6 crores.

Under irrigation facilities, a total of Rs. 41 lakhs was made available as loans to the Provinces, and the principal beneficiaries were C.P. and Berar, Rs. 29 lakhs; Bombay, Rs. 8 lakhs; and Orissa Rs. 4 lakhs. The grants for irrigational facilities, totalling Rs. 105 lakhs, were distributed principally as follows: the U.P. Rs. 30 lakhs; Bombay Rs. 13 lakhs; Bihar Rs. 11 lakhs; the N.-W.F.P. and Madras Rs. 10 lakhs each; the Punjab Rs. 7 lakhs; Bengal Rs. 6 lakhs; Orissa and Assam Rs. 2 lakhs each; and Baluchistan Rs. 38,000. The most interesting entry under this head was that of Baroda, which has a grant of Rs. 4 lakhs.

A total of Rs. 31 lakhs was outstanding in the books of the Government of India under the head loans for land clearance and improvement, the principal beneficiaries being Orissa Rs. 8 lakhs; Madras Rs. 6 lakhs; and the C.P. and Berar and Bombay Rs. 3 lakhs each. As for the grants under this head, the following was the order of importance: Bombay Rs. 16

lakhs; the Punjab Rs. 9 lakhs; Bihar Rs. 6 lakhs; Madras Rs. 2 lakhs; the C.P. and Berar, the U.P. and Orissa Rs. 1 lakh each; Coorg Rs. 41,000; and Baroda Rs. 82,000.

The loans for manure distribution totalled Rs. 54 lakhs, parcelled as hereunder: the C.P. and Berar Rs. 23 lakhs; Madras Rs. 19 lakhs; Bengal Rs. 6 lakhs; Bihar and Assam Rs. 2 lakhs each; and Orissa Rs. 1 lakh. The grants for manure distribution were of the order of Rs. 29 lakhs, and the spreading out was as follows: Bihar Rs. 11 lakhs; Bombay and the C.P. and Berar Rs. 8 lakhs each; Madras Rs. 7 lakhs; the U.P. Rs. 2 lakhs; and the balance in small amounts ranging from Rs. 90,000 to Bengal to Rs. 3,000 to Ajmer-Merwara.

Seed multiplicates and distribution loans and grants were the most impressive of all these categories of Central aid to the Provinces and States, and account for Rs. 224 lakhs. Under the category of loans under this head, the most had gone to Bengal, *viz.*, Rs. 79 lakhs; and other principal beneficiaries were Madras Rs. 26 lakhs; the C.P. and Berar Rs. 15 lakhs; Bihar Rs. 8 lakhs; and Ajmer-Merwara Rs. 2 lakhs. The grants under this head were most widely distributed, beginning with Rs. 14 lakhs for Bengal, with the major beneficiaries being as follows: Rs. 9 lakhs for Bombay; Rs. 8 lakhs for Madras; Rs. 4 lakhs for Assam; Rs. 3 lakhs for Bihar; Rs. 2 lakhs each for the U.P., Orissa and the North-West Frontier Province, and the remainder for the rest of the Provinces, with Rs. 18,000 for Baroda and Rs. 16,800 for Kashmir.

The table on the next page unravels the link-up in this sphere between the Centre on the one part and the Provinces and the States on the other:

UNION FINANCES

Loans and Grants to Provincial Government out of Central Revenues and Cotton Fund during 1943-44 and 1944-45.
(In Rupees)

Name of the Province or State.	Irrigation facilities.		Land clearance and improvement.		Manure for distribution.		Seed multiplicates and distributions.	
	Loan	Grant	Loan	Grant	Loan	Grant	Loan	Grant
	Ajmer-Merwara	2,35,500	7,250	8,000	2,27,000	1,33,716
Assam	.....	38,148	.....	.....	2,10,300	48,417	1,77,667	4,29,900
Baluchistan	.....	5,67,289	.....	.....	.....	11,000	1,66,400	1,17,016
Bengal	.....	11,09,000	.....	5,76,970	6,16,000	89,700	79,14,000	13,98,850
Bihar	.....	13,24,830	.....	16,00,000	1,92,800	11,00,000	7,71,200	3,06,100
Bombay	8,22,500	.....	3,00,000	1,47,985	.....	8,22,927	.....	9,14,719
C. P. & Berar	29,34,000	.....	3,48,970	41,250	22,86,000	8,21,000	15,00,000	4,62,166
Coorg	.....	9,76,250	.....	2,02,466	.....	6,000	.....	.....
Madras	.....	10,21,000	6,25,000	.....	19,00,000	6,66,836	26,00,000	7,75,626
N. W. F. P.	.....	2,45,600	8,22,060	.....	1,39,300	1,14,250	12,74,000	1,60,500
Orissa	2,73,500	.....	.....	9,00,000	.....	15,000	6,62,100	1,61,667
Punjab	.....	7,00,000	.....	.....	.....	.....	.....	.....
Sind	.....	29,83,500	.....	1,01,600	.....	2,15,000	.....	4,49,335
U. P.	.....	.....	.....	.....	.....	.....	.....	1,71,650
J. C. A. R.	.....	1,92,000	.....	82,000	.....	33,550	.....	75,000
Baroda State	.....	.....	.....	.....	.....	.....	.....	80,000
Kashmir State	.....	.....	.....	.....	.....	.....	.....	16,800
Kutch State	.....	.....	.....	.....	.....	.....	.....	.....
Rampur State	.....	.....	.....	.....	.....	.....	.....	.....
Total	41,30,000	1,03,02,117	30,95,571	37,85,571	53,51,650	29,46,877	1,58,92,367	55,52,445

This is the place for an examination of the behaviour of Provincial finances during the past ten years, i.e. 1938-39 to 1947-48, for an extraordinary phenomenon becomes observable with reference to almost all the Provinces. This is the remarkable improvement in the revenue yields of each Province, which was accounted for by the wider range and larger number of items of taxation which were taken recourse to under the stimulus of the wartime boom. While Central Budgets showed staggering deficits during each year of the increasing tempo of World War II, each of the Provinces, at any rate the vast majority of them, had windfalls of almost uniform precision.

Taking revenues first, it will be observed that Madras improved her revenue position from Rs. 16 crores to Rs. 50 crores; Bombay from Rs. 12 crores to Rs. 38 crores; Bengal from Rs. 13 crores to Rs. 48 crores; the U.P. from Rs. 13 crores to Rs. 40 crores; the Punjab from Rs. 11 crores to Rs. 31 crores; Bihar from Rs. 5 crores to Rs. 17 crores; the C.P. from Rs. 4 crores to Rs. 13 crores; Assam from Rs. 3 crores to Rs. 9 crores; the N.W.F.P. from Rs. 2 crores to Rs. 4 crores; Orissa from Rs. 2 crores to Rs. 6 crores; and Sind from Rs. 4 crores to Rs. 9 crores. This three-fold increase in the revenues of almost all the Provinces is a feature which must be reckoned with in any study of the finances of the Union Centre or Pakistan, for it is clear that each one of these Provinces, as units of the Indian Union and Pakistan, can be expected to depend more and more upon their own resources for the financing of their current, routine annual expenditure. Extraordinary expenditure is bound to be met from loan finance, and from Central grants or subventions, as we will see in the last Chapter of this book.

This conclusion of ours is buttressed from a study of the surplus-deficit position of the Provinces during the past decennium. Madras had never experienced any deficit at all during these ten years, though her surpluses were drastically reduced. Bombay, which had a deficit of Rs. 35 lakhs in 1938-39, had no deficits at all during the rest of this decennium, though her bumper surpluses of 1942-43 and 1943-44 of Rs. 2 and Rs. 4 crores respectively were precipitately cut down in the later years. The U.P. had modest surpluses during the majority of the earlier years of this period, but her biggest surplus of

Rs. 95 lakhs of 1946-47 (revised estimates) was converted into a deficit of Rs. 47 lakhs during the current financial year (budget estimates). The record of the Punjab is the most impressive of all Provinces,—it was one continuous story of surpluses of considerable magnitude, though her peak of Rs. 9 crores was brought down to Rs. 3 crores in the current year (budget estimates). Bihar had comfortable surpluses, with a deficit of Rs. 54 lakhs only once, in 1943-44. The C.P. had a surplus financial position, and her deficit of 1938-39 had never recurred in any of the years of this period. Twice in these ten years the North-West Frontier Province had deficits, once of Rs. 5 lakhs in 1939-40, and the second time of Rs. 25 lakhs in 1946-47 (revised estimates), but otherwise it had always enjoyed surpluses. Sind never experienced a deficit in this period, but her surplus of Rs. 4 crores in 1943-44 was brought down to Rs. 3 lakhs in the current financial year (budget estimates).

Of the deficit Provinces of the present day, the cases of Orissa and Assam need not be discussed here in any great detail. Bengal alone was in the exceptionally unfortunate position of having enormous deficits, ranging from Rs. 3 crores in 1943-44 to Rs. 13 crores in 1946-47 (revised estimates), and Rs. 6 crores in the budget estimate for the current financial year. The earlier deficits were caused largely by the denial policy and war measures rendered obligatory by the temporary Japanese push to Kohima, whereas the later deficits were conditioned by phenomenal failure of crops, tornadoes in Midnapore, Chittagong and other areas, and the appalling death roll of 3,900,000 people from starvation, on which the Woodhead Committee had such a lot to say. Added to this was the other complication relating to political instability, and a complete collapse of civil government in the Province, which had always been regarded as very inefficient from the administrative point of view.

The tables on the following three pages show in ready form the substance of Provincial finance during past ten years:

TAXES ON INCOME

Provincial Budgets—Revenues.
(In Crores of Rupees)

Province.	1938-39	1939-40	1940-41	1941-42	1942-43	1943-44	1944-45	1945-46	1946-47 (Revised)	1947-48 (Budget)
Madras	16.1	16.7	18.1	19.5	22.0	29.8	41.2	48.0	60.0	49.7
Bombay	12.4	13.1	14.5	16.9	19.8	25.2	33.7	35.0	36.1	38.9
Bengal	12.8	14.3	13.6	15.0	16.5	23.5	39.4	45.6	39.7	47.7
U. P.	12.8	13.6	14.7	16.4	20.5	24.3	27.5	30.0	34.2	40.1
Punjab	11.4	12.1	13.8	15.4	18.5	26.3	28.9	28.0	29.4	30.8
Bihar	5.2	5.5	6.1	6.6	7.5	10.3	12.8	15.2	15.9	16.6
C. P.	4.3	5.1	5.2	5.3	6.7	8.6	9.6	10.6	11.4	13.0
Assam	2.6	3.0	3.3	3.3	3.9	5.6	6.2	6.5	6.8	9.4
N. W. F. P.	1.8	1.9	2.0	2.2	2.4	2.6	2.8	3.0	3.2	4.2
Orissa	1.8	1.9	2.0	2.4	2.2	2.6	3.2	3.6	4.4	6.1
Sind	3.7	4.3	5.2	5.8	6.6	9.9	8.8	8.6	8.5	9.2

UNION FINANCES

Provincial Budgets—Expenditure.
(In Crores of Rupees)

Province.	1938-39	1939-40	1940-41	1941-42	1942-43	1943-44	1944-45	1945-46	1946-47 (Revised)	1947-48 (Budget)
Madras	16.1	16.4	17.5	18.7	20.7	22.8	40.2	48.0	60.0	49.7
Bombay	12.8	12.8	13.6	15.2	17.8	21.5	31.2	34.1	36.0	38.9
Bengal	12.7	13.7	14.4	15.5	16.8	26.3	44.2	40.6	52.0	53.9
U. P.	12.8	13.4	14.6	16.5	20.4	24.2	27.4	29.9	33.2	40.6
Punjab	11.6	12.0	12.3	13.7	15.1	16.9	21.1	21.3	25.5	28.2
Bihar	4.9	5.4	5.9	6.0	6.6	10.9	10.1	12.1	15.1	16.3
C. P.	4.7	4.8	5.0	5.1	6.5	8.5	9.6	10.5	11.4	11.6
Assam	2.9	3.0	3.1	3.3	3.5	4.5	6.2	6.8	6.8	10.8
N. W. F. P.	1.8	1.9	1.8	2.0	2.3	2.1	2.9	2.8	3.4	4.2
Orissa	1.8	1.8	1.9	2.0	2.1	2.6	3.0	3.4	4.8	7.2
Sind	3.1	4.1	5.1	5.6	6.5	5.9	8.8	8.6	8.5	9.2

TAXES ON INCOME

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Provincial Surpluses and Deficits.

(In Lakhs of Rupees)

Province	1938-39	1939-40	1940-41	1941-42	1942-43	1943-44	1944-45	1945-46	1946-47 Revised	1947-48 Budget
Madras	3.7	28.5	52.8	88.0	125.6	.6	.6	.2	.4	.6
Bombay	-34.9	39.9	87.4	161.0	191.5	370.5	303.5	84.2	8.3	5.9
Bengal.. .. .	..	60.4	-90.9	-56.1	-32.8	-273.7	-480.1	495.8	-1,328.5	-620.1
U. P. .. .. .	..	7.6	1.0	2.0	1.6	1.6	1.5	1.5	94.7	-47.3
Punjab	-25.4	15.5	1.5	1.7	332.5	944.0	828.1	664.1	384.4	258.4
Bihar	31.1	11.8	30.2	54.3	88.7	-54.2	279.7	311.7	75.2	24.7
C. P.	-43.6	32.9	29.9	19.9	21.7	1.1	1.3	11.0	.5	147.1
Assam	-40.9	1.0	16.2	-2.5	32.1	71.5	8.1	-25.6	-1.4	-237.5
N. W. F. P.	2.6	-4.5	9.2	22.3	1.8	20.4	5.3	15.8	-25.0	2.2.
Orissa .. .. .	.7	3.8	11.1	14.7	7.1	1.9	17.8	16.6	-31.5	-110.1
Sind	24.5	23.8	14.5	25.7	13.4	401.4	.1	.6	1.0	3.1

It is a very encouraging thing to note that provincial finances fared extraordinarily well, barring Bengal for the reasons given earlier, during the war period. The Union Centre can take comfort at this remarkable resilience of provincial finances during the current decennium. But it is clear that the Niemeyer Award should be completely scrapped, at any rate as far as subventions are concerned. In the first place, some of the grants-in-aid paid out of Central revenues to Provinces, e.g., the U.P., have ceased to operate. Secondly, if ten years are not sufficient for a Province which was newly created in 1937 to become financially stable, it is time that the Union Centre told the Province to set its house in order and to stop from looking to the Centre for financial aid. In other words, there must be a ceiling put to deficit Provincial finance, and such a ceiling is possible in view of a great variety of additional revenues which the greater number of Provinces have come to enjoy since 1937. A good example of the increasing revenue finances of the Provinces is supplied by the Sales Tax.

We concede the point that, with the assumption of power by popular ministries in the Provinces, nation-building activities have been taken in hand, to an extent hardly ever dreamt of in India, and that consequently Provincial needs of revenue are very great and will continue to be great in the coming years. What with the introduction of progressive prohibition in the Provinces and the consequent loss of excise revenue, and the introduction of schemes of compulsory elementary education, and the extension of medical and sanitary relief, etc., Provinces are definitely in need of additional revenues than ever before.

But the needs of the Centre are far greater than those of the Provinces. In the Budget for 1947-48 the abolition of Salt Tax alone had meant a gap of over Rs. 9 crores of revenue a year, and thanks to the emergency created during the War period, there is a decline in the quantum of overseas trade, though present high price levels (which *will not* continue for ever) still bring considerable moieties into the fisc of the Centre from sea customs. More and more, the Centre is, as shown earlier, depending upon taxes on income and excises to equalise the impending fall in customs. As far as we can visualise from the present indices, it is clear that the Defence expenditure

of the country will never come back to the average position of the inter-war period. In other words, at any rate compared with the averages of the inter-war period, the Defence expenditure of the land in the coming ten years may be up by anything up to Rs. 50 crores. The recommendations of the Pay Commission, when fully implemented, will mean an additional Rs. 30 crores of annual expenditure for the Centre.

On the other hand, the Railways will no longer be in a position to make their expected contributions to the Central fisc. The creation of the Foreign Office and diplomatic representation abroad might make a difference of anything between Rs. 5 to Rs. 10 crores a year to Central expenditure. Vast schemes of planning and development, now under contemplation, will make a tremendous demand on Central resources in the coming years, for the Centre is definitely concerned with the overall picture relating to both the Provinces and the States. Both in respect of capital expenditure, and of expenditure which is met out of revenue, the needs of the Centre for finances are and will continue to be greater than those of the Provinces. If, as yet, this is not recognised as such, we consider that the time has arrived in this country when the Centre must be recognised to shoulder greater responsibilities and greater burdens.

This argument has not been used by us in order to detract from the validity of the general proposition that it is the responsibility of the Union Centre of the future, as it is the responsibility of the Government of India today, that deficit areas should be looked after. Here we derive considerable comfort from paragraph 448 of the Davidson Committee Report, quoted earlier, which, though inoperative today in view of the abandonment of Federation as projected in the early thirties of the present century, brings States also into the picture relating to surplus and deficit areas in the country.

EXISTING ARRANGEMENTS WITH STATES

A brief examination of the existing arrangements between the States and the Government of India, in regard to taxes on income as they exist today, becomes interesting. The States entered into an agreement with the Government of India,

whereby a person living in States' territory does not pay double income-tax. Recently, the Government of India have amended the Income-tax Act, Section 14(c), by which a person living in the Provinces, having an income in a State, is not liable to pay tax on amounts which he does not bring, or is not supposed to have brought, into provincial territories. This was a very thorny problem for some time, because the Government of India was threatened by States like Bikaner or Jaipur, that if incomes received within these States are taxed in the hands of the people in the provinces, they would start levying taxes on people belonging to the States and doing business in the Provinces. The result was this amendment.

During the War period, a notification under the Defence of India Rules was issued, whereby the Government of India undertook to enter into a contract with the factories functioning from these States in the territories of the adjoining Provinces. The result was that contracts which were entered into by the Government of India in an adjoining district in the Provinces brought to the Government of India taxes on income. This was resented by the States, since they felt that any articles produced in their territories and required by the Government of India should not be taxed in the form of income-tax by the latter. The position continued as such during War period, but factory owners in the States found an easy way out of this, by selling their articles to a third person at a nominal profit on which the Government of India could charge income-tax. For this purpose the contract was also entered into with the Government of India by that third party purchasing the factories in the States.

The question of the incomes of the Rulers of the States in the Provinces is rather a difficult one. The income of the Rulers, even though brought into the Provinces, is exempt from the operations of the Income-tax Act, whereas income derived from shares, property, etc., is taxable, even though they are individual in the real legal sense. The only exemption Rulers have been allowed is exemption from payment of income-tax on interest received by them on government securities. This they realise through the Reserve Bank of India, on a certificate of exemption issued by the Income-tax authorities under Section

18(3) of the Indian Income-tax Act. While the property of Rulers is taxable in the Provinces, although there is no clear distinction between the property of the Ruler and the property of the State, property pertaining to the Government of the State is not taxable in the Provinces, unless it falls within the purview of the existing legislation. Even then, in case they trade, or do business which is in the nature of trade, the States, under the provisions of this legislation, are exempt like in any British Dominions. This principle has been clarified in Section 155 of the Constitution Act, which reads: "Subject as hereinafter provided, the Government of a Province and the Ruler of a Federated State shall not be liable to federal taxation in respect of lands or buildings situate in British India or income accruing, arising, or received in British India."

The question of dividends from income derived in the Indian Provinces is still under consideration, and a case on behalf of the Baroda Government is, as we write, before the Bombay High Court. The States feel that dividends from shares of joint stock companies, being the property of the State, should not be subject to the operation of the Income-tax Act, as they do not correspond to business or trade, but a difficulty arises in view of the fact that dividends are charged at the source from the Company. The States, not being treated as individuals or corporate bodies in the Provinces, are not entitled to any refund. Under Section 49-B of the Income-tax Act, it is laid down: "Where a shareholder has received a dividend from a company which has paid income-tax imposed in British India or elsewhere, he shall be deemed, in respect of such dividend, himself to have paid the income-tax (exclusive of super-tax) paid by the company, of so much of the dividend as bears to the whole the same proportion as the amount of income-tax on which the company has paid such income-tax bears to the income of the company." Income-tax officers in the Provinces have, on claims raised by the States on this item, held that they do not come within the charging section of the Act to which refund relates and are therefore not entitled to claim refund. The States, however, feel that since the amount paid by the company is paid on their behalf, as provided in Section 49-B, the amount charged from the company in proportion to their income is wrongfully receive-

ed by the Government of India, and is liable to be paid back. The decision of the Baroda case in Bombay will have a very strong bearing on the question of payment of income-tax on shares by the States.

We have already dealt with the specific position of States in relation to the Crown, and we are here concerned only with the helpful suggestion of the Davidson Committee that, once the States enter the Union Centre, or Pakistan, they have an obligation to discharge towards ensuring the economic stability of the component units of the Union Centre. By implication—and here we enter upon as yet an uncharted domain—the financial stability of the States which enter the Union Centre must also be secured by the combined finances of Provinces and States, which are component parts thereof. How to secure the financial stability of States, which are not yet amenable to budget and audit scrutiny, is a question which has got to be remitted to the care of constitution-makers. Our purpose here is only to show the necessity for a uniform code of financial conduct on the part of Provinces, States, and the Union Centre, in order that the financial stability of the Union *as a whole* is guaranteed.

The Philadelphia Charter has said that “poverty anywhere is a danger to prosperity everywhere”, and, on the same showing, the financial instability in one of the units of the Union Centre, whether it be a Province or a State, is a danger to the ultimate security of the Union Centre. There can be no escape from the recognition of this salubrious principle of public finance, but we would not like to be understood to say that this is an argument for the continuance of the Niemeyer Award. The Award must be scrapped, and new common financial resources both for the States and Provinces in relation to the Union Centre must be created. In other words, Provincial Autonomy which was inaugurated in 1937 at the cost of the Centre, and specifically for the sake of preserving the financial integrity of the Provinces, cannot be the model for the formulation of the financial structure of the Union Centre. The time has long since arrived when the finances of the Union Centre must be placed upon a sound basis, and must have the assurance that in a knock-out fight between the component units on the one part

and the Union Centre on the other the latter will have priority and precedence given to it. In other words, the financial stability of the Union Centre must be recognised as constituting a greater guarantee for the financial stability of the country, than formulas of financial equilibrium for the component units thereof, whether they be Provinces or States.

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CHAPTER IV

CUSTOMS, EXCISES AND SALT

“ It may be said that it is an essential part of a Federal scheme that there shall be a uniform system of customs duties—uniform in the scales of charge on each commodity, in the method of collection, and in subordination to the Federal Authority—and that it would make for efficiency, if not necessarily for economy, if all customs staff were concentrated under one administration; and that, if the revenue realised from such a uniform system of customs duties is to be allotted wholly to Federal needs, it is reasonable that against the value of duties levied at their ports and hitherto retained by the States, there should be set off the value of the general benefit which would accrue to the States from Federation, including the right to a voice in the determination of the Federal policy.”

—Davidson Committee Report, Paragraph 241.

“STRUCTURE OF CUSTOMS REVENUE—CONSIDERATIONS RELATING TO STATES—TRAVANCORE AND COCHIN PORT—HYDERABAD’S CUSTOMS POSITION—KATHIAWAR MARITIME STATES—CUSTOMS ALWAYS A CENTRAL HEAD—LAND CUSTOMS—CENTRAL EXCISES—SALT TAX.

In spite of the fact that customs, as a head of central revenue, might, as we have pointed out in the preceding Chapter, decline in importance, there cannot be any question of its usefulness to the Union Centre in the coming years. Sea customs and the significance of the ramifications thereof to several maritime States; and land customs, which gave the States some Rs. 4½ crores a year in 1930 according to the Butler Committee, become easily distinguishable, and must be dealt with separately. For our immediate purposes, it must be stated that neither the maritime States, nor the land-locked States, can be permitted to pursue independent policies in respect of sea and land customs, whether they come into the Union or not. We will argue the case at considerable length in the following pages, but we would establish the preliminary issue here, that the economy of the Union is integral in character; that the States must conform to this unified whole; and that adjustments, both economic and financial, are capable of being arrived at, as they were repeatedly arrived at during the past one hundred years between the Paramount Power and the States, in order that the economic and financial structure of the Union does not become imperilled, as a result of isolationist and contradictory policies pursued by

each one of the heterogeneous mass of States which dots the political map of India.

STRUCTURE OF CUSTOMS REVENUE

The following figures are detached from the key table, which is incorporated in the preceding Chapter, indicating the relative importance, on the existing basis, of taxes on income, customs and excises to the Central revenues.

Customs revenue of Central Government
(In lakhs of rupees)

Year	Collection.	% of total revenue.	Year	Collection.	% of total revenue.
1920-21	31.90	23.6	1921-22	34.41	53.1
1922-23	41.35	57.2	1923-24	39.70	51.9
1924-25	45.75	60.9	1925-26	47.78	31.4
1926-27	47.38	48.9	1927-28	48.21	63.3
1928-29	49.28	62.3	1929-30	51.28	63.4
1930-31	46.81	60.4	1931-32	46.44	60.4
1932-33	51.95	64.0	1933-34	47.16	61.6
1934-35	52.67	65.1	1935-36	54.11	65.8
1936-37	53.58	66.9	1937-38	43.11	57.3
1938-39	40.51	54.4	1939-40	45.88	56.4
1940-41	37.30	48.9	1941-42	37.89	39.4
1942-43	25.12	12.0	1943-44	26.57	15.5
1944-45	39.77	15.9	1945-46	73.61	26.0
1946-47 (R.E.) ..	87.50	32.3	1947-48 (B.E.) ..	93.00	33.8

The following tables illustrate the territorial distribution of customs revenue,—a point of considerable importance to the country, now that she is being divided into the Indian Union and Pakistan, to which the Indian States must, either today or eventually, become affiliated in customs *regimes*.

Import duties collected at Principal Ports
(In thousands of rupees)

Year	Bombay.	Calcutta.	Madras.	Karachi.	Chittagong.	Madras outports.	Bombay outports.
1936-37 ...	15,24.93	9,76.30	2,90.69	4,52.47	15.37	93.68	1,10
1937-38 ...	17,51.33	12,22.13	4,24.18	5,09.59	29.53	2,10.11 (a)	68
1938-39 ...	15,54.68	12,08.03	3,94.86	5,50.78	38.51	2,14.14	64
1939-40 ...	18,71.70	14,11.46	3,94.15	5,78.95	35.92	2,53.45	71
1940-41 ...	15,56.23	11,44.00	3,57.90	4,35.49	27.67	2,06.29	64

(a) Includes Rs. 10,187 duty on Burma petroleum etc.

Export duties collected at Principal Ports

(In thousands of rupees)

Year	Bombay.	Calcutta.	Madras.	Karachi.	Chittagong.	Madras out-ports.	Bombay out-ports.	Karachi out-ports.
1936-37	86	4,27,54	1	1,28	7,38	3,45	24	5
1937-38	93	4,30,47	..	1,30	7,06	3,59	24	8
1938-39	98	3,96,00	..	1,82	7,07	3,98	16	12
1939-40	1,17	3,92,00	..	2,00	6,73	4,37	14	..
1940-41	(a) 2,05	(b) 3,10,27	..	2,92	4,08	5,26	7	..

(a) The totals exclude the following figures (in thousands) for agricultural produce cess, namely—Bombay—3,04; Calcutta—(Nil); Madras—1,20; Karachi—2,34; Chittagong—(nil); Madras Outports—2,85; Bombay Outports—51; and Karachi Outports—(Nil).

(b) Includes Rs. 4,000 from Government Stores.

Export duties on Rice and Jute

(In thousands of rupees)

Article.	Year.	Bombay.	Calcutta.	Madras	Karachi	Chittagong.	Madras out-ports.	Karachi out-ports.	Bombay out-ports.
Rice	1936-37	69	3,67	..	1,22	.....	3,35	5	24
..	1937-38	75	4,83	.....	1,24	.....	3,51	8	24
..	1938-39	82	4,66	.....	1,75	.....	3,88	12	16
..	1939-40	65	4,83	.....	1,93	.....	4,02	..	14
..	1940-41	90	3,90	2	2,86	.....	4,73	..	7
Jute	1936-37	17	1,23,87	1	6	7,38	10	..	..
..	1937-38	18	1,25,64	..	6	7,06	8	..	..
..	1938-39	16	3,91,43	..	7	7,06	10	..	..
..	1939-40	52	3,87,17	.....	7	6,73	35	..	..
..	1940-41	1,11	3,06,37	.....	6	4,08	53	..	..

Note:—Export duty on hides and skins was not collected between the years 1936-37 and 1940-41.

CONSIDERATIONS RELATING TO STATES

Attempts have been made in the past to estimate the relative importance of the Provinces and the States in the trade and commerce of the country. We have not before us any up-to-date estimate, but the following table from the Nind Committee Report of 1930 will be illustrative of the broad proportions of the import duties available to the Provinces and the States.

Estimated Shares of States in import duties

	Percentages	Thousands of rupees.
Articles of general or universal consumption	20	1,66,74
Articles intermediate between A Class towns and universal	17.75	11,44,57
Articles mainly consumed in towns of 10,000 and over	15.5	66,87

Estimated Shares of States in Import Duties—(Contd.)

	Percentage	Thousands of rupees.
Articles intermediate between A and B class towns ..	15	7,45
Articles consumed in towns of 20,000 and over (Class B)	14.5	81,38
Articles classes as factory (general items)	9	6,26
Articles intermediate between A class town and factory	12,25	44,56
Factory Special :—		
(a) Printing Presses	6	3
(b) Tobacco factories	25	25,99
(c) Cotton weaving	17	9,06
(d) Silk weaving	11.5	3,48
(e) Rope works .. .. .	.....	.....
(f) Mines and quarries	54	1,54
Railway materials	30	10,20
Articles intermediate between railway materials and factory stores	19.5	12
Liquors	10	20,72
Steamers & launches .. .. .	.....	.....
Total Import Duty ..		5,88,97

Note : (a) :—To this gross total figure, export duties of the value of Rs. 9,98,000 must be added, which brings the grand total of the estimated share of the States in customs revenues to Rs. 5,98,95,000.

Note : (b) :—The net imports of silver into India in 1928-29 amounted to 63,673,037 ounces. On the basis of the duty of 4 annas an ounce prevailing in 1930-31, the customs revenue from this source would have amounted to Rs. 1,59,18,000 and the States' share would have been Rs. 31,84,000 approximately.

An examination of the relative importance of the resources of the Provinces and the States becomes very illuminating at this stage of our inquiry. We have, with considerable difficulty, been able to obtain statistics relating to the trade originating in the broad groups of the States, in their relation to the totals of all-India trade according to commodities. The following rather complicated and long table illustrates the position in a representative fashion, though it is clear that not all the States could be brought into the picture, and that the sum total of the impression relating to these proportions is at best illustrative.

(In maunds.)

Extent of Trade Originating in States—(1943-44.)

Article.	Rajputana States.	Central India States.	Nizam's Dominions.	Mysore.	Kashmir.	Total India.
Animals :						
Cattle (excluding sheep and goats)	9,624	9,849	4,274	467	....	2,98,774
Horses, ponies and mules	481	265	1,364	375	5	29,915
Sheep and goats	6,91,485	94,459	68,215	37,622	66	17,79,097
Others	1,144	992	3,654	8,347	100	8,34,480
Bones	32,995	4,489	59,928	26,541	1,806	14,47,169
Cement	42,07,184	7,78,623	22,98,835	4,736	....	2,22,91,114
Coal and Coke	12,287	78,92,257	1,32,29,071	12,254	....	44,07,59,286
Coffee	....	22	81	40,110	....	2,55,765
Cotton Twist and Yarn :						
Foreign	....	19	....	....	....	4,275
Indian	58,967	68,098	14,026	1,37,301	117	43,21,597
Cotton Piecegoods :						
Foreign, in bales	438	29	3	4	....	22,055
Foreign, in boxes	1,24,646	6,46,758	71,689	80,490	2,498	1,09,60,352
Indian, in bales	602	1,712	156	299	....	71,896
Indian, in boxes	62	1,50,882	35	41,060	28	11,17,443
Myrobalans	2,761	30,696	24,022	6,23,968	8,957	98,56,021
Fruits, Dried	2,467	5,425	11,407	13,102	39	8,18,156
Glass						
Grain, Pulses and Flour :						
Gram	5,58,909	3,71,004	6,01,518	5,015	....	1,31,25,133
Jowar and Bajra	2,48,677	2,73,981	10,57,626	30,690	....	97,22,481
Rice in the husk	3	2,013	....	93	....	34,28,058
Rice not in the husk	1,062	1,18,281	10,719	2,843	19,115	3,06,14,908
Wheat	11,135	1,12,551	3,181	5,548	....	2,49,79,290
Wheat flour	2,468	10,974	539	4,295	56	58,94,133
Other sorts	11,29,563	10,23,854	7,01,428	19,798	4,875	1,96,41,649
Hemp, Indian and Other Fibres (excluding jute)	4,759	7,720	8,769	974	8	11,03,189
Hides, Raw	1,861	10,363	5,641	33,502	847	20,33,817

CUSTOMS, EXCISES AND SALT

Skins, Raw	42,798	11,498	17,946	1,12,203	• 1,946	10,62,955
Hides & Skins, Tanned & Leather	3,568	259	45,194	68,553	17	8,96,850
Jute Raw :						
Loose	12	....	7	5	6	1,41,52,854
Pucca Bales .. .. .	....	109	16	....	....	24,36,837
Gunny Bags and Cloth	40,979	17,293	9,178	35,922	436	84,56,039
Iron and Steel Bar Sheets, Girders and other Commercial forms of Iron and Steel	70,435	29,536	38,449	2,80,159	601	2,88,13,000
Lac and Shellac	1,470	16,850	86	63	1	4,58,962
Manganese Ore .. .. .	....	....	....	319	....	1,34,69,537
Oilcakes	95,979	52,611	10,94,265	50,483	1,639	72,53,463
Oils :						
Kerosene	2,719	11,017	713	1,264	....	86,88,434
Vegetable Coconut	69	1,638	5,598	9,580	....	13,44,345
Groundnut	3,116	1,756	6,77,697	54,708	....	36,58,009
Other Vegetable Oils	45,672	66,117	80,210	23,705	17	27,51,799
Oilseeds :						
Castor	13,789	9,185	5,22,980	3,341	....	10,17,630
Cotton	81,839	2,90,711	7,43,612	23,683	306	64,46,245
Groundnuts	35,405	49,665	50,55,821	3,06,779	3	1,34,28,511
Linseed	3,723	1,90,318	2,48,923	3	....	16,93,455
Rape and Mustard	10,60,403	1,39,321	14,678	16,754	311	63,70,996
Till or Jinji	1,42,868	58,234	77,259	2,07,513	12	15,24,593
Ghee	35,115	18,095	371	2,706	4	4,40,398
Rubber, Raw .. .. .	....	....	53	78	....	2,67,803
Salt	1,03,41,471	13,676	7,472	709	....	3,45,11,066
Sugar	2,596	7,635	1,574	88,581	82	1,70,78,509
Gur, Rab, Molasses, Jaggery, Etc.	37,115	52,497	4,993	1,353	....	1,29,35,448
Tea	57	1,855	985	11,671	466	59,53,906
Tobacco, Raw	2,333	19,922	1,727	66,634	175	26,01,735
Wood and Timber :						
Teak	2,785	13,328	12,245	7,964	....	5,69,569
Other Timber	40,097	2,27,077	25,863	96,293	53,937	1,52,08,556
Wool, Raw	1,24,430	5,019	33,681	939	484	9,14,430

In view of the difficulty relating to lack of statistics for all the States, and our consequent inability to delimit the percentage importance of trade originating in all the States to India as a whole, including potential Pakistan areas, we have to abandon the attempt to work out percentages for the more recent years. But we are able to record below at least one attempt made in this country, viz., by the Nind Committee in 1930, to arrive at these percentages. We are convinced that the Nind Committee's work was based on approximations, and that, consequently, there is no accuracy vouched for the estimates of percentages given in their report. Still, we feel that the following table, which is built up from that Committee's *Report*, will be extremely important to any discussion dealing with the relative proportion of the economies of the Provinces and the States, to the totality of resources which must ultimately belong to the Indian Union and Pakistan.

**Percentage of Export Trade Originating in States to total
Indian Trade (1930)**

Raw cotton	41.0	Manganese Ore	22.0
Cotton Seed	41.0	Pig Iron, steel .. .. .	.....
Tea	7.6	Ingots & finished steel ..	12.7
Groundnuts	8.2	Oil Cakes	22.0
Linsced	7.7	Leather	12.0
Rice	3.4	Lac	11.0
Wheat	18.8	Cow hides	18.0
Jute raw	0.8	Buffalo hides	18.0
Yarn	13.0	Sheep and goats	26.0
Wool and woollens	9.4		

(average of looms and spindles)

The question naturally arises as to what the proportions are of the total import and export trades of the States to the totals of India? We must confess our inability to obtain relative and comparable statistics, in order to draw more or less valid conclusions regarding the pattern of export and import trades of the Provinces and the States, for purposes of eventual merger into the polity of the Indian Union, on a basis which is uniform in its incidence in the fiscal sphere. But we consider that the same percentage importance becomes operative in the sphere of consumption goods, as is prevalent in the case of exports. We confess that this approach to the problem is no more valuable than a rough yardstick, but it is clear that even this

rough measurement of the economic importance of the States to the Union Centre of tomorrow is not without its merits.

The time is fast approaching when the entire economic system of India becomes integral in character, in the process smashing down barriers to trade and commerce which have existed, at any rate with respect to the States, under the protecting wing of the Paramount Power. It is clear to us that India cannot hope to progress with a fiscal system enveloping sea and land customs (in the latter category including the unequal duties prevailing in the States, be they transit duties, octroi or *chungi*) as the one which prevailed in Europe in the inter-war period. The late M. Briand sought, though without result, to bring about a European Union from out of the congeries of national states, until Hitler wiped them out of existence, and, if we do not misread the situation, the application of the "Truman Doctrine", under which billions of dollars of credits are being poured into the countries of Europe, would, if it could succeed at all, bring about a uniform economic system in which a uniform customs *regime* becomes the principal ingredient. We venture to hope that a unified customs *regime*, which is more impressive and more generous to all the parties concerned, than has been available so far under British rule, is possible for this country, even after Pakistan establishes its temporary and unstable existence, and this is an ideal which every one in this country will endeavour to bring into existence after the present political madness passes.

TRAVANCORE AND COCHIN PORT

We have arrived at a stage in our inquiry where we can take up examination of customs as an item of revenue to the States. Today, on the eve of Indian independence and the division of the country into two sovereign entities, with the option for States to adhere to the one or the other, note must be taken of the existence, for longer or shorter periods, of sea customs rights on the part of the States, especially the maritime States, which are about a dozen in number, and in regard to land customs *e.g.*, in the case of a State like Kashmir. Time and again, attempts had been made by the Paramount Power to negotiate, with the maritime States in particular, settlements which were

intended to bring about a reasonable amount of unity of incidence of taxes, prevention of tax evasion and the preservation of a general customs *regime*, in which the people inhabiting various areas in this country enjoyed common benefits. Most of these negotiations have so far failed to produce an equitable pattern, which is capable of investing a possible Union Centre with powers on an overall basis.

Travancore, which has four important ports, viz., Colachal, Trivandrum, Quilon and Alleppey, is certainly not a maritime State involving any appreciable difficulty to the customs *regime* of the Indian Union, by virtue of the fact that these four ports are hardly modern in character. The Port of Cochin, however, belongs to category by itself, among *all* the ports of the maritime States in India today. At the moment it is worked on a basis involving financial contributions from the Government of Madras, the Government of Cochin and the Government of Travancore.

The following tables illustrate the importance of the overseas import and export trade of Travancore.

Travancores' Foreign Imports

(Values in rupees)

	1941-42	1942-43	1943-44
Total British Empire	47,26,115	10,87,548	9,88,221
Total Foreign countries	22,37,418	56,111	.....
Total Imports ..	69,63,533	11,43,659	9,88,221

Travancore's Foreign Exports

(Values in rupees)

	1941-42	1942-43	1943-44
Total British Empire	26,18,269	6,39,431	49,325
Total Foreign countries	5,53,401	26,665	16,573
Total Exports ..	31,71,670	6,66,096	65,898

Twice within the past sixty years, conventions were drawn up for the administration of the Port of Cochin, viz., the Inter-Portal Convention of 1865 and the Port Agreement of 1925. The Inter-Portal Convention is still operative in its main clauses,

as modified by the Agreement of 1925, and enormous sums have been sunk by the tax-payers of the Provinces towards the modernization and equipment of this emporium to the south-west of this country. When the Davidson Committee enquired into this question in 1932, it was found that out of the capital expenditure of Rs. 83.5 lakhs, as much as Rs. 36.95 lakhs was loaned by the Government of Madras, on which the Port pays both interest and sinking fund charges. The Davidson Committee reported that the port of Cochin "is of great present value, and must in the future be of even greater value to an Indian Federation, in whose undivided possession, unhampered by any obligations to third parties, it clearly ought to be." We hold that this enunciation of principle by the Davidson Committee is capable of being extended to every other port belonging to any maritime State in the country.

The question very naturally arises as to what Travancore proposes to do with her customs. Will the State have her own tariff system and, if so, how does it propose to delimit her dealings with the Indian Union? Cochin has joined the Constituent Assembly of the Union, and is likely to adhere to the Indian Union, with the result that her interest in the Port is secured on a par with the Province of Madras and the Union Government. If Travancore stays out as an independent entity, its government cannot expect even to obtain the status of Gdynia, in relation to Danzig of the inter-war period, for the Cochin port. Here is a straight problem for Travancore which, on declaring independence, becomes foreign territory, with all the incidents in the sphere of passports, customs regulations etc., attached to it.

HYDERABAD'S CUSTOMS POSITION

The case of Hyderabad must be examined here in some detail. Under the commercial Treaty of 1860, between the East India Company on the one part and the Nizam's Government on the other, certain understandings were arrived at with respect to the so-called "claims" of the Nizam to access to the sea. The East India Company agreed under this Treaty to grant the Nizam "the free use of the sea-port of Masulipatam", with the right to establish a commercial factory and agents at that

place, "under such regulations as the nature (*sic.*) of the Company's Government shall require, and as shall be adjusted between the Governor-General-in-Council and His Highness." Protection was given to the ships flying the flag of the Nizam by all the men-of-war belonging to the East India Company, and similar protection was granted to the Nizam's ships whenever they entered the ports belonging to "the British Government in India". Article 3 of the Treaty provides: "There shall be free transit between the territories of the contracting parties of all articles being the growth, produce or manufacture of each respectively", and "also of all articles of growth, produce or manufacture of any part of his Britannic Majesty's Dominions".

Further, under the Treaty, the right to collect transit (*rahdari*) duties by intermediary agents of both parties or trade relating to the territories of Hyderabad was abolished, and thus freedom of movement of merchandise was guaranteed. Under article 5, a customs duty of not more than 5 per cent "shall be levied at Hyderabad indiscriminately on all articles of merchandise imported into" the Nizam's territories. It is also provided that no article shall pay duty more than once, *ad valorem* on their declared values as mentioned in invoices. Further, it is provided that "the said duties shall be fixed and immutable, except by the mutual consent of the contracting parties." Reciprocity was provided for on the part of the East India Company in this regard.

Duties on goods exported from the Nizam's territories to those of the Company shall be collected at Masulipatam, or at such other centres as were agreed to by the contracting powers, at not more than 5 per cent, to be collected at Hyderabad on "the prime cost of all the commodities purchased" in the Nizam's territories, and this provision is the only mention of a permissible export duty which can be levied by the Government of the Nizam. Export of grain from the Nizam's territories to the Company's territories was to be under licence. Under exceptional circumstances free transit of grain may be arranged by mutual agreement "into the respective territories of the two contracting powers in Hindoostan and Deccan." Article 10 of

the Treaty provides that nationals of foreign powers are excluded from the benefits of the provisions of the Treaty.

A supplementary treaty between Queen Victoria and the Nizam in 1860 provided as follows: "The navigation of the River Godavari and its tributaries, so far as they form the boundaries between the two States, shall be free, and no customs duty or other cess shall be levied by either on goods passing up or down the aforesaid River". In 1875 a partial revision of Article 3 of the Treaty of 1802 was arrived at under which the Nizam's Government agreed to prohibit the export of salt to British territory "in temporary contravention [of] and to amend the Treaty of 1802, even though at that time no salt was being exported owing to its limited production". Under the Opium Agreement between Queen Victoria and the Nizam, in 1883, the Opium Agent to the Government at Indore "shall issue passes for the transport of opium to Indore", and "shall levy on same on behalf of His Highness' Government pass duty at the rate which may, from time to time, be fixed by the British Government," remitting the same through the Resident at Hyderabad. The two Railway Agreements between Queen Victoria and the Nizam of 1883 and 1897 provide that the materials required for the construction of the new railway lines in the Nizam's dominions shall be "free of all customs charges or other imposts".

This is the basic treaty position subsisting between the Paramount Power and the Nizam, and it is on this foundation that the claim was put forward by the Nizam for a corridor to the seaboard of the Bay of Bengal. According to the Davidson Committee, the Nizam's Government claimed, on the basis of the above treaties, the following rights (paragraphs 361-365):

(1) The right to a free corridor to the sea at Masulipatam, and permission to participation in the development of the port so as to enable Hyderabad to make use of it "under the conditions that would obtain in the India of the future." The Nizam's Government urged that this consideration renders it very necessary that "Hyderabad should own and control a railway of its own form its border to Masulipatam."

(2) The right to import, free from all British Indian customs, through any port, or overland, all articles which are

the growth, produce or manufacture of any part of the British Dominions, together with a corresponding right to export, free of duty, all articles of Hyderabad origin.

(3) The rights *inter se* of Hyderabad and the Paramount Power should be ascertained.

On these extravagant claims of the Nizam, in so far as the supposed right to Masulipatam was concerned, the Davidson Committee expressed no opinion as to the meaning of the words "free use". The second claim was rejected, according to the Davidson Committee, by the Government of India in 1873. As regards the Nizam's claim for having "the respective rights of the contracting parties being ascertained", the Davidson Committee wrote that, during the course of the discussions at Hyderabad, the Nizam's Government made them understand that they "would not necessarily insist upon exercising the right in question."

We have dwelt upon this claim of the Nizam at this length, because we are convinced that all known indices of the Nizam's views lead to the impending formation of a Sovereign State, cutting up India, at any rate the Indian Union, into two distinct portions of territory. The treaties we have analysed above are clear on one point, namely that there is no basis for the Nizam to claim territory and dominion in the areas separating the relevant districts in his State from Masulipatam. By all means, let the flag of Nizam's Government fly on all ships entering the port of Masulipatam, and the Indian Union will not object to the exercise of that right. By all means, again, let the ships of the Nizam ply up and down the River Godavari without paying any transit duties. We are certain that if the Nizam wants to sink money into the Port of Masulipatam for its development, and desires to establish a "Factory" there, there would be no objection raised at all on the part of the Union Centre. But, because his great-great-grandfather had put his thumb impression to a document prepared by the East India Company, without obviously knowing the consequences thereof, it cannot be held today that the Nizam's "claim", to sovereignty over the Andhra areas should be reopened.

Whatever might happen to any of the States in India, with respect to their adhesion to the Constituent Assembly of the

Union Centre and the Constituent Assembly of Pakistan, one thing is clear, that not an inch of territory would be retroceded to the Princes. It is time that this question is put beyond any shadow of doubt, for otherwise Patiala would claim Simla, Kashmir would claim Murree, Gwalior would claim Jhansi and Agra, Baroda would claim Ahmedabad, and so on. There cannot be any question that such a fantastic proposition can ever be allowed even to be debated in public, even if the consequences thereof are that the Princes would decide not to give up their rule of medieval despotism, by rejecting unionisation with the Provinces, and would even prepare to meet certain economic and political death arising out of their present isolation.

KATHIAWAR MARITIME STATES

We have now to enquire, rather elaborately, into the question of the customs revenue of Kathiawar States, for we recognise that an immediate decision has got to be taken on the future of the Viramgam Customs Cordon. For nearly half a century, the Viramgam Customs Cordon had been the bone of contention between the Government of India and the Government of Bombay on the one part, and the heterogeneous mass of Kathiawar and Cutch States on the other. Decisions have been made and reversed times out of number during the present century, in order that a satisfactory settlement, which is equitable both to the Provinces and the States concerned is reached, but the country is still as farthest removed from such a settlement as it was when the customs Cordon was introduced for the first time at Viramgam at the beginning of the twentieth century.

The place of Kathiawar ports in the export and import trades of India is considerable. The following tables illustrate this point clearly:

Imports into Kathiawar Ports		(Value in rupees)		
		1941-42	1942-43	1943-44
Total British Empire		86,79,005	58,53,610	28,29,490
Total Foreign Countries		98,13,695	65,86,433	92,11,851
Grand Total		1,84,92,700	1,24,40,043	1,20,41,341
Share of Baroda		70,61,104	74,72,426	83,48,157
„ Bhavnagar		16,60,635	29,626	....
„ Jafarabad		1,126	....	....
„ Junagadh		25,88,648	52,589	73,628
„ Morvi		24,99,705	28,80,604	80,19,850
„ Nawanagar		19,98,502	13,73,080	1,88,361
„ Porbandar		26,87,980	6,31,718	4,11,350

Exports from Kathiawar Ports
(Value in rupees)

	1941-42	1942-43	1943-44
Total British Empire	64,79,909	41,61,064	1,76,33,729
Total Foreign Countries	25,05,058	52,52,193	1,45,15,455
Grand Total	89,84,967	94,13,257	3,21,49,184
Share of Baroda	40,66,019	34,51,207	17,71,865
„ Bhavnagar	2,53,790	3,36,142	6,66,851
„ Junagadh	12,48,028	19,93,365	21,65,547
„ Morvi	19,73,111	36,529	40,67,270
„ Nawanagar	6,82,475	28,27,709	1,82,08,008
„ Porbandar	7,61,544	7,68,305	52,69,643

Imports of Silver Bullion and coin into Kathiawar Ports
(Value in rupees)

	1941-42	1942-43	1943-44
Total Private*	12,47,044	14,36,445	....
Total Currency Notes .. .. .	....	....	....
Grand Total	12,47,044	14,36,445	....
Share of Baroda .. .. .	....	....	....
„ Bhavnagar .. .. .	....	....	....
„ Jafarabad .. .. .	....	....	....
„ Junagadh .. .. .	....	....	....
„ Morvi	4,28,280	14,36,445	....
„ Nawanagar .. .. .	....	....	....
„ Porbandar	8,18,764	....	....

This is the place for an examination of the routes and value of goods passing through the Viramgam Customs Cordon into the territories of the Provinces. The following table illustrates the value of the total local manufactures, produce and re-exported trade across the land customs line:

*The total imports of silver bullion and coin from foreign countries on private account include the imports from United States of America to the tune of Rs. 3,57,619.

There are *no exports* from the Kathiawar States in the matter of silver bullion and coin.

It is very interesting to note here that in June 1947 the Government of India banned movements of gold across the Kathiawar ports.

(Value in rupees)

	1941-42	1942-43	1943-44
Via Viramgam	4,20,08,052	6,23,65,630	9,74,11,589
„ Dhandhuka	1,05,01,842	2,85,28,227	2,63,46,422
Total ..	5,25,04,894	9,08,93,857	12,37,58,011

The following table illustrates the value of foreign goods (duty-free or dutiable, passed with or without concession) across the Viramgam Customs Cordon, and the respective proportions thereof of individual States of Kathiawar and Cutch.

(Value in rupees)

	1941-42	1942-43	1943-44
Via Viramgam	74,77,447	97,46,987	2,63,78,476
„ Dhandhuka	4,47,153	3,50,952	3,75,724
Total ..	79,24,600	1,00,97,939	2,67,54,200
From Bhavnagar	1,03,240	2,79,446	13,07,726
„ Baroda	33,96,819	48,48,795	91,71,353
„ Jafarabad .. .. .	.....	.....	.....
„ Junagadh	26,307	62,744	13,754
„ Morvi	18,65,445	21,36,322	6,07,058
„ Nawanagar	13,50,531	11,82,127	37,548
„ Porbandar	2,04,452	6,08,420	21,891
„ Miscellaneous Places ..	3,87,897	9,80,085	1,55,04,870

The Viramgam Customs Cordon was introduced in 1905 and remained in force till 1917, when it was abolished. It was again reimposed in 1927, and in 1944, owing to the promulgation of the Export Trade Control policy of the Government of India arising out of war conditions, the Cordon was further tightened. It is generally believed that the Political Department, now under liquidation, holds the view that the abolition of the Cordon would be welcomed by all the parties concerned, because it is a bother which cannot be tolerated on either side. Now that the salt tax has been abolished, the importance of the Viramgam Customs Cordon has been greatly subtracted from, and the whole question must be examined *de novo* to suit the requirements of the Union Centre under conditions arising out of the abolition of Paramountcy.

The Viramgam Line originated as a result of the system of salt revenue introduced in the Provinces, and was originally intended to prevent duty-free salt from the States entering the territories of the Provinces. At a later stage, the Line became a regular Customs Line, because in the wake of the abolition of free trade in India in 1895, the Government of India were compelled to take notice of menacing competition from Kathiawar Ports. The Customs Cordon runs from the Rann of Cutch to the Gulf of Cambay, with customs stations all along the Line, enforcing Indian rates on all goods crossing from States' territories into those of the Provinces. This had naturally meant opposition from the States, which felt aggrieved at the fact that the profitable trade they had enjoyed till then had been deprived, and that the imposition of the Indian Customs Regulations had meant considerable inconvenience and additional work to the *durbars* concerned.

During the First World War, as much as during the Second World War, this customs controversy between the States and the Government of India receded into the background, in as much as war-time regulations were of the steam-roller variety which did not brook opposition from any quarter. In the inter-war period, however, diversion of trade, particularly in matches and sugar from Bombay to the Kathiawar Ports, enabled goods to enter the States' territories duty-free and re-enter the markets of Provinces at lower prices, with which duty-paid goods could not compete, and brought this question to a head. As a matter of fact, the diversion of Bombay trade to Kathiawar and Cutch Ports, which commenced direct trading with Goa, Colombo and Aden, had become such a menace to Central revenues, that the Government of India were obliged to take up the question in earnest. Additionally, the improvement of port facilities at Okha in Baroda State, and Bedi Bunder in Nawanagar State in particular, with direct shipping routes established from them to Javanese and European Ports, brought about a crisis in the relations of the Government of India with the maritime States.*

* The following notification was issued in the daily papers by the Director of Commerce, Baroda State, on May 18, 1947: "Direct steamer service from United Kingdom Ports to Okha, which was discontinued during the war, has now been re-established. One direct steamer is

The proposals of the Government of India, at the Mount Abu Conference in 1924, to the Rulers of maritime States in the Western India States Agency, were as follows. As an alternative to the reimposition of land customs line, the States should agree to an arrangement, under which the customs administration of the ports that remained open to foreign traffic, whether direct or by transshipment, should be handed over to the customs officers appointed by and responsible to the Government of India, who would collect customs duties involved. The proceeds of such collection would be credited to Central revenues, from out of which each State concerned would receive an assignment. The remaining ports in this area should remain closed to foreign traffic. Under this assignment proposition, the States concerned would have obtained according to the Davidson Committee (paragraph 304) the following allotments:

	Rs.
Baroda	20 lakhs
Junagadh	12 lakhs
Mangrol	2 lakhs
Nawanagar	34 lakhs
Probandar	10 lakhs
Morvi	6 lakhs
	Rs. .. 84 lakhs

However, the Conference was infructuous, because it did not produce any agreement between the Government of India on the one part and the Kathiawar and Cutch States on the other, or, for that matter, between Kathiawar and Cutch States *inter se*.

In 1927, the Government of India were compelled to enforce their customs *regime* at Viramgam, of which the following were the three principal features:

expected at Port Okha every month from U. K. ports. *Unique facility for prospective importers.* Northern India and North Gujarat can be served most economically from Okha. Reference for concessions and other facilities should be made to C. V. Bhatt, Director of Commerce, Baroda State, Baroda." (Italics in the original).

We do not know what the concessions and facilities referred to are, but it is clear that this advertisement, which is culled from the *Hindustan Times* of New Delhi, is eloquent testimony to the rather blatant manner in which some of the maritime States are attracting custom from the ports of the Provinces. We believe that no one disputes the claim of the Government of India that revenue losses, through unfair practices on the part of the maritime States, have taken place, and these will continue to take place, unless the Centre protects its legitimate interests.

- (1) The export tariff was not extended to the land customs frontier;
- (2) All goods produced in Kathiawar were passed free of duty across the land frontier; and
- (3) *Bona fide* passengers were permitted to import, duty free, personal and household effects and merchandise, on which the total duty was not more than Rs. 10.'

During the subsequent ten years, intransigence on the part of the Kathiawar and Cutch States led to further discussions, and in 1936 a fresh *regime* was imposed. Under this, these maritime States were bound to levy customs at Indian rates, and undertook to enforce the Indian Customs regulations. In return for this, they were permitted to send across the Line specified quantities of goods, duty free, on certificate. On their part, the Government of India withdrew their control. The Viramgam Customs Line, however, became celebrated as the bottle-neck through which smugglers, profiteers and black-marketeers from the States trading in the Provinces had to pass through, even though there was an assurance that traffic in goods of pure Kathiawar and Cutch origin was not interfered with.

In September 1944, the Government of India issued fresh regulations for the examination of passengers' goods at Viramgam stations, each compartment being examined at one time. There was an uproar against the tightening of the customs Cordon, which was necessitated, as far as the Government of India were concerned, by war-time export and import regulations, as much as the well-established fact that the States *did* benefit from and actually encouraged smuggling and duty evasion. It was also proved that some States did a roaring trade, *e.g.*, with Near-Eastern countries, illicitly, and that there was a famine of consumer goods. It was, however, realised that the maintenances of the customs Cordon at Viramgam was a nuisance to both the States and the Provinces. It was also realised that, while there was a flight of commodities and goods, *e.g.*, silver from the Provinces to the Kathiawar and Cutch States, the maintenance of the customs Cordon was not justified by the actual amount of smuggling detected. On the other hand, corruption on the part of customs and police staff maintained for the Cordon had reached such heights that it was recognised that

the sooner it was abolished, and a uniform system of customs enforced, the better it would be for the country as a whole.

On the basis of the 1930-31 figures, the following table, constructed by the Davidson Committee (paragraph 338) is very interesting. The table below gives a summary of the figures (1930-31) for those States which are subject to the orders arising out of the re-establishment of the Viramgam Line:—

(In lakhs of rupees)

	Value of Foreign Imports.	Value of Exports.	Customs duties on Imports.	Amount retained by States.
Janjira (Jafarabad)	6.25	7.03	0.45	0.45
Junagadh	28.92	16.39	13.71	13.71
Mangrol .. .. .	..	..	1.18	1.18
Okha (Baroda)	60.25	12.12	14.65	3.80
Porbandar	78.61	48.42	5.06	5.06
Nawanagar	2,41.70	71.30	1,55.80	44.00
Morvi	43.24	13.03	4.63	4.63

The following table shows the amount of customs duties that would be retained by the maritime States, on the basis of 1930-31 figures, under each of the three alternatives:—

(In lakhs of rupees)

	Maintenance of Viramgam Line as then existing.	Abolition of Viramgam Line.	Establishment of Customs barrier between maritime and inland States.
Bhavnagar	51.05	51.05	51.05
Janjira (Jafarabad)	0.45	0.45	0.37
Junagadh	13.71	13.71	16.71
Mangrol	1.18	1.18	0.75
Porbandar	5.06	5.06	3.55
Okha (Baroda)	3.80	14.65	5.89
Nawanagar	44.00	1,55.80	12.57
Morvi	4.63	4.63	3.46
	1,23.88	2,46.53	93.85

It was estimated that the whole customs revenue of Kathiawar ports, including Nawanagar, in 1930-31 was

Rs. 246.53 lakhs, out of which 122.65 lakhs were recovered for Central revenues, the balance being the share of the States concerned. Of the States' share of Rs. 123.88 lakhs, forty-one per cent represented the share of Bhavnagar, and thirty-six per cent that of Nawanagar. It will be seen that only these two States of Bhavnagar and Nawanagar are more vitally involved in the Viramgam Customs Cordon, than any of the heterogeneous mass of principalities in the Western India States Agency.

We have been fortunate in obtaining figures relating to Kathiawar customs for the years 1941-42 to 1943-44. The following table shows the amount of customs duty on goods imported, the amount of duty foregone and the amount of duty demanded or recovered from the Kathiawar States, on the basis of the Viramgam Customs Cordon.

(Value in rupees)

State.	1941-42	1942-43	1943-44
A. Duty on imports from—			
Jamnagar (Nawanagar) ..	4,97,938	4,68,170	18,256
Baroda	21,79,716	49,30,522	70,28,587
Morvi	4,03,876	6,45,896	3,15,753
Junagadh (including Mangrol)	9,902	27,356	4,495
Porbandar	1,16,108	37,382	9,039
Bhavnagar	32,274	58,578	1,08,963
Miscellaneous places ..	70,977	2,13,359	15,18,601
Total ..	33,10,791	63,81,263	90,03,694
B. Duty foregone on imports from—			
Jamnagar (Nawanagar) ..	4,97,938	4,68,170	18,256
Baroda	21,79,716	49,30,522	70,28,587
Morvi	4,03,876	5,00,000	3,15,753
Junagadh (including Mangrol)	9,902	27,356	4,495
Porbandar	1,16,108	37,382	9,039
Total ..	32,07,540	59,63,430	73,76,130
C. Duty Demanded or recovered in cash—			
Jamnagar (Nawanagar) ..	.....	.....	.....
Baroda .. .. .	.....	.....	.....
Morvi .. .. .	.....	1,45,896	.....
Junagadh (including Mangrol)	.....	.....	.....
Porbandar .. .. .	.....	.....	.....
Bhavnagar	32,274	58,578	1,08,963
Miscellaneous places ..	70,977	2,13,359	15,18,601
	1,03,251	4,17,833	16,27,564

The question arises as to what should be done with this Viramgam Customs Cordon, as much as with the customs rights of other maritime States. During Lord Reading's viceroyalty, a scheme for the establishment of a customs *zollverein* was drawn up, with the following objects in view (Butler Committee Report, paragraph 83) :

- (1) The adoption of a common tariff administered by officers of the Government of India even in maritime States;
- (2) The abolition of all land customs; and
- (3) The division of customs revenue among the Indian Provinces and the different States.

The *zollverein* scheme was, however, not formally presented to representatives of the maritime States, for reasons which are not explicable today. It was, however, recognised that in view of the fact that as much as Rs. 4½ crores a year were raised by the States, from local import and export duties alone, the share of maritime States from the general customs revenue would be of considerable magnitude, in so far as the Government of India were concerned, while questions of sovereignty, on which the States were very sensitive, block the way for a further pursuit of this arrangement.

It is here interesting to make a reference to the Barcelona Transit Convention of 1921, to which India (meaning thereby the Provinces as administered by the Government of India) was a party, of which article 15 runs as follows: "It is understood that this Statute must not be interpreted as regulating in any way rights and obligations *inter se* of all territories forming part or placed under the protection of some sovereign States, whether or not these States are individually members of the League of Nations". The States sought to take shelter under the provisions of this Convention, the only argument in their favour being vague considerations of sovereignty to impose customs revenue (with the possible exception of Mysore).

CUSTOMS ALWAYS A CENTRAL HEAD

On this vexed question of maritime customs, the Butler Committee wrote as follows (paragraph 81 of their Report) : "On principle, then, we hold that British India is fully entitled

to impose maritime customs for the purpose of India as a whole. It is a central head of revenue in which the Provinces of India have no share”.

We must here take into consideration what the Davidson Committee concluded after further enquiry into this vexed question. This Committee wrote (paragraph 382): “If . . . the port-owning States are to enter Federation, as every one must desire that they should, room must be found for a compromise in which ideals and logic would yield in some measure to hard facts. An arrangement whereby the maritime States were at least enabled to retain in their own hands the value of the duties on goods imported through their ports for consumption by their own subjects, even though it would involve some slight diminution of federal revenues, might well be accepted in a federal scheme embracing so many diverse elements.” The Davidson Committee (paragraph 383) took notice of such of the existing treaty rights between the Paramount Power and the States, and laid down that they must be adhered to as far as possible. Where, however, there are no such treaty rights, the Committee recommended some system of financial adjustments “whereby the State would retain or have refunded to it the amount which, consistently with the suggested principle, it was entitled to receive, or else the maintenance, where necessary, of a customs barrier”.

We would conclude the examination of this question with a further quotation from the Davidson Committee Report (paragraph 242): “No one disputes the right of the States, in their own interest and for their own purposes, to levy customs at their ports; but it is clear that the British authorities are fully entitled to take steps to secure that their own revenues are not thereby prejudiced. British India also not unreasonably complains that trade is diverted from its own ports, with consequent loss of revenue, to ports developed and maintained by States by means of subsidies from their general revenues, which are being constantly increased by the customs duties arising from the trade which those subsidies have attracted”.

We agree with the recommendations of the Davidson Committee (page 131) that “the ideal of a true Federation is difficult to reconcile with the retention by any federal unit of customs

duties collected at its ports, but we recognise that no maritime State is likely to relinquish this right". The Committee observed (paragraph 379) that the rights of the States concerned came into existence as the consequence of a mutual exchange of valuable concessions, with the result that there was no question at all of any cession of rights arising from sovereignty, and that, in fact, the customs rights were purely commercial rights, which should be susceptible of adjustment on a commercial basis agreeable to both the parties.

We have now more or less merged from the welter of discussion which has characterised the study of this question of maritime customs belonging to the States during the past half a century, and it is now necessary to make a projection into what should be done by the Union Centre to tackle it satisfactorily, and put its solution on an enduring basis. The Union Centre, composed as it is of Provinces and States, cannot, under any circumstances, surrender customs, as a source of its revenues. Such surrender would be inconsistent not only with principles of public finance, but would greatly endanger the very structure of taxation and income appertaining to it. There is no known example in world history where a Federation, or even a Confederation, had surrendered customs rights to any of its component parts. In the case of India, the behaviour of Central revenues has been such that, at any rate until recently, customs supplied the greater portion of the grist to the mill of Central finance than any other head of revenue, with only taxes on income trying to precede this as the main head of revenue. Our projection into the future finances of the Union Centre compels us to state, at any rate in the light of existing indices, that Central expenditure would be far ahead of that ever so far reached, and that it would continue to depend upon customs revenue to a more or less extent as before.

In any case, there cannot be integrity to the Union finances, if customs revenue, both maritime customs as well as land customs, is not collected by the Union Centre, even if such a proposition involves an allocation of revenues to such of the maritime States and States like Kashmir, in due proportion, to compensate for losses of revenue to which the States would become subject in the process. In other words, something very much

like the creation of a Central income-tax pool, and its division as under the Niemeyer Award, must be brought into existence with reference to the customs *regime* for the Union Centre.* This, certainly, is a task of considerable magnitude and complexity, but we venture to hope that, since numerous enquiries have been held so far into this question during the previous decades, it would be possible for the incoming maritime States, and States like Kashmir, to arrive at a basis of settlement with the Union Centre, and to surrender customs in order to make possible a Federal *regime* of tax collection. Closely allied with this question of tax collection and tax division as between the Union Centre and the States, is the question of the control, management and development of maritime ports, as a vital problem of defence for the Union Centre. Without surrender of rights by the States concerned to the Union Centre, there cannot be any possibility for the constitution-makers to bring about a uniform system of commerce and defence for the Union as a whole.

What should be the principles for the determination of the moieties of maritime States from the Customs revenue? The Nind Committee (paragraphs 6 to 35) have attempted to discuss this question at some length. The Committee pointed out the extremely complicated character of the administration of customs under the existing treaty rights. Travancore received compensation for the abolition of land customs. Cochin receives a moiety of customs collected, after deducting working expenses. Kashmir can import goods direct through the Indian Ports, and obtain a rebate of duty charged at the ports. There are special arrangements for the transfer of goods from Indian Ports intended for Afghanistan on the one part, and Nepal, Bhutan and Sikkim on the other. The widely separated areas of the

*The Joint Parliamentary Committee, Volume I, paragraph 264, observed as follows :—

“We recognise that it is impossible to deprive States of revenue upon which they depend for balancing their budgets and that they must be free to alter existing rates of duty to suit varying conditions. But internal customs barriers are in principle inconsistent with the freedom of interchange of a fully developed Federation, and we are strongly of the opinion that every effort should be made to substitute other forms of taxation for these internal customs. This change must, of course, be left to the discretion of the States concerned, as alternative sources of revenue become available.”

new-fangled Pakistan State must necessarily discuss with the Indian Union these and other cognate matters. It is clear that some formula must be arrived at, which would secure to the States immunity against losses from the surrender of maritime or land customs, at the same time making it possible for the Union Centre to function as an integral whole, with a completely unified customs *regime*, without which it cannot survive as a State.*

The Nind Committee adopted a dozen yard-sticks to ascertain the moieties of customs revenues which maritime States would be entitled to. The Committee had taken into consideration population proportions *vis-a-vis* the maritime States on the one part, and India as a whole. It had also meticulously gone into the consumption habits of classes of people in the States in order to determine equations of imports, on the basis of which the financial adjustments are to be brought into existence. The Committee wrote (paragraph 34) as follows: "An assumption underlying the scheme is that articles of universal consumption are consumed in all parts of India in quantities proportionate to the total population. This may be true of the country considered as a whole but not of particular areas in it." After very careful investigation, the Committee, however, came to the conclusion that no single method, nor even all the dozen methods of approach, adopted by it would stand scientific scrutiny, and satisfy all the parties concerned. The Committee wrote as follows (paragraph 31): "The individual States differ so greatly in composition that the utmost that we can hope for is that the total figure at which we have arrived, represents a fair estimate

*The following report appeared in the *Hindustan Times*, New Delhi, of July 4, 1947: "The Union Government, it is understood, will enter into arrangements with Nawanagar State for developing Nawanagar into a first class port and airfield, soon after August 15. The Jam Saheb of Nawanagar is understood to be willing to let the Union Government take charge of the port for extension and development. One of the proposals is to take the port on long lease from Nawanagar and to pay the Jam Saheb a fixed yearly lease money. Another suggestion is to let the Jam Saheb enjoy a portion of the customs revenue on goods imported through the port. Detailed negotiations, on the arrangement that will be entered into with the Jam Saheb, are expected to take place immediately after the conclusion of the coming session of the Constituent Assembly. The capacity of Nawanagar to be developed into one of the finest ports of India has been testified by various experts who have, from time to time, surveyed the port on behalf of the Central Government."

of the amount of import duty which the States, as a whole, contribute by their consumption of the articles imported. It is possible, by taking the census and other statistics of individual States, to divide this sum into separate shares for each State, but the results so obtained are likely to be less accurate as representing the shares contributed by individual States. Still less accurate is the result likely to be when applied to particular items in the tariff; for instance, a State which is mainly agricultural is likely to import more manufactured articles than have been allotted to it in our scheme and less than its allotted share of factory stores."

LAND CUSTOMS

The small but cognate question of land customs must be discussed here in some detail. According to the latest figures available to us, the total receipts from the various land customs stations on the frontiers of Goa and Daman amounted to Rs. 17,56,274 in 1940-41, as compared to Rs. 26,20,281 in the preceding year. As for the land customs collected on the Pondicherry and Karikal frontiers, the figures for the same years were respectively Rs. 5,56,589 and Rs. 10,16,130. We have already seen the importance of Viramgam land customs, which merge into and again taper off from maritime customs relating to the ports of Kathiawar and Cutch.

In addition to these, there are land customs in which Kashmir, which is now supposed to be ready to declare its independence, occupies a prominent place. Kashmir has a small interest in customs belonging to the Central Government, arising out of the Treaty of 1870. Under this Treaty, Kashmir agreed to allow free transit for merchandise passing through the State's territory by the Central Asian trade route, thus establishing trade relations between the Provinces and Central Asia. In return for the loss of revenues thus engendered, Kashmir was accorded the privilege of importing "sea-borne goods in bond". The method adopted was that all goods imported in bond are covered by the invoices shown at the port of entry. These amounts are credited to the *darbar*, on the authority of the endorsements made on the invoices by the Resident at Kashmir.

This arrangement was of little practical importance about half of a century ago, but today, however, the customs revenue foregone by the Central Government represents, according to the estimates of the Davidson Committee (paragraph 366), on an average Rs. 25 lakhs per annum. The Central Asian trade passing through Kashmir was of the order of Rs. 21 lakhs. For our purposes, it is clear that, with minor adjustments it will be the concomitant of the possible entry of Kashmir into the Union Centre, these two heads of revenue might be adjusted, one against the other. If Kashmir stays out of the Union Centre, or of Pakistan, then her trade belongs to the sector of foreign trade which belongs to any country, and will have to be treated as such.

We have no objection to the continuance, if such were desired, of the practice of allowing duty free goods intended for ceremonial purposes by the States' *darbars*, but we cannot agree that the customs *regime* of the Union Centre can, in any way, be deflected through the medium of bonded goods and book accounts. Perhaps, we should say that a revision is called for of the existing arrangements between the Union Centre on the one part, and such independent kingdoms like Nepal on the other. An examination of this question in relation to Nepal is, however, clearly outside the scope of this enquiry.

CENTRAL EXCISES

Central excises are playing an increasingly important *role* in the finances of the Government of India during recent years, and it is clear that they must also play a greater part than hitherto in the evolution of Central finance enveloping both Provinces and States. The Constitution Act (section 140) has the following provision: "(1) Duties on salt, Federal duties of excise and export duties shall be levied and collected by the Federation, but, if an Act of the Federal Legislature so provides, there shall be paid out of the revenues of the Federation to the Provinces and to the Federated States, if any, to which the Act imposing the duty extends, sums equivalent to the whole or any part of the net proceeds of that duty, and those sums shall be distributed among the Provinces and those States, in accordance with such principles of distribution as

may be formulated by the Act. (2) Notwithstanding anything in the preceding sub-section, one half, or such greater proportion as His Majesty in Council may determine, of the net proceeds in each year of any export duty on jute or jute products shall not form part of the revenues of the Federation, but shall be assigned to the Provinces or Federated States in which jute is grown in proportion to the respective amounts of jute grown therein."

The following table illustrates the importance of excises to Central revenues.

(In lakhs of rupees)

Year	Collec- tion.	% of total revenue.	Year.	Collec- tion.	% of total revenue.
1920-21	20,44	15.1	1942-43	12,79	10.1
1937-38	7,66	11.8	1943-44	24,94	14.5
1938-39	8,66	11.6	1944-45	38,14	14.8
1939-40	6,53	8.0	1945-46	46,36	16.4
1940-41	9,49	12.2	1946-47 (R.E.)	42,79	15.8
1941-42	13,15	13.3	1947-48 (B.E.)	40,93	14.9

The above table needs explanation. A new basis of financial settlement was introduced between the Centre and the Provinces in 1921, under the Meston Award, to suit the wide measures of legislative, administrative and financial devolution made under the Montagu-Chelmsford Reforms. Subjects in Governors' Provinces were classified as Central or Provincial, with reference to the functions of the respective Governments, and there was a clean cut in the matter of allocation of heads of revenue and expenditure. The Provinces also obtained a share in the growth of revenue from income-tax, so far as that growth was attributable to the increase, in the amount of income assessed, and were also given powers to impose new taxes. The distribution of the sources of revenue on these lines resulted, during the initial stages of the new constitution, in a large deficit in the Central Budget, and this was met by the contributions from the Provinces. These contributions were gradually reduced, and were finally and completely remitted with effect from 1928-29. The constitutional machinery set up under the

Constitution Act made necessary a readjustment of financial resources and obligations between the Centre and the Provinces. The financial arrangements embodied in the Act provide for assignment to the Provinces of a definite share in the proceeds of income-tax, and its distribution among them in a prescribed manner, and allocation to the jute-producing Provinces a prescribed share of the net proceeds of the excise duty on jute and jute products.

The table on the next page illustrates the position of Central excises on the basis of Provincial collections.

UNION FINANCES

Provincial Division of Excise Revenue.
(In thousands of rupees)

	1937-38	1938-39	1939-40	1940-41	1941-42	1942-43	1943-44	1944-45	1945-46	1946-47 (Revised Esti- mates).	1947-48 Budget Esti- mate).
Madras	59,58	43,32	52,07	78,06	83,25	87,67	3,00,56	5,55,59	6,43,26	5,60,50	
Bombay	70,94	76,39	75,31	91,57	1,24,93	1,31,53	3,39,56	4,64,93	5,01,85	4,29,15	
Bengal.. .. .	1,20,27	1,24,41	1,09,90	1,43,90	1,99,59	1,75,02	6,98,30	13,05,30	16,20,26	11,62,29	
U. P.	2,33,11	3,08,25	1,78,93	2,29,92	4,50,66	3,53,74	5,65,83	6,96,79	6,18,81	7,65,11	
Punjab	22,76	40,57	53,46	1,18,62	1,06,51	1,32,81	1,28,98	1,40,51	1,45,42	1,34,70	
Bihar	1,04,12	1,02,31	76,17	1,01,69	1,69,28	1,21,60	2,52,69	2,82,88	3,17,12	4,35,47	
C. P.	62	74	52	41	1,60	2,49	86,25	1,07,47	1,12,75	1,05,63	
Assam	1,44,40	1,61,62	1,19,40	1,66,25	1,57,93	2,43,67	3,12,41	3,49,47	2,97,45	1,96,49	
N. W. F. P. .. .. .	.....	.....	.....	8	3,86	2,26	14,29	22,78	24,54	27,20	
Orissa	31	63	37	1,75	1,96	99	7,75	13,32	12,74	14,46	
Sind	15,08	82	1,24	1,72	1,95	22	11,73	17,44	18,73	24,02	
Indian States	-4,83	6,67	-14,87	14,64	13,60	27,85	-2,25,50	-1,44,86	.....	21,94	
Total	7,66,36	8,65,73	6,52,50	9,48,61	13,15,13	12,79,36	24,93,61	38,14,37	43,12,93	38,76,96	

Not Available

An examination of the structure and division of excises under Central and Provincial heads illustrates the point that the Provincial moieties to the Central pool, as indicated in the preceding table, do not explain the whole picture relating to excises in the country. The Provinces have their own excises, other than Central excises, and the figures given in the preceding table only relate to Provincial collections under the Central head. The following table gives the total Provincial collections of excises, including both Central and Provincial heads.

Provincial Excise Revenue
(In thousands of rupees)

Province.	1944-45	1945-46	1946-47 (R.E.)	1947-48 (B.E.)
Madras	12,77,89	16,79,50	14,21,73	9,58,87
Bombay	7,55,90	8,90,90	9,01,17	9,41,86
Bengal.. .. .	7,33,64	8,17,26	5,62,61	5,88,61
U. P.	4,97,76	5,94,97	6,15,20	5,25,06
Punjab	3,63,76	3,03,46	3,31,90	3,37,88
Bihar	3,50,05	4,61,81	3,95,00	3,95,00
C. P. .. .. .	.....	2,44,42	2,14,24	1,81,35
Assam	82,54	88,46	72,84	70,26
N. W. F. P.	22,84	21,33	26,33	26,15
Orissa	61,71	88,36	1,06,48	1,05,00
Sind	1,22,72	1,40,22	1,31,94	1,24,95

The preceding two tables require to be examined in their implications arising out of the series of constitutional developments of the inter-war period. Under the arrangement made with the States in connection with the imposition of the excise duty on matches, the whole of the proceeds of the tax collected in the various States is paid into the common pool, along with the proceeds of the tax from the Provinces, and the net proceeds of the pool, that is to say gross realisations less collection and other charges and refunds or rebates, are divided between the Provinces on the one hand and the States that have agreed to come into the arrangement on the other, on the basis of population, regardless of whether match manufacture does or does not at present, or may or may not in the future, take place in those States. The States which have joined the scheme have undertaken to levy the duty under the same pro-

cedure as is enforced in the Provinces. When the settlement with the participating States involved a payment to them of their share of the proceeds of the duty, such payments have been adjusted in reduction of receipts, and this accounts for the *minus* figure in the collection for "Indian States" in the first of the preceding two tables.

An examination of the operation of excises in the States shows some very incongruous facts. It was, as stated above, laid down that the match excise duty was one which should be uniform, even though some of the States may not be producing matches. Rampur, for example, has a match factory which produces more than what is required for domestic consumption. If, however, the match excise was to be distributed on the basis of production, then Rampur would have secured a very large income, but the division has been done on the basis of consumption, with the result that the State has been more or less "done in the eye", as the protagonists of the States would aver. This method is, however, necessarily inevitable. Tax collection in the States is, however, done by their own officers, and for the duties rendered States receive a certain percentage which is the normal collecting charge in the Provinces.

Similarly, there are taxes on tobacco, *vanaspati*, etc. These taxes are also collected through the States' officers in some States, while there are officers of the Government of India in others where the *durbars* do not undertake the duties involved. The Government of India, after laying their hands on the entire proceeds of the tax in question and after deducting expenses, distribute the resultant moieties to Provinces and States on a *per capita* basis.

The position in respect of sugar excise, however, is different. A few States have established sugar factories, and we again take the case of Rampur, of which we have some precise knowledge. When the sugar excise duty was levied by the Government of India, it was felt necessary to impose some tax on sugar produced in the States, since all the sugar produced in the States concerned could not be consumed within their boundaries, and had to be brought outside into the Provinces. This question was discussed at very great length by the Government of India and the States, and it was finally decided that some

portion of the income could be retained by the States, if they could show that it was necessary to ensure efficient administration of the tax within their jurisdiction. The result was that Rampur and a few other States continue to receive a portion of this sugar excise duty. During the recent war period, when the duty was raised, the Government of India made it a point that the States do not get the benefit of the increase, but only what they had received prior to that increase. Thus, the increase of the resultant income from the duty went into the coffers of the Government of India.

The Provinces had, for some time past, been imposing a cess on sugar cane produced within their territories, and utilised the proceeds for improving seed and methods of sugar cultivation. This practice was followed by the States, but no part of the cess was paid to the Government of India or to any neighbouring Province. This is as it should be.

The Indian Roads Congress had decided that, in order to improve roads in the Provinces and the States, a levy should be imposed on the sale of petrol, for purposes of the Road Fund. The amount so collected from all sources, including the States, would be put into a central pool, from out of which amounts would be doled out to the States for purposes of road development, if the authorities administering the pool were satisfied on the point. Thus, every State receives a quota, though, it is alleged by the protagonists of the Princes, not in proportion to the consumption of petrol within its jurisdiction.

Octroi duties imposed on goods intended for consumption are levied when they enter any State, and are refunded when they come out into the Provinces. The question of duties on goods transported by river has not been taken up as yet. *Rahdari* had been abolished in the States, in return for certain concessions granted to them in the Provinces, e.g., Rampur has a right to obtain cost-free and duty-free a specified quantity of timber from the Naini Tal region, in exchange for the abolition of *rahdari* duties within its territorial limits. *Kaththa* (the aromatic spread which is put on betel leaves) is in the same category as the Naini Tal timber under this head.

The question in respect of opium is rather a ticklish one. Formerly the States used to produce their own opium, and even

were in a position to export it to the Provinces and overseas countries. Since India had adhered to the International Conventions dealing with control of narcotics and opium, and as a result of the curtailment of consumption of opium and its export to China, the Government of India took upon themselves the task of centralising all the opium resources of the States and the Provinces. Some of these States have ceased to produce opium in return for certain contributions as compensation from the Government of India. Others producing it entered into long-term agreements with the Government of India, to supply crude opium to the Provinces adjoining their territories. The result is that now no State can cure or prepare opium for consumption within its territory. Each State obtains opium from the Provinces, at a rate which covers expenses of the manufacture additional to the cost of the raw product itself. The States have the immunity that no customs duty will be levied on opium supplied for consumption within their territories. We do not think that this exemption would be possible under the set-up of the Union Centre.

No Union Centre can function without unity in the administration of excises. According to the Davidson Committee (paragraph 190) the grievances of the States are two-fold. In the first place, rights leased in the past by the States to the governments of Provinces, which are contiguous to their territories, are being diminished gradually in value, owing to the adoption of a policy of progressive prohibition. This is in respect of country liquors, and even of foreign liquors. Secondly, there are certain excisable articles, particularly opium, which cannot be obtained in the States, except from the governments of contiguous Provinces, and the complaint has gone forth that the Provincial Governments concerned appropriate to their revenues a considerable part of the excise duties, for the time being in force, in respect of the supply of excisable articles to the States concerned.

The question of *charas*, a hemp drug which is imported from Central Asia and issued to the States and other local governments from warehouses in the Punjab, falls into a category of excisable articles which is entirely exceptional. Till recently, the Punjab Government had appropriated the whole of the

duty on this drug, but in recent years the Government of India had seen to it that the duty in question is refunded to the States on a basis which is equitable in its incidence. The Nind Committee has attempted to build up (Table IX of the appendices of its *Report*) a list of refunds on Central excises to the States as were in force in 1930, and we consider that their relative position today could not be much different to what it was nearly two decades ago. It is not necessary for our purposes here to examine each of the principal excises in force today, and we accept the finding of the Nind Committee (paragraph 152) that the net amount of revenue involved, after deducting refunds, is comparatively small. However, we cannot over-emphasise the point that the vital principle of the need for uniformity of administration, in respect of habits which are deleterious in character, is involved in the Union Centre's future policy regarding excises.

Taking the opium question, we entirely agree with the Butler Committee (paragraph 103) in the observation that it is "essentially a case in which the States must bear their share of Imperial Burdens imposed on India as a whole in the interest of humanity and civilisation. It is not practical politics to ask the Indian tax-payer to grant the States compensation in this matter when he has suffered so heavily himself". It is estimated that even since the adhesion by India, meaning thereby the Provinces, to the Hague Opium Convention of 1911, as amended by subsequent conventions which are half a dozen in number, the tax-payer of the Provinces had, till today, surrendered income of the aggregate order of Rs. 100 crores. This self-denying ordinance in the interests of humanity and civilization, as the Butler Committee put it, has hardly any parallel in world history. It is obvious that such of the States which elect to come into the Union, and the other States which stand out, cannot be permitted to imperil this *regime*, the quantum of whose social value cannot be over-emphasised. We shudder to think of the day when the States might precipitate something like the Boxer wars of China, by claiming to exercise, as a part of their sovereignty, the right to manufacture and trade in opium and narcotics *e.g.*, *ganja*, *charas* and other drugs.

The above statement remains valid with respect to the manufacture and sale of country liquor. With the progressive introduction of prohibition in the Provinces, as a part of national policy, and recognising the inextricably interwoven character of the Provinces and the States, whether the States come into the Union or Pakistan or not, we have to emphasise the point, that a common excise policy in respect of spirituous liquors, whether imported or country-made, must become a part integral to a unionised excise policy of tomorrow.

SALT TAX

Today there is a doleful interest in the salt tax as a source of Central revenues. The first Indian Finance Member of the Government of India, who is however now going to Pakistan, has this year abolished, in response to the demands of the Congress, the salt tax in the Provinces, and a source of revenue, of the estimated value of Rs. 9 crores a year, has been lost, and lost very willingly. We are not convinced whether the salt tax actually impinges heavily upon the margins of security of the common man in the country, but we know that from a purely psychological point of view there cannot be any question, either today or tomorrow, of the revival of this tax, which has for long been remembered as one of the specific ways in which British hegemony has been clamped down upon our people. The salt tax is dead and gone as far as the Provinces are concerned, but there is no knowing as to its future with respect to the States, with the result that an examination must be undertaken here of this tax in regard to production of salt and the tax thereon within their jurisdiction.

There are two aspects of this question which have got to be distinguished in this connection. States which elect to remain outside the Union Centre, or Pakistan, would be alien territories, whose relations with the two polities of the Provinces have got to be re-determined in terms of specific treaties or other arrangements. Secondly, States which come into the Union Centre, or Pakistan, must necessarily arrive at a basis of re-determination of the arrangements which have preceded the abolition of the salt tax.

The salt tax had been imposed in India by the East India Company, and was continued by its legal successor the British Government in India, on a two-pronged basis. In the first place, there was a general, though vague, attempt at making provision for the supply of salt to the population. Secondly, and this is the more important consideration—salt was considered to be one of the most important items of revenue to the Central Government, supplying, during the inter-war period, considerably over 6 per cent of its total revenues. Concentrated production, efficient methods of manufacture and sale, and abolition of transit duties have, to a large extent, secured the reduction of the price of salt, while the introduction of the salt tax, at any rate in the States, where it did not exist before, had meant the imposition of additional burdens on the peoples of the States concerned.

On the basis of the enquiries made by the Nind and Davidson Committees, it was established that the immunities and privileges enjoyed by the States in respect of salt were of the order of Rs. 46 lakhs a year in 1931-32. The Davidson Committee reported that it was almost impossible to secure the revision of the heterogeneous mass of agreements relating to salt, as between the States which produce salt and the Paramount Power, for the purpose of determining a valuation of these rights to the former. Earlier, the Butler Committee (paragraph 96) was not prepared to recommend any general revision of arrangements which, it claimed, have worked well on the whole. Now that Paramountcy is to be abolished in the States, a situation of considerable importance and delicacy has definitely arisen with respect to this question.

India has always been a deficit country in salt production. Prior to 1930, the total imports of salt were of the order of 50,000 tons a year. In the latter half of the inter-war period, these imports declined to 318,000 tons a year, of which the greater portion was supplied by Aden alone. During the recent war period, the import of salt from abroad declined naturally to 207,000 tons a year, of which 109,000 tons came from Egypt, and 79,000 tons from Aden.

The average production of salt in India during war years was estimated at 2,200,000 tons a year, as compared to 9,200,000

tons in the U.S.A., 3,900,000 tons in U.S.S.R., 2,700,000 tons in the U.K., and smaller quantities in China and Germany. Canada, France, Spain, Italy and Japan follow India in the descending order of importance. It is estimated that there is need for an additional 1,000,000 tons of production of salt if India is to become self-sufficient, what with the imperative demand for salt supplies for industrial purposes, and the equally necessary additional allotments for consumption by cattle. It is also estimated that, if the *per capita* consumption of salt in India is to be raised to the world average, we would require a total production of 5,000,000 tons a year.

One of the most curious features of the salt question in this country is that, in the first place, salt produced, whether it be rock salt from the Punjab and the North-West Frontier; from inland salterns like those of the Sambhar Lake and Khara-goda; or from the littoral salterns which are mostly spread on the Coromandel coast and in Kathiawar and Cutch, the distribution of salt is on a regional basis. Secondly, the surplus areas of the West have to supply salt to the deficit areas of the East, particularly to Bengal.

If we take the average production of the recent war years, and compare it with the production of pre-war years, the annual production of salt is as hereunder:

(In tons)

Source.	Pre-War average.	War Average.
North-west India	192,000	241,000
Rajputana	316,000	395,000
Bombay	452,000	545,000
Madras	419,000	491,000
Sind	116,000	128,000
Kathiawar and Cutch	225,000	298,060
Other minor sources	108,000	136,000
	1,828,000	2,234,000

An analysis of salt production from the viewpoint of the States become important at this juncture, for it has been variously estimated that the production of salt in their territories has a potential capacity of a fourth of the total requirements of

the country, on the basis of present *per capita* consumption standards. The figures we give below are tentative, and not exhaustive.

(In maunds)

Source.	Pre-war average.	War average.
Sambhar Lake	73,09,000	92,44,000
Didwania Salt Works	2,32,000	5,31,000
Pachbadhra	10,47,000	9,75,000
Kharagoda	29,43,000	33,68,000
Baroda	15,00,000	9,00,000
Morvi	7,00,000	9,00,000
Jamnagar	8,00,000	13,00,000
Dhrangadhra	6,00,000	14,00,000
Porbandar	13,00,000	11,00,000
Junagadh	2,00,000	1,35,000
Jatrabai	2,00,000	5,65,000
Bhavnagar .. .. .	.....	5,00,000
Cutch	3,00,000	9,00,000
Other Kathiawar and Cutch States	5,27,000	4,00,000
Travancore .. .. .	.....	16,00,000

It is obvious that the abolition of the salt tax in the Provinces, viewed in the light of the above information relating to salt production in the States, creates a vacuum in the fiscal sphere, and demands careful handling of the resultant problem. Let us study the proposition in two instalments. Will the States manufacturing salt copy the abolition of the tax as contrived in the Provinces, and bring about uniformity of conditions in these two components of the Indian Union, or Pakistan? If the States do not, what will be the position of salt manufactured in their territories, which will be outside the jurisdiction of the Union Centre, unless specifically surrendered to it within the ambit of the Instruments of Accession of the Rulers concerned? A projection into the immediate future of this question convinces us that, unless otherwise settled, the salt-manufacturing States would continue to manufacture salt for profit; that they would throw impediments in the way of the distribution of salt to the people of the areas outside their territories; that they would force up prices, thus imperilling the price structure of salt in the Provinces; and that they would succeed in sabotaging the new *regime* under which the salt tax was abo-

lished in the Provinces. The withholding of supplies of salt manufactured in the States might as well lead to a salt famine in the Provinces, while the continuance of the duty on salt in the States would mean the pushing up of the price of salt which the peoples of the Provinces and of the States have to pay.

This, certainly, is a dilemma of considerable complexity, and has got to be faced by the constitution-makers. It would seem to us that a series of arrangements have to be negotiated between the Union Centre and the salt-manufacturing States, through the Instruments of Accession of the Rulers concerned, commuting these privileges and immunities, and bringing about a uniform *regime* of a tax, which was abolished on the assurance that it would never rear its head again in this country.

It is not necessary for our purposes here to analyse the privileges and immunities catalogued in Appedix V to the Davidson Committee Report, but a few examples may be given as illustrative of the complexity and sometimes of the ludicrousness, of this question. Dozens and dozens of salt arrangements had been agreed to between the Paramount Power on the one part and the States on the other, in order to straighten out the salt tax imposed by the Government of India at various dates during the course of the British occupation of this land. In most of the agreements, the East India Company and the Crown had acquired the right to sell salt to the States, in exchange for a free supply of untaxed salt and an annuity in cash to each of the States concerned.

Thus, for example, Palanpur was given an immunity of 350½ maunds of untaxed salt, whose annual immunity value was estimated to be Rs. 548. In the case of Travancore, the right to manufacture salt from its own resources has neither been bought out nor restricted by agreement, and the immunity value of this right was estimated by the Davidson Committee at nearly Rs. 20 lakhs a year. Cochin is in the same category as Travancore, and the immunity value was considerably over Rs 4½ lakhs a year. Jaipur and Jodhpur jointly own the Sambhar Lake, and the share of Jaipur was leased out to the Government of India in 1869, in exchange for a cash compensation of Rs. 2,75,000 per year, together with a royalty and a free grant of

a specified quantity of duty-free salt for the use of the *darbar*. At a later date, these immunities of Jaipur were commuted for a cash contribution of Rs. 4 lakhs a year. In the case of Bahawalpur, all the rights of the State in respect of salt were surrendered without any immunity attached to them. Alwar has a compensation of Rs. 1 lakh a year for the surrender of its right to salt. In the case of Bikaner, the *darbar* was given the privilege of obtaining 70,000 maunds of salt a year, on the payment of half the prevailing duty, the remaining half accruing to the State. Jaisalmer has the restricted right of local salt manufacture to the extent of 15,000 maunds a year. Gwalior's immunities under this head were Rs. 2,125 a year! Indore has no immunity at all, for it was entitled to receive 45,000 maunds of salt at privileged rates each year.

The Nizam has the right to produce 5,000 maunds of earth salt, taxation on which does not accrue to the Government of India, and has an immunity of Rs. 7,812. In the case of Mysore, the right to produce earth salt is unrestricted, subject to the condition that it would not be exported outside the States' territories. The immunity value for this State was put down at Rs. 1,563. Mandi has rock salt mines, and has a special arrangement, under which an immunity of Rs. 27,438 was assessed per year in its favour by the Davidson Committee.

The Kathiawar and Cutch States constitute a category by themselves, and under the arrangements of 1883 the *darbars* of these States agreed "so to regulate the production in Kathiawar for the consumption of its inhabitants, and no salt produced in Kathiawar may be conveyed into British India." This position has since changed, and the annual value of the immunities of these States, which include Dhrangadhra, which is famous for its *Baragra* salt, are of the order of some Rs. 8 lakhs a year. The Davidson Committee has this very interesting recommendation to make with respect to Kathiawar and Cutch States (page 83 containing summary of recommendations): "All existing restrictions on the manufacture and marketing of salt should be removed, subject to the condition that the States concerned should permit collection to the federal salt duty by federal officers at the source of manufacture, together with the application of such administrative regulations as are common

to the maintenance of salt works and the movement of salt throughout India.''

The Nind Committee arrived at the very important conclusion that the cost of expenditure on the administration of the salt tax which the States shoulder was 19.75 per cent of the total for the country as a whole. It is clear that the Nind Committee and the Davidson Committee supply us with a clue to the solution of the new salt tax problem arising out of the abolition of the tax in the Provinces. Salt must be a Central head, not necessarily now of revenue, *but of management*. States coming into the Indian Union, or Pakistan, must undertake to abolish the salt tax, if only for the purpose of ensuring equitable distribution of salt as between themselves and the Provinces, and for maintaining an equitable salt price. Losses accruing to the States from the abolition of the salt tax within their territories must be commuted on a financial basis, and the finances of the Union Centre must have a charge placed on them of these payments to the States which agree to a voluntary loss of revenue from this source. States which do not come into the Union Centre or Pakistan, either on this score or on any other score, can only be left to fend for themselves in isolation. Here is yet another example of the need for integration of the fiscal and economic systems of the Union Centre. These arguments are valid in the case of Pakistan as well, both in the East and the West, subject to the proviso that in her case the States involved, and likely to adhere to its separate enveloping polity, can be counted on the fingers of one hand.

CHAPTER V

DEFENCE OF THE UNION

“The Paramount Power is responsible for the defence of both British India and the Indian States and, as such, has the final voice in all matters connected with defence, including establishments, war materials, communications etc. It must defend both these separate parts of India against foes, foreign and domestic. It owes this duty to all the Indian States alike..... It follows that the Paramount Power should have means to secure assets necessary for strategical purposes in regard to roads, railways, aviation, posts, telegraphs, telephones and wireless, cantonments, forts, passage of troops and the supply of arms and ammunition.”

—Butler Committee Report, Paragraph 48.

“The reason for the lack of enthusiasm that should accompany such a great event as the imminent advent of full freedom is the division of the country into two States, which are to be turned into two armed camps. The army is to be divided, and preparations are being made apiece to that end. I visualise a definite increase in military expenditure, all for fighting among ourselves. Instead of self-glorification, it is a time for deep self-introspection, self-examination and self-castigation.”

—Mahatma Gandhi, in his prayer meeting on July 6, 1947.

**OBLIGATIONS OF STATES TO SUPPLY FORCES—
STRENGTH AND COSTS OF STATES FORCES—
STRENGTH AND COSTS OF INDIA'S DEFENCE—
IMPLICATIONS OF PARTITION—SCOPE OF UN-
IONISED DEFENCE - FEUDAL ARMIES INCON-
SISTENT WITH UNIONISATION—NEED FOR
TERRITORIAL ARMY - DANGER FROM ZAHAROFFS.**

The provisions of the Constitution Act relating to the Defence Services must now be deemed to be completely inoperative. Items 1 and 2 of the Seventh Schedule of the Constitution Act, which are included in the Federal Legislative list, mention His Majesty's "naval, military and air forces borne on the Indian establishments and any other armed forces raised in India by the Crown, *not being forces raised for employment in Indian States*, or military or armed police maintained by Provincial Governments" (Italics ours). Under section 33 of the Act, the Governor-General has a special responsibility to discharge "his functions in relation to the administration of any territory in the direction and control of which he is under this Act required to act in his discretion."

OBLIGATIONS OF STATES TO SUPPLY FORCES

The following two tables illustrate the obligations of Indian States to supply contingents, raised and equipped by them, for service with the Imperial forces of Britain in India, which means

only their detailing for service outside the jurisdiction of the States concerned. The overall position of all the States is indicated below :

States' Forces Serving with Indian Units.

	July 1939.	July 1945.	July 1947.
State Officers	747	1,317	1,307
Indian Officers	1,286	2,039	2,115
Indian Commissioned Officers .. .. .	.....	279	.....
British Other Ranks .. .. .	.....	3	.....
Viceroy's Commissioned Officers .. .. .	.....	.....	.....
Indian Other Ranks	15,622	83,348	59,702
Civilians .. .. .	.....	.....	.....
Non-combatants (enrolled)	3,966	7,004	6,695
Non-combatants (un-enrolled)	3,826	1,110	594
Recruits .. .. .	.....	2,132	.....
Boys .. .. .	.....	286	.....
	55,447	97,518	70,413

The position of a few selected States is illustrated by the table below :

States.	State Forces. Officers	Indian Forces. Officers	Indian other ranks.	Non-Combatants (Enrolled).	Non-Combatants (Unenrolled).
Hyderabad	206	279	6,621	853	40
Travancore	45	86	2,822	197	.....
Baroda	36	71	1,827	128	7
Kashmir	149	231	7,060	734	3
Mysore	74	110	2,814	409	16
Bhopal	34	47	1,558	81	..
Patiala	121	176	4,725	411	5
Gwalior	103	177	5,045	777	..
Bhawalpur	48	93	2,320	241	..
Bikaner	47	69	2,211	383	..
Jodhpur	77	110	3,070	399	..
Bhavnagar	9	16	390	101	20
Cochin	10	21	604	55	..
Jaipur	55	99	2,789	473	99

Expenditure charged to the revenues of the Government of India on account of Indian States Forces was listed in official records as hereunder :

**Expenditure Charged to Indian Revenues on Account
of States Forces.**

				Rs.
1940-41	..	..	..	22,21,000
1941-42	..	..	..	27,13,000
1942-43	..	..	..	47,68,000
1943-44	..	..	..	1,05,08,000
1944-45	..	..	..	1,44,20,000

It is clear that the special responsibility of the Governor-General to ensure the peace and tranquillity in any areas under his governance, which obviously must include the States according to the language of Constitution Act, has completely disappeared from the scene, with the proposed abolition of Paramountcy. On the other hand, items 1 and 2 of the Seventh Schedule also are inoperative for purposes of the Union Centre, because there cannot be any question of screening the Indian Forces from the organization of the defence of the Union.

Clauses 285, 286 and 287 of the Constitution Act describe the saving of rights and obligations of the Crown in its relations with the States, and lay down the basis for the use of His Majesty's Forces in connection with the discharge of the functions of the Crown in relation to the States, in addition to making arrangements for the Governors and Provincial Military Staffs to assist in the discharge of the functions of the Political Department. The discretion of the Governor-General to place armed forces at the disposal of the Crown Representative, which is another incarnation of his own personality, becomes completely inoperative, once Paramountcy is abolished and States are vested with sovereignty.

Yet, the clause relating to the utilization of the armed forces of the country for the discharge of the functions of the Crown with respect to the States is important. It was laid down that "it shall be the duty of the Governor-General, in the exercise of the executive authority of the Federation, to cause the necessary forces to be employed accordingly," though it was also provided that the net additional expense incurred in the use of these forces, for obviously putting down internal disorders in the States and for maintaining the authority of the Ruler, "shall be deemed to be expenses of His Majesty incurred in discharging the said functions of the Crown". The

implication of this provision is that the costs of maintenance of peace inside the States, which is only euphemism for the maintenance of the autocratic authority of the Rulers over their subjects, are chargeable to Indian revenues, meaning thereby the revenues of the Provinces. Additionally, there is a provision (Section 287) of the Constitution Act which arranges for assistance from Provincial Governors to the Political Department in the discharge of the functions of the Crown in the same sphere.

We agree that once Indian States become legally sovereign, they will become foreign territories, which of their own volition have to come into the Union Centre, or Pakistan. It is, however, clear to us that even though there cannot be any special responsibilities of the Governor-General of the future Indian Union or Pakistan in this regard, because the Crown ceases to exist and will be replaced by the Chief Executives of the Union and Pakistan, the maintenance of tranquillity inside the States which are members of the Union, or of Pakistan, must necessarily be on a par, both in regard to security organisation and costs, with the similar problem which assails the Provinces inside the Union. It must, however, be stated clearly that, in case the States are unwilling to place their armies under the common command of the Union Centre and be budgeted for on a uniform basis, the preservation of the tranquillity of these States cannot become a charge upon the resources of the Union. It will, thus, be seen that there is no escape from integration of the policies and finances of the Union, enveloping both the Provinces and the States.

It is not our purpose here to go into a historical description of the origin and development of the Indian States Forces, particularly those portions of these Forces which are maintained, or earmarked, for external defence under the orders of the Imperial Government. But it is necessary to distinguish between the units which are earmarked for internal security of the States, from those which are to be put at the disposal of the Imperial Government in times of national emergency. Without such a distinction it will not be possible for us to obtain a comprehensive and unified estimate of the organization of the defence of the States on the one part, and the cost of such defence to the peoples of the States concerned on the other.

In 1928, the Nind Committee estimated the expenditure of Indian States under two heads: (1) expenditure relating to Indian State Forces, both for internal security and external defence, which is the equivalent of the effective charges known to the nomenclature of the Defence Department of the Government of India; and (2) other military expenditure which cannot be classified as effective military expenditure, for it might include expenditure on the Armed Police and the State Band of an Indian Ruler! The Nind Committee's investigation results (Appendix VI of its Report) have been tabulated by us as hereunder:—

Military Expenditure of Indian States (1930)
(In Thousands of Rupees)

	Expenditure on Indian States Forces.	Other Military Expenditure.
Hyderabad	11.55	47.18
Mysore	9.19	10.17
Baroda .. .. .	.....	24.36
Gwalior	38.80	8.28
Kashmir	48.70	1.90
Central India States (Bhopal: 8.26; Indore: 18.64)	15.46	29.03
Rajputana States (Jaipur: 1.502; Jodhpur: 13.92)	48.09	22.56
Madras States .. .. .	.....	5.39
Western India States (Nawanagar: 5.03)	16.97	1.16
Bombay States	4.16	3.34
Punjab States (Patiala: 17.88)	38.03	3.39
U. P. States	10.32	2.29
Tripura	4	66
Grand Total	2,38.71	1,59.71

It may be noted that the Nind Committee, as much as other committees which investigated this question, confessed difficulty in coming up against lack of unity in the returns of all the States on matters relating to the Defence Services. As a matter of fact, the Nind Committee wrote (paragraph 57), that certain States have either deliberately, or otherwise, completely screened their activities in this regard, and that, for example, returns of Cambay, Janjira, Saut, Bhadarwa, Umetha, Jambhughoda and Akalkot, which sought to indicate that they possessed no

regular troops, had to be corrected from the returns of the Political Department.

STRENGTH AND COSTS OF STATES FORCES

We have made a reference to this discovery of the Nind Committee to endorse our earlier statement that, owing to lack of popular governance and efficiency in the vast majority of the States, it is almost next to impossible to sort out the chalk from the cheese, and to build up accurate and comparable indices, relating to such a vital question as the armed forces and retainers of Princely India. We have our misgivings that the abolition of Paramountcy, and the revesting of sovereignty with the States, would lead to a considerable expansion of the regular military forces maintained by the States, as much as the irregular forces at the disposal of the Princes. The specious plea would, no doubt, be put forward that this expansion is required for tiding over the new emergency created by the withdrawal of the British power in India, as much as the advantage that such expansion of armed forces would give the Rulers in their negotiations with the Union Centre. We confess that even the most searching scrutiny of the conditions prevailing in the States today will not give us a correct estimate of the total number of troops, both regular and irregular, available to the Princes, leave alone a correct estimate of the amount of the taxpayers' money which the Princes must spend to maintain these props of the might and sanctions behind the autocratic rule of the vast majority of the 600 odd States in the country. The Union Centre must reckon with this question of the integration of the organization of the armed forces of the States, as of the Defence expenditure of the States, with those of the Provinces, in order to bring about the essential unity of army organization and defence expenditure, without which it cannot hope to survive even a single minute after its creation.

The wildest possible ambitions have now been revived in some of the States. The Nizam, Travancore, Kashmir, Bhopal, and even Bastar, talk of their independence and their right to separate existence. There will not be any limit, for example, to the ambitions of the Nizam in this regard. The lesser fry among the States also might, as we are convinced they would,

pursue highfalutin and grandiose ideas for the revival of the glory of their ancestors, as it existed before the death of Maharaja Ranjit Singh. We cannot have a correct projection into the immediate and ultimate implication of this definite expansion of the armed Forces of States, if only to assist the Rulers concerned to keep back, as long as possible, the rising tide of the revolt of their peoples. This is the reason why we lay down the point that the Negotiating Committee of the Constituent Assembly, which is to deal with individual Princes before the States concerned are admitted entry into the Union, should make itself certain that the returns submitted by the States, especially in regard to army organisation and expenditure, are correct. Otherwise, the greatest possible danger exists to the Union Centre, in so far as it would not be possible for it to formulate schemes of merger of the Indian States Forces with those of the Union Centre, leave alone the question of allocation of expenditure, based upon a pooling of resources in common as between the Provinces and the States.

We have, with considerable difficulty, obtained information regarding the army establishments of some of the principal States in India, and the following table illustrates the position as obtaining in June 1947.

Defence Forces of Selected States

State.	Field Service Unit.	General Service Unit.	State Service Unit.	Unclassified Unit.
Kashmir	733	8,063	1,281	1,673
Bhawalpur .. .. .	....	565	....	54
Patiala	1,128	1,692	1,762	1,519
Kapurthala .. .. .	....	316	158	357
Gwalior	1,306	1,959	4,922	3,065
Rampur	159	....	1,200	120
Jaipur	157	1,099	590	927
Bikaner	926	7,408	463	540
Jodhpur	2,199	733	3,390	1,828
Bharatpur .. .. .	....	2,750	789	745
Cooch Behar .. .. .	....	....	366	57
Baroda .. .. .	....	754	3,016	281
Nawanagar .. .. .	....	....	656	39
Bhavnagar .. .. .	....	....	1,082	5
Bhopal .. .. .	....	....	....	....
Rewa .. .. .	....	....	....	....
Hyderabad	2,238	5,968	4,236	2,188
Indore .. .. .	....	400	1,600	400
Mysore .. .. .	....	790	750	716
Travancore .. .. .	....	....	1,172	467
Cochin .. .. .	....	....	615	165
Kotah .. .. .	....	318	....	....

We have attempted to make a comparison between the relative positions of the Indian States Forces of some selected States as existed respectively in January and June 1947. Two remarkable tendencies become observable from this comparison. In the first place, the effect of demobilisation, at present in full swing, was noticed. There was, for example, a reduction of 2,500 under the Unclassified Unit of Kashmir. Secondly, the effect of rearmament in the States became equally clear. The tale of Hyderabad, between January and June 1947, is of outstanding importance to us, in view of that State's decalration of independence. There was an addition of 2,188 under the Unclassified Unit of this State, an entry which did not exist in January! Comment is needless. One thing we would like to state is that these figures cannot be conclusive, though their accuracy is vouched for by States circles. At best, they are gross underestimates.

We would urge the greatest caution in accepting the statistics of States as listed above, for the additional reason that there is a tremendous amount of confusion relating to the respective strengths of the units maintained by each State. Nomenclature and classification vary from State to State, making comparison and consolidation of figures extremely difficult. Thus, while a battalion in Hyderabad represents 13 State officers, 18 Indian officers, 421 Indian other ranks and 201 non-combatants enrolled, the same in Mysore represents 2 State officers, 4 Indian officers, 105 Indian other ranks and 47 non-combatants enrolled. In other words, while in the case of the former a battalion represents a total strength of 653, one in the latter stands for 153 only. This lack of comparison also exists in the case of regiments, mountain batteries, squadrons of horse, etc.

A detailed examination of the armed forces available to some of the most prominent States is interesting to an unusual degree, in the light of re-armament which is now going on in their midst, pursuant to the impending retrocession of sovereignty by the Paramount Power. Hyderabad has one Field Service Unit, meaning thereby one light armoured regiment. Under its General Services Unit, it has one light armoured regiment, one field battery, and four battalions. One regiment (horsed), one wireless transmitting section, two battalions, one

mechanical transport company and provost detachment go to make up its State Service Units. Finally, its Unclassified Service Unit has one cavalry training centre, one military hospital, one training school, one veterinary hospital, one artillery training centre and one training school.

In the case of Gwalior, the Field Service Unit comprises one mountain battery and one battalion. Its General Service Unit is one light armoured regiment. Two regiments, two and a half battalions and seven transportation units, three training units, one wireless transmitting section, one central school, one Indian training corps one transport training unit, and two artillery sections (training) comprise its State Service Unit.

Patiala's Field Service Unit consists of one armoured regiment and one battalion. Its General Service Unit comprises of one mountain battery and three battalions. Two squadrons (horsed), and one animal and technical transport company each are under the State Service Unit. The Unclassified Unit consists of one wireless transmitting section, one training school, one military hospital, half a section of veterinary hospital, one artillery training centre, and one Indian training corps.

While figures for Bhopal are not available, Travancore, which is so much in the news with its declaration of independence, is stated to be without any Field Service Unit or General Service Unit. Its State Service Unit consists of three battalions and one wireless transmitting section. Its Unclassified Unit comprises of one Indian training corps and one training school.

We give on the next page information relating to military expenditure of some of the principal States in relation to total expenditure, according to the latest administration reports available to us.

Military Expenditure of Selected States.

(In thousands of rupees)

State.	Year.	Military Expenditure.	Total Expenditure.
Kashmir	1944-45	89,69	4,22,80
Bhawalpur	1944-45	18,17	.....
Kapurthala	1944-45	4,01	25,09
Gwalior	1942-43	.....	22
Rampur	1943-44	12,51	81,73
Jaipur	1942-43	27,16	1,44,84
Bikaner	1943-44	8,59	1,39,66
Jodhpur	1937-38	.....	1,30,86
Udaipur	1945-46	3,91	.....
Bharatpur	1944-45	4,29	64,28
Mayurbhanj	1944-45	.....	37,07
Cooch Behar	1943-44	3,19	49,28
Baroda	1944-45	27,50	3,73,78
Nawanagar	1943-44	5,02	1,08,19
Cambay	1943-44	56	10,24
Bhavnagar	1942-43	4,31	83,59
Kolhapur	1943-44	9,73	75,77
Bhopal	1941-42	.....	84,03
Hyderabad	1938-39	89,24	8,90,59
Indore	1943-44	18,27	1,91,84
Mysore	1944-45	30,00	11,22,69
Travancore	1944-45	23,48	6,11,25
Cochin	1942-43	1,99	1,44,39

We repeat, again, that information about the military, as other items of expenditure in the States is, to say the least, not satisfactory, and is generally quite inside the actual mark. We do not know what exactly it costs to the tax-payer of the States in respect of the total defence and police forces of the *durbars*. The aggregates of expenditure under all the heads must necessarily add up to considerable totals for the States. From the above figures it is clear that military expenditure in the States constitutes a considerable moiety of the budget of each *durbar*, ranging from twenty per cent in Kashmir, to ten per cent in Hyderabad, seven per cent in Baroda, under four per cent in Mysore, and under three per cent in Travancore. It is clear that these percentages are extremely deceptive, but this is all the information we have at the moment. If the effects of the costs of re-armament in the States, which is now in full swing, are taken into consideration, these percentages would certainly

shoot up, while the actual incidence of military expenditure would be infinitely higher.

We wish it were possible for us to build up a table of expenditure on defence in all the States put together. A fairly accurate projection convinces us that this expenditure could not be much less than Rs. 25 crores a year, what with the increased costs of modern armament and the general rise in the standards of pay, clothing, food, etc. of the regular soldiers of the Princes, as in the case of the Provinces. It would be extremely difficult to add up to this amount the expenditure of the States on irregular levies and police, which, to our mind, constitute, alongside of the regular forces, the vast machine of oppression which the Princes have built up, in order that their subjects are kept under leash.

STRENGTH AND COSTS OF INDIA'S DEFENCE

Now that we have obtained a fairly intelligent idea of the strength and costs of the armed forces of the States, it is necessary that it must be viewed by the side of the strength and costs of the Defence Forces of India as they exist today. The accompanying rather lengthy table illustrates the position of the Indian Army, as existed at successive stages during the preceding eight years.

Land Forces of India

	King's Commis- sioned Officers.	Indian Commis- sioned Officers.	British Other Ranks.	Viceroy's Commis- sioned Officers.	Indian Other Ranks.	Recruits.	Boys.	Civilians.	Non- comba- tants (enrolled).	Non- comba- tants (unen- rolled).	Total.
<i>July, 1939.</i>											
British Army	1,411	...	35,408	184	9,935	....	....	....	3,109	2,170	52,217
Indian Army	4,263	294	40,548	3,481	1,24,451	....	....	7,644	16,402	10,803	2,07,886
Total ..	5,674	294	75,956	3,665	1,34,386	....	....	7,644	19,511	12,973	2,60,103
<i>July, 1945</i>											
British Army	15,713	65	2,21,810	168	5,771	....	36	464	5,078	906	2,50,011
Indian Army	39,208	13,013	59,603	39,764	12,28,516	1,69,876	15,979	75,365	3,60,710	51,993	20,54,027
Total ..	54,921	13,078	2,81,413	39,932	12,34,287	1,69,876	16,015	75,829	3,65,788	52,899	23,04,038
<i>January, 1947.</i>											
British Army	2,773	31	44,767	4	217	....	24	34	470	148	48,468
Indian Army	18,563	11,345	24,879	25,572	5,90,483	24,393	6,156	41,041	1,00,731	34,042	8,77,205
Total ..	21,336	11,376	69,646	25,576	5,90,700	24,393	6,180	41,075	1,01,201	34,190	9,25,673

The position of the Air Forces of India is indicated below:

Air Forces of India

Particulars.	July 1939	July 1942	January 1947
Royal Air Force Officers	219	1,974	1,624
British Other Ranks	1,909	30,304	15,152
Royal Indian Air Force Officers ..	16	313	1,430
Indian Other Ranks	269	2,099	14,916
Civilians	205	296	5,485
Indian Technical Personnel ..	1,138	2,286	11,427
Total ..	3,756	37,272	50,034

The strength of the Indian Navy was estimated at 16,821 at the beginning of 1947.

A few comments seem called for on the statistical information so far given above on the strengths of the three units of the defence services of the country. From an overall strength of 3,000,000 at the peak of the recent world war, the Defence Services of the country have been drastically curtailed through demobilisation. From V-J Day to the end of May 1947, the net reduction in the strength of the Indian Army amounted to 1,607,531 men and women. Of these 30,161 were British and Indian Officers, 12,177 were officers and auxiliaries of the WAC(I), 44,207 were British other ranks serving with the Indian Army, and 1,499,650 were Indian other ranks, including 60,854 civilians attached to the Indian Army. In May 1947, there was a net reduction of 1,332 officers, 24,263 Indian other ranks, 7,812 Non-Combatants enrolled and 3,266 British other ranks attached to the Indian Army. During that month 25 army units were disbanded. A total of 8,313 army units had by then been disbanded, 61 Indian States Forces units had been returned to the States and 11 Nepalese Contingent units had returned to Nepal. Up to the end of May 1947, a total of 37,458 Indian States Forces personnel had returned to their States, and 9,178 Nepalese Contingent personnel had returned to Nepal. As we write, the demobilisation plans of Government are becoming exhausted, and yet we cannot say that the three Defence Services have reached strengths which become *normally requisite* to the needs of the country.

We must now take note of the costs of the Defence Services of India during the past quarter of a century, including the recent World War II. The following table gives these costs at a glance.

Twenty-Seven Years of Defence Budgets.

Year.	Crores of Rupees.	Year.	Crores of Rupees.	Capital Portion.	plus	Revenue Portion.
1921-22	69.81	1935-36	44.98			
1922-23	65.27	1936-37	45.45			
1923-24	56.23	1937-38	47.35			
1924-25	55.63	1938-39	46.18			
1925-26	56.00	1939-40	49.54			
1926-27	55.97	1940-41	73.61			
1927-28	54.79	1941-42	103.93			
1928-29	55.10	1942-43	....	49.14	..	189.75
1929-30	55.10	1943-44		37.45	..	358.40
1930-31	54.30	1944-45		59.40	..	395.43
1931-32	51.76	1945-46		35.09	..	371.76
1932-33	46.74	1946-47(R.E.)		2.00	..	266.72
1933-34	44.42	1947-48(B.E.)		....	....	204.37
1934-35	44.34					

It will be noticed that there is no possibility for us at all to compare the defence expenditure of the preceding eight years with what had happened during the previous two decades. The figure of Rs. 69.81 crores for 1921-22 definitely reflected the aftermath of World War I, and financial bankruptcy alone, after the Great Depression, secured some reduction in defence expenditure for this country. The effects of the Chatfield Recommendations for the modernisation and equipment of the Army in India came to be felt during the few years preceding World War II, while during the War itself all financial considerations were thrown to the winds, and an aggregate of some Rs. 2,500 crores of defence expenditure, not shown in full in the above table, was thrown upon the back of this country.

One interesting thing about the defence budgets of the Government of India, including those of the recent war-period, is that they speak of a "basic normal budget of Rs. 36.77 crores," for this item is always Item One of the detailed explanatory memorandum, which is issued each year with the budget statement of the Finance Member. Column two of this statement indicates the effect of rise in prices on the defence costs. Then, there is the column dealing with India's "war measures,"

which in the revised estimates for 1946-47 accounted for Rs. 178.61 crores of the total defence budget of Rs. 258.11 crores! Finally, there is the column dealing with non-effective charges, meaning thereby payments to be made in respect of the British soldiers in India. These heads complete the revenue portion of the defence budget of the country, which became separated from the capital portion in 1939-40.

The capital portion of the defence budget has certain very interesting items, dealing with the manner in which the defence services were equipped and modernised, so as to subserve as a competent war machine, which is comparable to that of any other country in the world. There are heads relating to the capital outlay on industrial expansion; air fields of air forces; air fields under Reciprocal Aid; new constructions for the Indian Navy; and capital outlay on the tele-communications scheme. In the budget statement for 1947-48, however, the manner in which the defence budgets were set forth during the war years became simplified, meaning thereby that these stratagems for confusing the public mind about the enormities of defence or war expenditure, were dropped, and a straight, unvarnished statement was given of the gross total costs of the defence services.

In passing, we must comment that the days are long since past when the country could go back to the basic normal budget of Rs. 36.77 crores. Even for the purposes of a divided India, this figure becomes meaningless, for it is clear that Pakistan alone might have to spend more than this basic figure of yore for the country as a whole, while the Indian Union may not be able to service its defence services even with Rs. 100 crores a year, assuming that this figure relates only to costs on the basis of pre-war prices. It is here that Gandhiji's recent remark about an armament war between the Indian Union and Pakistan, leave alone the rearmament of the States, obtains significance.

IMPLICATIONS OF PARTITION

An extraordinary situation has arisen as a result of the *communiqué* of the Government of India of July 1, 1947, according to which the decisions of the Partition Council have led to the division of the Defence forces of the country into those

of the Union of India and of Pakistan, with effect from August 15, 1947. It is clear that the final division of the Defence forces, which is to be on a voluntary basis, depending entirely on the individual and designated choice of the officers and men concerned, will take time. One estimate indicates that the Indian Army, meaning thereby the land forces, can be easily distinguished into 54 Hindu, 19 Muslim and 12 Sikh complete units. It is also computed that the following will be the percentages of composition according to communities.

Community.	Officers.	Other Ranks.
Hindu	47.8	55.7
Muslim	23.7	33.8
Sikh	16.3	7.5
Others	12.2	3.0
Total ..	100.0	100.0

According to the *communiqué*, (Section VI, A, B & C) the following was the method of partitioning the Defence forces of the country into those of the Indian Union and Pakistan:

“The partition of the Armed Forces will be in two stages:

“(a) The first stage will be a more or less rough and ready division of the existing forces on a communal basis. Plans should be made forthwith for the immediate movement to the Pakistan area of all Muslim majority units that may be outside that area, and similarly for the movement of India of all exclusively non-Muslim and non-Muslim majority units at present in the Pakistan area.

“(b) The next stage would be to comb out the units themselves on the basis of voluntary transfer. To this, however, there would be one exception, namely, that a Muslim from Pakistan now serving in the armed forces would not have the option to join the armed forces of the Indian Union, and similarly a non-Muslim from the rest of India now serving in the armed forces would not have the option to join the armed forces of Pakistan. There would, however, be no objection to non-Muslim personnel from Pakistan and Muslim personnel from

the rest of India electing to serve in the armed forces of the Indian Union and of Pakistan respectively.

“(e) While this reconstitution is being carried out, arrangements should be put in train to ensure that each Dominion shall have as soon as possible its own administrative machinery to enable it to maintain its own Armed Forces. It is not until these two processes have been completed that central administrative control can be dispensed with. Every effort should be made not only to complete the reconstitution of units, but also to provide each Dominion with its own administrative and maintenance services for its own Armed Forces by April 1, 1948, thus making it possible to dispense with central administrative control by that date. This, of course, does not preclude arrangements or agreements between the two Governments for sharing any administrative or training establishments.”

We have quoted the above provisions in full, for the reason that the people in this country do not clearly comprehend the inward character of the military sovereignty which the Indian Union and Pakistan become vested with, the first on paper on August 15, 1947, and in plenary fashion on April 1, 1948. We have examined with considerable care the chart, which was issued along with the *communique*, dealing with the control of the Army during the reconstitution process. There is a Joint Defence Council at the top, to which both India and Pakistan are attached, and then there is the Supreme Commander in charge of operational control of the Defence forces of both the Dominions. Under the Army Headquarters, India, there are the Eastern and Southern Commands, with General-Officers-Commanding in saddle, more or less on the basis existing before partition. Under the General-Officer-Commanding, Eastern Command Headquarters, there are area commanders in charge of General-Officers-Commanding, for Delhi and East Punjab, the U.P., Bihar and Orissa, and West Bengal and Assam area. Under the Southern Command, there are the usual divisions of Bombay, Deccan and Madras area commands. In the case of the Pakistan Army Headquarters, the area commands are those of Peshawar and Waziristan, West Punjab, Bengal or East

Pakistan Area, and Sind, each in charge of a General Officer-Commanding.*

The question naturally arises as to what happens to the Indian States, which had been attached to each of these Commands under the pre-partition dispensation? It is true that most of the States have demanded retrocession of cantonment areas, and the chances are that they would obtain the same sooner than most people expect. Taking, for example, Bangalore and Secunderabad, it is clear that the British and Indian Units of the Army in India, which used to be located there, would be withdrawn, as it is proposed to be withdrawn, by August 15, 1947, and that once this withdrawal is effected, the Princes concerned would become completely sovereign. There is a popular belief in the country, that the guns of the Residency in Secunderabad are so trained, and are of sufficient calibre, that by switching a button the palace of the Nizam, which is situated in the neighbouring city of Hyderabad, would be blown into smithereens. We confess that this popular belief is only symbolical of the power of the Paramount Power in the States, and cannot be taken literally. But it can be taken literally that division of the Armed Forces of the country, as adumbrated above, would completely destroy the only basis which kept the Princes under leash all these long years of the British occupation.

We are not clear in our minds as to what would happen to the Armed Forces of the States. It is estimated that in January 1947 there were some seventy thousand officers and other ranks belonging to the Indian States' Forces serving with Indian Units, and that automatically these units would be completely withdrawn by the Princes back into their respective

* Some of the decisions of the Partition Council of the Government of India, on the division of the defence forces between the Indian Union and Pakistan, are now known.

According to a *communiqué* issued on July 11, the Indian Union would have 15 infantry regiments, 12 armoured corps units, 18½ artillery regiments, and 61 engineering units, while Pakistan would have 8 infantry regiments, 6 armoured corps units, 8½ artillery regiments and 34 engineering units.

The division of the Air Forces could not be settled yet, but in the case of the Navy the Indian Union was allotted four sloops, viz. the *Sulaj*, the *Jumna*, the *Kistna* and the *Cauvery*, whereas Pakistan was allotted two sloops, the *Narbada* and the *Godavari*.

territories. This is a backwash of the organisational set-up of World War II, but it is clear that these forces of the States would have got to be reckoned with, in conjunction with their regular forces, which are not detailed for duty with Indian Units under the Imperial service obligations which the Princes were subject to till but yesterday. Once these lent forces are clubbed with internal units of the States, the colossal total of the armed strength of the States would be arrived at.

We consider that this is a frightening prospect indeed, and there is also the spectre of re-armament of the States in anticipation of assumption by their Rulers of complete sovereign powers, as has been repeatedly pointed out in the earlier sections of this book. How the States propose to adjust their relationships with the Indian Union and Pakistan cannot be stated now with any degree of precision, at any rate in the sphere of the defence forces. But it is clear that, once the States elect to enter the Indian Union or Pakistan, they must surrender their right to maintain standing or private armies, which must get merged into the respective military establishments of the Federation they choose to adhere to. If this is not done, on a par with the Provinces, which are their co-equal partners of the Indian Union and Pakistan, then there will be definite threats of recalcitrance, not to speak of open rebellion, especially on occasions when passions become supercharged and when Princes feel that there is a threat to their sovereignty. Such of the States which choose to remain outside the Indian Union, or Pakistan, naturally become sovereign territories, and will be treated as such.

In view of the centuries-old ties between States and Provinces under British hegemony, there will be occasions, without number, when oppression, for example inside the territories of the States, would be considered to be an unfriendly act by the people of the Provinces, and a system of hostages, not to speak of inter-statal wars, would ensue. For example, the people of the Andhra areas cannot look with equanimity at any threat to the liberties of their brethren across the border in the Nizam's territories, particularly in view of the fact that, historically, the Nizam's dominions were Andhra territory, and that sixty per cent of the people of this State are Andhra-speaking people,

who have glorious memories of Warangal and Prataparudra, who, legend has it, while a prisoner at Delhi, had outwitted Aurangzeb, even before the first Nizam-ul-mulk ever dreamt of his independence from the Mogul Emperor. We can postulate the same principle with respect to almost every other State. Actually, long pent-up dynastic and racial factors would come to the surface, and alleged violation of liberties in certain areas would constitute *câsus belli* between the States and the Provinces, and even between the States themselves *inter se*. For example, the demand for a United Kerala Province might any day throw Travancore into a conflict with Cochin, for Travancore "in terms of international law", which unfortunately does not yet apply to the States at all these days, might complain that agitators from its territory seek asylum and "foment" trouble from Ernakulam and other cities and towns in Cochin, as is the case today, and, finding redress inaccessible, might take recourse to armed intervention.

We have said enough to demonstrate the utterly fantastic position which the States might find themselves in, on the basis of their re-asserted military sovereignty, both from within the pale of the Indian Union and Pakistan, or from without. Mr. Pattom Thanu Pillai, the President of the Travancore State Congress, has set up headquarters at Ernakulam, and is directing from there the people's movement in Travancore against the *durbar*. Pandit Nehru's roving personal representative, Mr. V. K. Krishna Menon, is issuing broadsides from Madras. The Economic Adviser to the Government of India, Dr. P. J. Thomas, presided over a meeting of protest in New Delhi against the decision of the Travancore Ruler to declare independence. Surely, Travancore might elect to demand extradition of its subjects like these gentlemen, from non-Travancore territory, and might indulge in acts which would bring that State perilously near war with neighbouring territories. In any case, there might be numerous frontier incidents between Travancore and Cochin, and Travancore and the Madras Province, which might lead to armed clashes, which would be beyond the power of the ordinary police of any or all of these territories to cope with.

We consider that we are not pursuing a figment of our imagination in arguing in this manner, for we recognise the real dynamite we are dealing with in a re-vested military sovereignty of the States. The manner in which the territories of Baroda and Gwalior, to mention only States, criss-cross those of the Provinces, convinces us of the inescapable need for the surrender of military sovereignty of the States for merger into the common pool of the defence of the Indian Union. Now that the British occupation army is quitting India, and the Paramountcy of the Crown evaporates into thin air, it is clear as crystal that the Government of the Union Centre, as of Pakistan, must have the means at its disposal to ensure security within its territories, including those of the incoming States. For, otherwise, there would be a vital lacuna in the set-up of the country which would lead to the destruction of the integrity of the States, whether the State be the Indian Union or Pakistan.

SCOPE OF UNIONISED DEFENCE

It is necessary for us, at this stage, to take a peep into the probable size and costs of the Defence Services of the Indian Union, including such of the States which elect to come into it. The same general principles apply to Pakistan also. During the inter-war period the effective strength of the standing army of India was 150,000 Indians and under 50,000 Britishers. If the regular armies maintained by all the States are taken alongside of the standing army of India, this effective strength would have been somewhere in the region of 300,000 to 350,000. During the time of the recent World War, the strength of the army in India, inclusive of ancillary and subordinate services, was 3,000,000. A cross-section of the probable requirements of the future would give us an estimate of about 400,000 as the effective strength of the army of the Union, inclusive of the States. We cannot bring ourselves to believe that Pakistan proper can have an effective army of anything more than 200,000 men, unless it be that Mr. M. A. Jinnah and his co-adjutors would like to bleed white their subjects, in order that an army, say, of a million *Pakistanis* might be available for Pakistan, to vie with

the Indian Union in prowess and military strength, which clearly is an absurd proposition.

We would like to break off here from our main lines of argument, and make a brief reference to the discussions which took place at the time of the British Cabinet Mission's visit to this country in May 1946. We are given to understand that these Cabinet Ministers suggested to the leaders, on the then hoped for basis of one single Union for the country, an army of 1,000,000. This army was to be divided into three units, viz., respectively those relating to the predominantly Hindu majority area, the predominantly Muslim majority area, and the States, and that it should be divided into Union Forces and National Forces. The Union Forces were to be drawn indiscriminately from all these three units, in the proportion of 400,000 Muslim, 400,000 Hindus and 200,000 Sikhs. We would not comment here on the implications of the weightage proposed between three principal communities, from the three areas of the country as marked out by the British Cabinet Mission, but will proceed with an examination of the National Forces scheme of 1946.

The National Forces were to be designated specifically for the purpose of securing internal tranquillity, and were to have been drawn in the following proportion: the States, 50,000; Hindu majority area 100,000; and Muslim majority area 75,000, giving an *absolute maximum* of 225,000 for the country as a whole. These National Forces were to be considered as the reserves of the Union, and could be of any of the three branches of the Defence Services, viz. land, sea, and air forces. One condition for the creation of these National Forces was that they could be called upon for Union service, in consultation, of course, with the parties concerned.

The effect of these proposals can be summarised as follows, with the provision of a ten per cent dilution in the case of Sikhs in all categories:

Area.		Muslims.		Hindus.		Sikhs.	
		Union.	National.	Union.	National.	Union.	National.
States	.. ..	75,000	20,000	125,000	25,000	50,000	5,000
Muslim	.. ..	200,000	67,000	25,000	.....	75,000	7,500
Hindu	.. ..	125,000	.....	250,000	90,000	75,000	10,000
Total	..	400,000	87,500	400,000	115,000	200,000	22,500

It was stated that the above estimates were purely imaginary, and that their principal purpose was to strike *some sort of balance* between the three parties to the question of Unionisation under one government, and if that were not possible with one common defence system for two separate Unions. One interesting feature of this plan of the British Cabinet Delegation was that the Hindu area was to shoulder nine-twentieths of the costs of defence expenditure; the Muslim area six-twentieths; and the States five-twentieths.

We would like to state here clearly that the estimates which we have given of the requirements of the Indian Union and Pakistan bear out comparison with the figures given to political leaders at the time of the visit of the British Cabinet Mission. But the vital difference of the respective positions then and now is that there is no longer any need for weightage between the Muslim and the Hindu, and that the Indian Union and Pakistan would become completely sovereign in course of time, fulfilling their destiny each in its own way.

The average expenditure of the inter-war period on the standing army of India was about Rs. 50 crores. The Nind Committee estimated in 1928 that the cost of the armies of the Indian States was Rs. 4 crores, and today this head cannot be less than Rs. 20 or 30 crores. In the light of the costliness of modern defence equipment, and of the growing needs of the Defence services today (and here we steer clear of the peaks of expenditure reached during the recent seven war years), a normal defence budget of Rs. 100 crores a year might meet the requirements of the Union Centre, inclusive of the States. Pakistan may have to spend anything up to Rs. 40 or Rs. 50 crores to finance its own Defence services.

We repeat that there is no validity for these propositions, which are, however, based upon a fairly close general application of the relevant criteria available to us so far, as regards army organization and defence expenditure in the country.* Incidentally, it may also be remembered that the figures relating to expenditure in the inter-war period, given earlier in this

*In this connection, the reader's attention is drawn to Dr. Lanka Sundaram's book entitled "*India's Armies and Their Costs*," issued in 1946 by *Avanti Prakashan*, Bombay-14.

Chapter, are only for meeting the requirements of a normal peace year, in which there was neither aggression from without, nor disturbance from within, of a type which would demand the utilization of the Armed Forces for preserving the security of the country.

The effective strength of the Army of the Union, or for that matter of Pakistan, comprising of units both from the Provinces and the States, is definitely a matter which had better be left to the decision of experts. In the same manner, estimates of costs for the maintenance of Armed Forces in the Union, inclusive of the States, and in Pakistan, are also matters which largely depend upon the pre-determination of military strengths and the type of equipment which these Armies are to possess today or tomorrow. By the middle of July 1947, reports began circulating at the highest level that the defence forces of the Indian Union would necessarily be strong, and in keeping with the dignity and needs of the new State. It was suggested that the Union would take recourse to a five-year plan capable of raising forty-five squadrons of air force, and a respectable navy, which has the task of defending a coast line as long as that of the U.S.A. There were denials issued from London regarding the immediate acquisition of two cruisers by the Indian Union. But it is clear that once the British element in the Defence Forces is withdrawn, and India is removed from the military strategy of the British Empire and Commonwealth, there would be great need for the re-equipping of the Union Forces with the latest weapons, and with the requisite arms of the Air Force and Navy, in which she is bound to be deficient after partition. These arguments hold good in respect of Pakistan also. The overall impression as we write is that India, both Indian Union and Pakistan, are bound to embark upon considerable schemes of expansion and modernisation of defence services, with the result that costs are bound to be greatly augmented.

For the purposes of our enquiry, it is only necessary that we stopped at a point where agreement must be reached on only two questions: (1) that the organization, equipment and control of the Defence Forces of the Union, inclusive of the States, must be vested in the Commander-in-Chief of the

Union who, in his turn, is responsible to the Union Executive and Legislature; and (2) that the States must share Defence expenditure on an ascertained basis which is equitable in its incidence, and that the Defence budget of the Union is an integral whole. The continuance in any shape or form of the so-called military sovereignty of the States would surely become a menace to the security of the Union, as to that of Pakistan, for such sovereignty could only mean an engine of tyranny as far as peoples of the States are concerned, and a Democracies' sword hanging over the head of the Union itself. In short, the Princes cannot be permitted to blackmail the Union, either today or tomorrow, into doing things which are against the interests of the Union as a whole. There is no scope for feudalism and feudal organization in the polity of the Union Centre, or of Pakistan.

FEUDAL ARMIES INCONSISTENT WITH UNIONISATION

It is not our intention here to lay down *ex cathedra* statements belonging to the region of polemics, but we cannot afford to miss emphasising the point that till today the Princes had no need for the maintenance of these regular and irregular forces inside their territories, for a purpose other than that of keeping their people under complete subjection. We say this because the Paramount Power, under precedent and practice which had become hallowed with the march of time, always bound itself to the preservation of dynastic succession and the maintenance of the rule of every Prince within his State's territory. In all certainty, the costs of British troops, *e.g.*, in the case of the suppression of the Meo revolt in Alwar and the Sikar uprising in Jaipur only a few years ago, were paid for by the Princes concerned from out of their revenues. We have persuaded ourselves to discuss this question at some length, for the reason that, in terms of the overall defence of the Union Centre, and in keeping with the new *tempo* in public administration which is pervading every inch of territory in the Provinces, the maintenance of the Indian States Forces and other engines of oppression, specifically for the purposes of maintaining the prestige and power of the Princes, cannot be allowed to continue.

Defence Forces are intended for securing the preservation of a country's territorial integrity from attack from without, and for use on rare occasions when cataclysmic events occur internally. They cannot be used as props for any *regime* or administration. If this point is not conceded by the Princes, it is just as well that they do not come into the Union Centre. The reason is that any unequal yoking of the States to Provinces would put intolerable burdens upon the Union Executive, which has to condone, or even support, lawlessness on the part of the Princes, in their well-known effort to curtail the privileges of their peoples. In as much as the Princes are to participate in the Union Executive, it is clear that this sort of tyranny in the States cannot be allowed to continue.

In other words, the basic principle must be agreed to in advance that, if at all regular forces are needed for the purposes of administration in a State, they could be so only as a part and parcel of the general military forces available to the Union. We leave out, for the present, questions like whether these States' contingents should be recruited by the individual States, or whether they should be detachments, may be with strong local territorial colour, from the general forces of the Union. But it is clear to us that Indian States Forces cannot be allowed to function as independent units at the disposal of individual Princes, without any relation to the organization and control of the forces of the Union, under one single command and under one single administration. In other words, the forces of the Princes must become parts integral to the Defence Services of the Union. Such of the recognized Indian States Forces—and recognition must be within the competence of the Union Centre, in whose Executive the representatives of the Princes function as partners of those of the Provinces—must be under the unified command of the Commander-in-Chief for the Union, who is amenable to control on questions of policy by the Union Executive and the Union Parliament.

Again, the forces of the States, to the extent to which they are located in the territories of individual Princes, must be budgeted for in the common Defence budget of the Union Centre. Whether the States, which may be permitted to retain sections of the Union's defence forces, are to make a *pro rata*

contribution to the defence budget, with the Union authorities making payments out of the common pool, is a question which we need not discuss here at any great length. It is quite conceivable that some of the States, at any rate the bigger ones, might be permitted to make payments out of their local fises, subject, of course, to the usual credits and debits which must be there in all federal or confederal polities.

What we are emphasising here is that the States participating in the Union cannot have any separate military existence of their own. In other words, forces which are permitted within the territories of the individual States must only have one single loyalty, namely loyalty to the Union Centre, through the Commander-in-Chief of the Union. This would preclude any possible division of loyalties as between the Prince of any State and the Union Centre. Such a division of loyalties would not conduce to discipline and effective control. In addition to this, in cases of emergency a division of loyalties would bring about complete military chaos. The Union Centre must avoid at all costs the recrudescence of conditions similar to those which occurred after the death of Aurangzeb, when the *sabdalars* of the Moghal Emperor set up for themselves independent kingdoms, with the result that the Moghal dynasty could not rule the country as a whole. At a time like the present, when political tempers are frayed and when conflicting economic and political interests of individual States prevent the formation of uniform policies, it is clear that a unified military command and a unified defence budget become the pre-requisites of participation by the States in the Union.

The experience of federal constitutions in the world does not give us any clue as to the manner in which the respective sovereignties of the Princes on the one part and of the Union Centre on the other, in the military sphere in particular, can be reconciled on a basis other than that of integration. We are aware of the outcry of protest which is likely to issue from Princely quarters to any suggestion of this character, but it is clear to us as day light that the continuance with the Princes of military rights will prove to be the Achilles' Heel of the Union. To carry the point a little further, the Union Centre would be bringing in, so to speak, a Trojan horse within the

gates, if the States are allowed entry within its framework, with the recognised right to maintain private levies of regular and irregular troops, over which the Union Centre is not to have any control at all.

One pertinent reason why there should be unity, both operational and budgetary, in the administration of the Defence Services of the Union, is that with the abolition of Paramountcy, which involves the abolition of the Political Department and the Residencies, there would be no chance for the issue of requisitions to the Princes in Defence matters. We consider that the creation of an Indian States Department in the Government of India, in charge of Sardar Vallabhbhai Patel, does not meet squarely the situation arising out of the abolition of the Crown Department which it seeks to replace. The Crown Department has the mighty support of the military strength of Britain behind it. The new Union Government is shorn of any such might, and is actually surrounded by hostile Pakistan territories to the East and the West, besides facing the opposition of the Princes who would carry the fight to the last ditch, in order that their sovereignty is preserved.

This is the reason why the Defence Member of the Union, as much as the Commander-in-Chief of the Union, must have directional control over policy and operations respectively, as much as that the Finance Member of the Union must have budgetary control of such of the Indian States Forces which are permitted to be located in individual States. In other words, the ukase of the Union Centre must prevail in the States in all defence matters. However unpleasant it might seem to the Rulers, it is clear that there is no escape from the overall implication of this proposition. This dictum naturally holds good in the case of the possible merger of States with Pakistan.

We have not set before ourselves the task of laying down the limits of army organization and defence expenditure in the Indian Union or in Pakistan, for such an enquiry is a matter for technical experts. We, however, feel called upon to discuss a few salient features of the army organization and defence expenditure of the Union, and of Pakistan, specifically including the States, at any rate in the Indian Union.

In this atomic age, it is absurd to lay down ceilings for the strengths of armies or of defence expenditure, for they have the aspect of a runaway horse, which cannot be brought under reins in any country. With the phenomenal changes in army tactics, and the daily discovery of more and more deadly weapons, whose costs cannot at all be calculated in advance, it is clear that our projection into the Defence Services of the Indian Union, or of Pakistan, can only be illustrative.

We have reached the stage where the two essential points involved in the integration of armies of the States, which are members of Union, with the armies of the Union proper are established beyond all shadow of doubt. In the first place, there must be organizational unity, including unity of command of the Defence Forces available to the component parts of the Union, or even of Pakistan. Secondly, there must be budgetary unity in so far as expenditure on military forces, by the component parts of the Union which, for our present purposes, are synonymous with the States only (for the Provinces cannot maintain, under the Constitution, separate defence forces), is concerned. This budgetary unity can be contrived in either of the two ways. Firstly, if forces are to be retained in individual States, even under the general organisational set-up of the Defence Forces of the Union as a whole, the States concerned can be asked to defray the costs involved, for which they will get a credit in the accounts of the Union Centre. On the other hand, the States can be asked to make a block contribution, which is previously estimated to be necessary for the servicing of these forces, and then the Union Centre might re-allocate that money to the State in question. There cannot be any escape from either of these two alternatives.

We say this because of a very valid reason. Defence Services are maintained in any country specifically for the purpose of meeting possible aggression from without, in addition to coping with civil commotion, which the ordinary police might not be in a position to bring under control. It is sheer nonsense to expect the Union Centre to meet aggression from without, or a revolution from within, if it is to depend upon contingents placed at its disposal, voluntarily for the time being, or on specific request to those States which are members of the Union.

The old parallel of Imperial Services Troops maintained by the States, under treaties of sub-infeudation or under subsidiary alliances with the Paramount Power, cannot be pressed into argument at the present stage. The reason is that, once they come into the Union, the States surrender their sovereignty, though to the extent specified in the Instrument of Accession of the Ruler concerned.

The Union Centre cannot be brought to the level of the Paramount Power of yesterday, because it does not, in the first place, exercise control over the States members in the manner in which the Paramount Power exercised control, and cannot, for that matter, petition for assistance, in the name of a King who disappears from the scene, to the States in times of war. Whichever way one looks at the problem, it is clear that, if only for purposes of meeting effectively external aggression, the defence services of the Union, as also must be the case with those of Pakistan, must possess organizational unity and control, besides a common budget which has got to be specifically arrived at with respect to the existing position of the armies of the individual States, as also of the needs of the Union of today and tomorrow.

NEED FOR TERRITORIAL ARMY

Once the principle is admitted that the maintenance of the armies of by the Rulers cannot be, as it should not be, for the purpose of coercing their people into submission—and this is the goal which the Union Centre will have before itself—it is clear that the maintenance of feudal armies by the States is incompatible with the time spirit prevailing today or with the needs of the community as a whole. In this atomic age, any justification which the Princes had in the old days for maintaining regular and irregular armies, and that vast mass of loose rabbles of pikemen which is always available to support Princely dignity, is completely obliterated. With the phenomenal changes which are daily taking place in the sphere of warfare and with the mounting number of new and costly weapons without which a modern army machine cannot hope to function as an efficient unit, it is clear as crystal that these feudal armies of the Princes are completely out of place. The Defence budget of the Union will necessarily be larger than it

ever was in peace-time, and the resources of any of the States, even including Hyderabad, will not be sufficient to meet modern requirements, unless it be that the estate of the community is rack-rented and the people are bled white, a proposition which is clearly untenable today.

We feel, however, that for the Defence budget of the Union Centre,—and this proposition holds good in the general interest of Pakistan—regular expenditure on the maintenance of armed services should be kept as low as is possible, even in terms of modern technical warfare. In other words, the size of the regular Armed Forces, including the Army, the Navy and Air Force, should be kept within reasonable limits, for no standing army in the world today can possibly shoulder the responsibilities involved in atomic warfare, and no standing army of sufficient strength can be maintained even by such a powerfully organised industrial State like the U.S.A.

In order, however, that the essential requirements of security of the country are met, there should be, in addition to a standing army of reasonable proportions, a territorial army which will inculcate in the people a sense of obligation towards the country. It was only recently that Britain instituted conscription in peace time, for even today the war-time emergency of the preceding ten years has not passed and, with far-flung commitments the world over, Britain had perforce to maintain an army of considerable proportions. But British history gives the students of world affairs one very important lesson. It is that the organisation of a territorial army, based upon the principle of voluntary service, supplies the second line of defence, which is far more important for insuring security, than even a standing army.

In India, so far, this principle of territorial army, as one of the essential ingredients of military policy, has not been even the thought of. Commanders-in-Chief have consistently rejected suggestions of this character in all these two centuries of British occupation. Instead, the army in India had been kept on the basis of a mercenary army of rice soldiers doing duty by Britain, both within our own territorial limits and in overseas areas. Such, indeed, was the case both in war and peace, during the long rule of Britain over this hapless land.

The future army of India cannot be based upon this principle of mercenary services. In fact, the future army of India must be a People's Army, but even such an army cannot be merely a standing army of reasonable proportions, the emphasis for our purpose being a recognition of the duty of the people to service in the Army Forces of the country. There will certainly be a career in the standing army of India for both officers and ranks, but such a career would be subordinate to the national requirements of the Union.

We have already indicated certain dangers of the continuance of a possible division of loyalties on the part of Army Forces as between Indian Rulers on the one part, and the Union Centre on the other. We will certainly have no objection to the State, alongside of the Provinces, creating and maintaining local corps for a territorial army for the Union, within the framework of a standing or national army, to serve as second line of defence for the Union. The institution of a territorial army, with the provision of local corps in the States, is likely to whet the appetite of the Princes, in that they will not be deprived of uniformed people for demonstrational purposes, and at the same time will have ensured the security of the Union, in so far as the contingents from the States to the territorial armies would also function under a unified command in times of national emergency.

Obviously, the costs involved in the raising of State contingents to the territorial army of the Union must be borne by the States themselves. The principles behind the University Training Corps, which we have been familiar with in this country during the past thirty years, must also become applicable to the territorial armies of the Union. It is now a question of the citizen's recognition of an obligation to defend his own country, with or without emoluments befitting such a career. Standing armies have no meaning in these days of total war, where it is the man-in-the-street who ultimately has to fight for his own survival and for the survival of his country, at a time when atom bombs hurtle down from immeasurable heights, which, like Death the Leveller, do not make any distinction between 'strips of khaki' and the 'common home-spun' on the backs of people.

DANGER FROM ZAHAROFFS

The question of supply of arms and ammunition for the Regular Forces and Police of the States is bound to assume dangerous proportions after the abolition of Paramountcy, if it is not tackled well in advance of the deadline for the inauguration of the Indian Union and of Pakistan as sovereign States. The present position is that almost every one of the States depends upon the General Headquarters and the Ordinance establishments of India for the supply of arms and equipment for their Regular Forces and Police. Indents are normally sent to the Political Department of the requirements of the individual States in this regard, which are scrutinised before submission for issue by the General Headquarters.

Occasions are known when the States could not even vouch for the accuracy of the requirements thus submitted. Occasions are also known when issues were delayed, sometimes for unreasonably long periods. It is also known that some of the individual Rulers, who failed to obtain their requirements in the appropriate manner, tried to indulge in private negotiations in New Delhi, which, however, were known to have not yielded the required results. It is a recognised principle, as far as the States are concerned, that they cannot be allowed to maintain and operate private armament factories, and they must justify that their so-called requirements, both for the Regular Forces and Police, of arms and equipment are legitimate and within reasonable bounds.

We shudder to think of the consequences of the unfettered right of the States, on the abolition of Paramountcy, to establish armament factories. For one thing, the financial burdens involved might as well cripple the resources of the States concerned, and might assist the Rulers in becoming tyrants. For another, the security of the Union, as well as of Pakistan, would be put in permanent jeopardy, if every one of these 582 princes are allowed to indulge in an armaments race, in order that their power and prestige in the eyes of their own people, as well as in comparison with neighbouring Princes, might be enhanced, through the maintenance of large regular defence forces and police fully equipped with modern armaments.

The question has been mooted whether on the abolition of Paramountcy the States are not to be enabled to import armaments and equipment for their regular forces and police from overseas countries. We consider that such an eventuality would certainly bring chaos in the *regime* of military administration which must envelop the country as a whole, and that it would assuredly lead to potential civil war (perhaps we should say a series of inter-statal wars), as between the States *inter se*, as well as between the States on the one part and the Union Centre and Pakistan on the other.

The terrific potentialities of the right of the States like Hyderabad, Travancore, Bhopal, etc. to import arms and ammunition from abroad cannot be exaggerated. Already the cry has gone up that Britain, even in advance of quitting India, is seeking military asylum in some of the prominent States. We are not in a position to substantiate the truth of allegations of this character, but we cannot afford to refuse to take note of prevailing fears in the country in this regard. We have known of situations like the progress of the Nizam in the recruitment of Pathans and Arabs in his State into regular, as well as irregular and private, armies of his own. We dare to say that a similar situation is likely to arise, if it has not already arisen, in some of the principal States of the country.*

A projection into the future, on the basis of indices available to us today, makes us feel that the right of the States to import arms and equipment from abroad would lead the country into a situation which China, under that disastrous *regime* of War Lords which preceded the Japanese invasion of Manchuria in 1931, had experienced. Additional to this certain danger to the security of the country and the weal of the community from War Lords setting themselves in trade in some of the principal States, there is the greater risk of the country being divided, in the military sphere, between Hindu and Muslim States. We have already seen the dawn of such a political alignment of States into Hindu and Muslim, in order that the politics of the Union Centre *versus* Pakistan might be buttressed on either

* Since we wrote the above, the All-India States' Peoples' Conference, at its session in New Delhi in June 1947, issued a public warning about rearmament in the States. The resolution concerned is printed at page 10 of this book as a footnote.

side with some pretence to purposiveness. Rampur alone is an exception to this statement. No sane-minded person in this country can view with equanimity the emergence of conditions in which the States, by and large, are to be set up as independent kingdoms, with the unfettered right to indulge in an armament race, thus leading to financial bankruptcy and the wasting of the seed of the community in civil or inter-statal wars.

It is from this angle of approach that we come to laying down the proposition that there must be integral military unity of the Union, inclusive of the States, as well as the integral unity of Pakistan on the same showing. The potential threat to the peace of the country, as we know now, from a possible military clash as between Pakistan and the Union Centre is fully recognised. In fact, the demand for Pakistan, which has now become an actuality, is based on the principle of hostages. Mr. Jinnah claims that, if the 40,000,000 Muslims left behind in Hindustan are not treated properly, he will have at least 17,000,000 Hindus in Pakistan, who could be pounced upon for the purpose of securing "good behaviour" on the part of Hindustan.

We have already adverted to the possibility of the creation of a Muslim Chamber of Princes, as a counter-blast to the certain adhesion of the majority of Hindu States to the Union Centre. Long pent-up dynastic hatreds would assuredly come to the surface, and the turbid history of India, of the past 1,000 years or more, would be thrown into the cauldron, in order that the descendants of the former Hindu, Muslim, Mahratta and Sikh Rulers might sing *hosanna* in the name of their departed ancestors. No greater catastrophe can befall the country, even if it were to have two independent States, than this attempt to revive tribal glories, which had better be buried in the limbo of the past. This is a proposition which is not a figment of our imagination, but a reality of stark realities.

Under no circumstances can the States be permitted to set up arsenals and ordnance factories, with the right to manufacture arms and equipment, leave alone the right to import arms and equipment from abroad. There will be dozens of Zaharoffs who will be willing to indulge in gun-running to assist those Princes who are anxious to invest their coming sovereignty with flesh and blood. In the electrical international situation which pre-

vails today, Princes might as well become pawns in the hands of competing world powers. The attempt of the U.S.A. to send a trade mission to Nepal, and to establish a Legation in that kingdom, has been characterised by Moscow as a foretaste of the coming economic and military imperialism of Americans in India. The establishment of an American Consulate in Hyderabad, as is now projected, falls into the same category of developments facing the country. If Travancore becomes independent, the Thorium deposits of that State might as well supply the cockpit for international intrigue, for whoever has access to this basic ingredient of the atom bomb controls the East.

We need not further pursue this trend of thought, but we have said enough to indicate the fatal consequences of the right of States to military independence. This is where we feel that the country has been sadly let down by the British. For two centuries the British have "controlled", at all events to subserve their imperial purposes in our midst, this heterogeneous mass of States. The tragedy is that even before they quit India, as they propose to quit, they are now providing unfettered discretion to States to indulge in an armaments war, the consequences of which would be to stab the Union Centre, as well as Pakistan, in the back.

Geography is a greater pre-disposing factor of the polity of India today than of any other country in the world. The territories of the Princes are so mercilessly criss-crossed with those of the Provinces, that no individual unit can extricate itself from out of the mesh. And, yet, it is proposed to make the Princes sovereign in every aspect of the term. The preponderating majority of the States are landlocked, and are hemmed in by the territories of the Provinces. There need not be any *agents provocateurs* to create *câsus belli* between the States on the one part and the Provinces on the other, whether it be with reference to the Indian Union or Pakistan. We have already indicated the thousand and one ways in which fiscal and economic questions alone are bound to prejudice the continuance of cordial relations between the States on the one part, and the two independent Governments in the country on the other. The situation which already subsists between the States on the one part, and the Union Centre and Pakistan on the other, is ex-

plosive enough, without the assistance of a re-vested military sovereignty on the part of the Princes. The people of the States are grappling with their liberties, and clashes are imminent between them and their Rulers. The peoples of the Provinces cannot remain mute when this struggle for freedom between States obtains a spearhead, for the quitting of the British from India is only the consummation of the struggle for freedom of the Provinces, and there cannot be any black patches on the map of India, where tyranny rides strident. Once the Rulers of the States are permitted to raise armies and equipment, without any reference to the Union Centre, or even of Pakistan, then the distressing pattern of war-torn China will reproduce itself in our midst sooner than most people expect.

Every true patriot in the country must deplore the recrudescence of the situation in which the armies of the Indian Union are marched against Bhopal, or for that matter, the armies of Western Pakistan engage themselves in pitched battles with those of Kashmir. Perhaps, a more pertinent illustration would be the potential danger to peace and security of India from the Nizam cutting up this sub-continent into two. It will be a sad day for India as we know it now, as our forebears knew it before, when anarchy overtakes us, and when national and territorial armies, including those of some 600 Indian Princes, plunge themselves, without reckoning, into the battle-field. Surely, this is a negation of governance, and surely this is not the settlement which India had expected from Britain, after two centuries of the rule of the successors to Lord Clive.

CHAPTER VI

RECONSTRUCTION FINANCE

“Central Planning in our opinion implies some degree of central control. We may arrive at a common plan by voluntary agreement between Provinces and States, but there must then be some means of enforcing it. The obvious means is through legislation. In the case of the Provinces, central legislation is possible, if the development of those industries, which are to be the subject of central planning, is brought by law under the control of the Central Government. This can be done under the existing constitution, and we strongly recommend that it should be done. It is impossible, as things stand at present, for the Central Government to legislate for the Indian States. It will be necessary therefore to get them to enact analogous legislation by agreement. The main purpose of the proposed legislation would be to ensure that, in the field selected for central control, no new factory should be started or an existing one continued or expanded without a licence.”

*- Report of the Advisory Planning Board. (Neogy Report),
Paragraph 53.*

OBJECTIVES OF NATIONAL PLANNING— DEVELOPMENT EXPENDITURE IN STATES PROVINCIAL DEVELOPMENT PLANS—PUBLIC DEBT AND STERLING RESOURCES—BORROW- ING AND AUDIT—TARGETS OF RECONSTRUC- TION FINANCE.

The Reconstruction Committee of Council, in its second Report on Reconstruction Planning, postulated (page 12 of Second Report) an all-India plan in respect of post-war reconstruction and development as a whole; a detailed five-year plan for the Indian Provinces for Central subjects including finance; a detailed five-year plan prepared by each Province in respect of its own subjects, also including finance; and a detailed five-year plan prepared by each State of suitable size in respect of all subjects, including finance.

While dove-tailing the above, the Reconstruction Committee postulated that the Centre would have a seven-fold responsibility in respect of planning for the country as a whole, as follows: initiation of plans and policies for those questions for which the Centre is responsible, elaborating them in detail if necessary in consultation with Provinces and States; provision for expert advice to Provinces and States, in order to ensure a common policy on important questions; provision for interchange of information and possibly of technical advice between Provinces and States; co-ordination of plans and priorities;

provision of financial advice and assistance, where considered justifiable or necessary; provision for assistance in respect of procurement of plant or technical staff; and co-ordination of scientific research and experiment, expert technical investigations, training of technicians etc.

The Reconstruction Committee described the *role* of the Centre in the following manner: "It is implicit in nation-wide planning that the needs and requirements of all co-operating regions should be viewed as a whole, and it follows, therefore, that the Centre must have authority to initiate projects and to make arrangements for getting them executed, where the interests of several Governments are affected, if such projects cannot be taken up by individual governments. For instance, in the matter of erosion, action is to be taken at the source of the trouble, while the benefit may accrue to an area far removed from the source. In such a case, the Centre must initiate action at the source of the trouble, while arrangements may be made for the apportionment of expenditure between the Provinces which carry out the work and the beneficiary Provinces. Another instance is of measures designed to control the diseases of plants and animals. In order to prevent the spread of diseases, it may be necessary to initiate control measures in one area, in order to protect the neighbouring areas. Further instances of a similar nature are large-scale land reclamation schemes, or large-scale afforestation schemes, and the co-ordination of research."

It was also stated by the Reconstruction Committee that the Centre must accept responsibility for providing an increased measure of expert advice, equipment and finance to the Provinces. If the required expenditure is beyond the resources of the Provinces, the Centre may have to provide financial assistance of a suitable scale. The means by which funds will be raised, and the basis on which financial assistance will be given to the Provinces, are matters for detailed examination, but the general policy, in the view of the Reconstruction Committee of Council, in respect of the obligation to render financial assistance regarding approved projects, is tacitly accepted by the Government of India.

We consider that, at the time when the Reconstruction Committee of Council reported, the question of the immediate functioning of the States in a unionised polity and economy, with a recognised Centre, could not be anticipated along with the plethora of its implications, and we hold that, on this account alone, the Reconstruction Committee could not project beyond its nose, and see the terrific importance of the extension of this principle of financial aid to the States as well in the unionised economies of the Indian Union or Pakistan. Now that the Indian Union and Pakistan are coming into existence, and the States, after a standstill period, are perforce to be linked in one form or another to these two sovereign entities, it is clear that these two respective Centres, in relation to their satellite States, must have the same attitude as the one recommended by the Reconstruction Committee of Council with respect to the Provinces.

OBJECTIVES OF NATIONAL PLANNING

The National Planning Committee had for its objective the Karachi Congress Resolution of 1930, which stated that "the State shall own and control key industries and services, mineral resources, railways, waterways, shipping, and other means of public transport." To achieve this programme, the National Planning Committee laid down that planned advance has to be measured by certain tests from year to year. These tests include the improvement of nutrition from the standard of an irreducible minimum of proteins, carbohydrates and minerals, ranging from 2,400 calories to 2,800 calories per adult worker. The doubling of the *per capita* cloth ration from 15 yards to 30 yards a year, and a housing standard to reach at least 100 sq. ft. per capita, were also declared as the essential ingredients of this programme. These criteria naturally include increases in agricultural and industrial production, diminution of unemployment, increase of *per capita* income, liquidation of illiteracy, increase in public utility services, provision of medical aid on the basis of one health unit for 1,000 of population, and the increase in the average expectation of life.

The following two quotations from the Report of the National Planning Committee suffice to indicate the principles

which should animate national endeavour today and tomorrow: "The principal objective of planning the national economy should be to attain, as far as possible, national self-sufficiency, and not primarily for the purpose of foreign markets. This does not exclude international trade which should be encouraged, but with a view to avoid economic imperialism. The first charge on the country's produce—agricultural and industrial,—should be to meet the domestic needs of food supply, raw materials and manufactured goods. But outlets for surplus goods may be explored to meet the requirements of India's international indebtedness." "Planning under a democratic system must be defined as technical co-ordination, by disinterested experts, of consumption, production, investment, trade and income distribution, in accordance with social objectives set up by bodies representative of the nation. Such planning is not only to be considered from the point of view of economics and the raising of the standard of living, but must include cultural and spiritual values, and the human side of life."

The National Planning Committee had, for reconstruction and development purposes, divided industries into four categories:

Defence Industries: Fire arms (land, air and marine) and their parts; munitions; cartridges, explosives, shells, torpedoes, etc.; and tanks and armoured cars, and other forms of mechanical equipment, especially designed for military purposes.

Key Industries: Hydro and thermal power (generator); fuel, coal and fuel wood, mineral oil, power alcohol and natural gases; metals, ferrous and important non-ferrous, including the winning of ore for them; industries for the making of machine tools; and industries for the making of machinery and machinery parts.

Public Utilities: Distribution of electricity, gas and other forms of energy; public transport and communication services; warships of all types, including submarines; military aircraft of all kinds; gases for warfare and gas masks (warships and military aircraft can also be made in ordinary peace-time establishments); heavy engineering industries for the building of ships, locomotives, wagons, automobiles, aircraft (vital); in-

struments and apparatus—commercial, industrial and scientific (standards); chemicals, heavy chemicals, fine chemicals including dyes (some vital), fertilisers and refractories; and water supply. Banking and insurance were reserved for consideration later by the Committee.

Cottage Industries: Textiles (silk, wool and cotton), cotton spinning and weaving especially up to 30s.; dyeing and calico printing; cotton ginning and cleaning for hand spinning, except pressing; oil crushing; soap and toilet articles; furniture and timber works; paper for use as stationery (except paper for newspapers, art printing, for wrapping and packing, etc.); sugar; rice husking and milling; brass, copper and silverware; tallow, guts and glue; tanning and shoe making; pottery and ceramics; glass and bangles; beads; polishes, paints and varnishes; locksmithy, nails; blacksmithy, cutlery; hemp, coir and rope; bristles and fibres; bricks; tiles; gold and silver threads; salt; toys; umbrellas; gums, resins; matches; carts; countrycraft; tailoring; embroidery; hosiery; buttons; carpets, confectionery; fruit preserves and syrups: and dairying.

No scheme of planning and development can have meaning, without concentration on the development of industry in the country. In the case of India, with the existing bewildering gap between agriculture and industry, the emphasis on industrial development is bound to continue for a long time to come. In fact, one of the left-wing charges against the Bombay plan was that the suggested expenditure of Rs. 10,000 crores over a period of 15 years was intended, by and large, only for development of industries, meaning thereby an increase of production, without any adequate thought bestowed upon distribution and social justice.

This is not a treatise on political and economic theory, and we need not get embroiled in the controversy relating to the existence, or the lack of it, of a broad basis for any or all of the plans, both official and non-official, for reconstruction and finance, which have been issued during the past seven or eight years in the country. It is, however, clear that the fact must be stated beyond any shadow of doubt, that planning and development, without forgetting the social objective, viz., to enable the people to reach higher standards of living and comfort,

must necessarily concentrate upon the creation of economy for the country *as a whole*, which is self-sufficient in character. Self-sufficiency becomes meaningless in India, unless agriculture and industry are yoked together as two equal partners to the economic activity of the people. Indeed, one-sided economic development has kept India as an *El Dorado* for the exploitation of the industrialised West. Such a thing cannot continue, now that National Governments are in saddle in both the Indian Union and Pakistan. It is from this angle, that we consider that a brief examination must be made of industrial development in India, in relation to the projected development programme and reconstruction finance.

Planning and development must proceed on a basis which is pre-determined, in order that industrial dispersion takes place in the land on a scientific basis. In these days of total and global wars, concentration of industry in any particular area cannot be considered to be in the national interest, and strategic and security considerations alone demand that the industry should be located, dispersed and even camouflaged, in order that it escapes attack in the event of war.

Apart from this question of the military security of the free Indian Union, the problem must be recognised that there cannot be any undue concentration of industry in any particular area. For example, there has been a huge outcry in the country that the sugar industry has been completely concentrated in the U.P. and Bihar; that the textile industry has been localised in Bombay and Ahmedabad; that steel is a virtual monopoly of Bihar; and that the jute manufacturing industry is entirely in the grip of Calcutta. Ever since discriminating protection became the official policy of the Government of India, twenty-five years ago, a sedulous rearguard action has been fought by the areas which are unrepresented in industry, to see that there is a wider degree of dispersion thereof, and that undue bottlenecks of industry are avoided in any part of the country. Partition of Pakistan from India proper has proved the validity of these arguments, at a cost which Mr. Jinnah alone knows!

For example, more and more sugar mills are being started all over the country, traversing north Madras, Hyderabad,

Bombay, and even the Punjab. This is as it should be, and the same principle holds good with respect to every other industry in the land. The urgency of a properly planned location of industry becomes evident, in the light of the gigantic plans of reconstruction now projected by the Government of India, the Provincial Governments and the State Governments. The following is a statement relating to industrial location in India and the distinction between different territories has been drawn by us, in order to show clearly how the resources of the Indian Union, Pakistan and the States, in respect of industrial production, stand marshalled today.

Industrial Location in India

	<i>Indian Union.</i>	<i>Pakistan.</i>	<i>States.</i>
Cotton Mills	671	9	62
Iron and Steel Factories	17	Nil	1
Engineering Workshops	369	45	26 (Including 4 in Hyderabad and 1 in Gwalior).
Jute Mills	106	Nil	1
Sugar Mills	149	4	13 (Including 1 in Hyderabad and 2 in U. P. States.)
Woollen Mills	14	2	8
Silk Factories	66	2	25 (Including 3 in Hyderabad)
Paper Mills	14	Nil	8
Match Factories ..	80	5	28 (Including 10 in Hyderabad and 1 in Gwalior).
Chemical Factories ..	29	2	7
Glass Factories ..	71	2	6 (Including 2 in Hyderabad)
Soap Factories	16	1	9 (Including 2 in Hyderabad)
Cement Factories ..	10	3	6 (Including 1 in Hyderabad and 1 in Gwalior.)

We consider that in any scheme of reconstruction, the respective interests of the Indian Union, and Pakistan, and the re-

relationships of States which are contiguous to both these sovereign entities, must have proper weightage given to each. With the exaggerated emphasis, which has now come into evidence, of local or territorial patriotism, it is obvious that no overall plan of reconstruction and development for the country as a whole will have legs to stand upon, unless the aspirations of the peoples concentrated in defined areas (meaning thereby those of Provinces and States,—and even of linguistic groups like the Andhras, the Kannadigas and the Maharashtrians) are dealt with adequately and justly. The days of monopoly of business activity either by the Marwari or Gujarati community are definitely over. The right to development is a fundamental human right, and includes definitely the right to industrial development in all the areas of the country, in and outside the Indian Union, on a basis which is comprehensive and equitable.

DEVELOPMENT EXPENDITURE IN STATES

An examination of the financial resources of the 532 States in the country today shows that not more than a dozen have an income of Rs. 1 crore and over. There are less than ten States with incomes ranging from Rs. 50 lakhs to Rs. 1 crore. The balance of 550 States have only incomes of less than Rs. 50 lakhs a year. It is estimated that of the 90,000,000 people in the States over 60 per cent are in the first dozen major States. The total income of the States was computed at about Rs. 60 crores a year, and the vast majority of them have an income of less than Rs. 1 lakh a year.

It is obvious that, by and large, the resources of the States, barring perhaps the first dozen, are not sufficient for the inauguration of planning and development programmes on their own individual responsibility. It is quite likely that States like Hyderabad, Mysore, Travancore, Baroda and Gwalior may embark upon programmes on their own initiative, and yet it is clear to us that even Hyderabad and Travancore must come to the Centre for financial and other assistance, if their reconstruction programmes are to yield any dividend within a measurable distance of time. The principle of Central subvention to the States thus becomes more and more insistent, as the affairs of the Indian Union become straightened out. This principle

remains valid even in the case of those States whose planning and development programmes do not get interlocked with those of neighbouring Provinces.

From an organisational point of view, the Indian Union must recognise the point that planning becomes of necessity a correlated subject, enveloping both Provinces and States which are its members. For example, it is unthinkable that States and Provinces concerned can undertake hydro-electric projects in isolation. The harnessing of rivers, and the generation of electric power therefrom, in the case of Hyderabad and Gwalior, for example, would bring in quite a good number of Provinces and other States into the picture. We have similar experience in the case of the Bhakra Dam and the Lloyd Barrage Scheme of the inter-war period. The Ganga Canal of Bikaner, and the problem of conservation of rivers passing through the Rampur State and flanking the Tehri-Garhwal State, belong to the same category of questions. It is unthinkable that the development of Bastar, which has declared its independence on paper, can take place without any reference to the fortunes of the Central Provinces and Orissa on the one part, and Hyderabad on the other. Thus, it is too late for any one to plead for the rejection of co-ordination in planning and development. The existence even today of wartime controls regarding capital issues and on dismantling, moving and erection of factories, and of export and import restrictions both on seaborne and land traffic, constitutes a warning to the States, that they cannot hope to survive in isolation in the economic sphere. Even in the fields of crop planning, rural finance, forest conservation, etc. there must be an inevitable link up between the States and Provinces under the *aegis* of the Centre. In any case, the overriding consideration of finance for reconstruction purposes compels States and Provinces to function together in an integrated system of activity.

We are convinced that there cannot be any scope at all either in the Indian Union or Pakistan for the declaration of Munroe Doctrines in the economic sphere, which are calculated to guarantee isolationism and unrelated economic and financial activity in the States, whether they remain completely independent, or as reluctant partners in these two Unions. The

Ramapadasagara Scheme of Rs. 86 crores, relating to the conservation and reclamation of the Godavari River, cannot conceivably be financed by the Province of Madras, the Government of Hyderabad State or even the Centre, in isolation from each other. Such colossal amounts on multi-purpose schemes demand the pooling not only of the revenue resources of all the parties, but also their credit, saddling the future generations with the costs of present activity, which is calculated to increase productive effort and living standards. In our approach to these problems, we have declined to distinguish between what are loosely designated as nation-building activities and development or reconstruction plans proper, as are available in the records of the Government of India, the Provinces and the States. Our decision is based on the fact that financial distinction is not feasible between these categories of expenditure, while not infrequently these two categories of expenditure overlap and interlock with each other.

Nation-building activities and plans for development and reconstruction in the vast majority of the States are not generally understood by students of the economic problems of India. We cannot, however, be surprised at the lack of adequate information relating to nation-building activities in the States, if only for the reason that such of the legislatures which exist in a few of the States have not yet annexed to themselves sovereign functions, while in the vast majority of the rest there is no basis at all for bringing the pressure of popular opinion to bear upon the administration of the *durbars* concerned. As long as autocracy rules the roost in the States, it is clear that the welfare of the community could not have a premium put upon it, both in terms of policy and administrative action.

We have, however, built up the table on next page of percentages of expenditure on nation-building activities in some of the principal States:

Expenditure on Nation-Building Activities in Selected States

States	Year	Percentage of total
Kashmir	1944-45	18.1
Kapurthala	1944-45	18.0
Jaipur	1942-43	9.7
Rampur	1943-44	18.5
Udaipur	1945-46	12.0
Kolhapur	1943-44	15.9
Cooch-Bihar	1943-44	10.6
Bhavnagar	1942-43	11.8
Bikaner	1943-44	10.6
Nawanagar	1943-44	2.0
Indore	1943-44	12.4
Baroda	1942-43	21.0
Mayurbhanj	1944-45	12.2
Cambay	1943-44	20.0
Bharatpur	1944-45	8.1
Mysore	1944-45	11.9
Travancore	1944-45	15.8
Cochin	1942-43	22.7
Hyderabad	1938-39	19.6

Statistics can prove anything, and the percentages given above might almost lead an unwary student into the impression that all is well in the States in the field of nation-building activities, and that these percentages stand comparison with similar percentages relating to activities in the Provinces.

Going back to our key tables of Chapter II, we would like to invest the statistics of percentages given above with some sort of flesh and blood, in order that a more live picture of conditions in the States is made available. In the case of Kashmir, out of an expenditure of Rs. 423 lakhs, the amount spent on education was Rs. 34 lakhs, that on co-operation Rs. 1½ lakhs, and that on commerce and industry Rs. 24 lakhs, while public works accounted for Rs. 19 lakhs and communications Rs. 36 lakhs. Compared to these moieties of expenditure, the civil list of the Ruler was stated to be Rs. 23 lakhs. As regards Hyderabad, out of an expenditure of Rs. 9 crores, education accounted for Rs. 94 lakhs, co-operation Rs. 5 lakhs, commerce and industry Rs. 4 lakhs, communications Rs. 79 lakhs and public works Rs. 15 lakhs. In Mysore, out of a revenue of Rs. 11 crores, education accounted for Rs. 84 lakhs, co-operation Rs. 2 lakhs, communications Rs. 40 lakhs and public works Rs. 50 lakhs. Travancore's

budget of Rs. 70 lakhs on education, out of a total expenditure of Rs. 6 crores, is something exceptionally good, but the expenditure on co-operation was only Rs. 1 lakh, that on communications Rs. 60 lakhs, and that on public works Rs. 5 lakhs. Cochin follows Travancore with Rs. 21 lakhs on education, out of a total budget of Rs. 144 lakhs, while expenditure on co-operation was only Rs. 32,000. Communications in this State had absorbed Rs. 21 lakhs, and public works Rs. 13 lakhs.

We believe that further detailed examination of expenditure on nation-building activities in the States need not be pursued here, apart from stating that in recent years most of the States have undertaken programmes of industrial and commercial development, in order that their resources are improved, and concurrently, that standards of living of the people are also improved. The following table is an index of the projected plans of industrial development, in some of the States, through extension of cheap electrical power (Neogy Report p. 82) :

Hydro-Electric Schemes in States

(Installed capacity of generating plant in Kilowatts)

State	As in January 1946		By end of 1950.	By end of 1955 or later
Hyderabad ..	13,051	(a) Nizamsagar Hydro-electric Power Station ..	15,000	....
		(b) New Thermal Station in Godavari Area at Ramagundam	37,500	....
Kashmir ..	4,270	Sind Valley Project ..	6,000	9,000
Mysore	61,000	(a) Jog Falls Scheme ..	120,000	....
		(b) Mekadatu Falls ..	....	22,500
Travancore ..	16,947	Pallivasal Scheme Extension	22,500	72,250
Cochin	2,919	Poringalkutheu Scheme ..	18,000	28,500
Other States ..	48,459	.....	4,800	67,000
			228,800	199,250

It is next to impossible to obtain adequate information on the post-war reconstruction plans of every State, though it is more than probable that almost every State has, on paper at any rate and definitely with a view to pleasing the Political Department, plans of some sort for reconstruction and development. We have been unable to obtain comparable plans for each State, and yet we have got to look into the effort made by some of the States in the realm of reconstruction.

The latest administration reports of States which are available to us, however, give a glimpse of reconstructional activities in some of the States, which we propose to analyse below. In the case of Mysore, for example, a Post-War Reconstruction Officer was appointed in the middle of 1945 to investigate the position and report. As regards Bahawalpur, a Post-war Reconstruction Committee started functioning in the cold weather of 1944, and *one hundred* schemes were prepared on a five-year basis! These schemes include all branches of State activity, such as extension of the irrigation system and the opening up of new land, land drainage, agricultural reforms, seed supply depots, roads, civil and veterinary hospitals, extension and improvement of educational institutions, model town schemes, construction of buildings, extension of State railways, water and electric supply in towns, motor transport, afforestation, and establishment of major and minor industries. The capital cost of the Bahawalpur schemes was estimated at Rs. 4 crores, and the recurring cost at the end of the five-year period at Rs. 90 lakhs. A reserve fund, with an annual instalment of Rs. 15 lakhs, was sanctioned during 1944, in order to meet part of the cost of the scheme.

We have been fortunate in obtaining a rather elaborate account of reconstructional activity in Baroda. In this State, seven committees began work in April 1943, as follows: Resettlement and Re-employment Committee; Transport, including Railways, Committee; Electric Power, Water Supply and Irrigation Committee; Trade and Industry Committee; Agricultural Policy Committee; and Disposals, Contracts and Government Purchases Committee (which was, however, discontinued after a time). In October 1944 a Ministry of Reconstruction

was created in the State, and the various Committees and Departments completed their plans for the first five to ten years.

An examination of the projects of the Baroda Government is extremely interesting. As regards education, a ten-year plan offering greater diversity in secondary and higher education was drawn up, under which pre-primary education was to be provided for all, with a school in every town with a population of 5,000. Primary education, secondary education, technical education, higher education and physical education received treatment separately, and it was estimated that over a 10-year period the capital expenditure would be Rs. 99.8 lakhs in the first year, sliding down to Rs. 14.20 lakhs in the tenth year. Under communications, it was projected, at a cost of Rs. 54 lakhs, to lay down 58 miles of narrow gauge and 24 miles of metre gauge railways, additional to the existing railway system. The road plan has a target of doubling the road mileage in the State, at an estimated cost of Rs. 440 lakhs in the first five years. Four hundred and fifty miles of additional telegraphs and telephones, with a capital cost of Rs. 19 lakhs and a maintenance cost of Rs. 1.8 lakhs a year, were also planned.

Under the head irrigation, two major projects were taken in hand in Baroda. The Zankhari River Project (Rs. 1.35 lakhs) is expected to irrigate 37,000 *bighas*, and is to be completed during the first five years of this plan. The Sabarmati project, at a more ambitious cost of Rs. 156 lakhs, is to be taken up in the second five-years slab of the reconstruction programme. Minor irrigation schemes at a cost of Rs. 26 lakhs, and the electrification of the Zankhari and the Sabarmati projects at a cost of Rs. 62 lakhs, are also indicated. Extension of the tube well system at a cost of Rs. 76 lakhs, and a vast scheme of open-well construction at a cost of Rs. 46 lakhs are laid down. The intensification of the present agricultural and animal husbandry activity in the State, at an estimated gross capital cost of Rs. 51 lakhs, with Rs. 56.7 lakhs recurring, is to be taken in hand for the first five-year period. Under the head co-operation, it is proposed to start 585 multi-purpose societies at a cost of Rs. 3.25 lakhs in the first five years. As regards industries, Baroda projected the construction of four ships at a cost of Rs. 54 lakhs, in addition to the installation of about a dozen new factories.

The total cost in the first five years of the Baroda plan is estimated at Rs. 10 crores. In 1942-43 a post-war reconstruction fund, with an initial grant of Rs. 30 lakhs, was started, with accretions of Rs. 84 lakhs in 1943-44, and Rs. 12 lakhs in 1945-46, making a total of Rs. 126 lakhs available for reconstruction finance.

We consider that it would not serve any useful purpose if a further detailed examination of the reconstruction plans available so far in some of the States is made here. The above description of the Baroda Plan is sufficient for our present purposes. The most gratifying thing about the Baroda Plan is that out of an estimated total of Rs. 10 crores for the first five years, only Rs. 126 lakhs were assembled together during the four financial years 1942-43 to 1945-46. Details are not available as to the manner in which these funds were raised for reconstruction purposes, but our impression must be valid that these funds were created out of revenue surpluses. This is a very encouraging feature of the finances of Baroda, and, as we will argue later in this Chapter, no State would normally resort to deficit finance. What strikes us most as vitally valid is the fact that no State can obtain the required reconstruction finance through loans from its own subjects, or for that matter through loans from the open stock markets in India.

This is the reason why we hold that reconstruction finance must, by and large, depend upon public borrowing, and such borrowing can only be done through the agency of the Centre. In other words, without Central subvention, reconstruction finance for the States, in particular, cannot be carried on to the extent desired, and with the speed necessary, for the execution of the plans involved. Since the presumption is there that the vast majority of reconstruction plans will not be unremunerative, it is clear that some sort of a self-liquidating provision in Central subventions to the States must become operative, even at the very outset. Even assuming that some of the States will be unable to pay back the money borrowed from the Centre, it is clear to us that there should be joint responsibility, both on the part of the States and of the Provinces, for shouldering the burdens of the Indian Union, on the principle that each of the Units is responsible for the weal of the rest. We consider

that the analogy of the Niemeyer Award grants and subventions to Provinces, under which the Centre underwrote the financial stability for Provinces, like Sind, Orissa, the N.W.F.P., Assam, and the U.P. becomes automatically applicable to the States.

PROVINCIAL DEVELOPMENT PLANS

A detailed examination of the proportion of nation-building expenditure to the general expenditure of each of the eleven Provinces in India, becomes necessary at this stage. Under nation-building expenditure are mentioned, as noticed by us earlier in this chapter, the following heads: Education; Medical; Public Health; Irrigation Works; Agriculture; Veterinary; Co-operation and Industries; and these heads are, more or less, uniform for all the Provinces in India. The following table illustrates the general percentages of nation-building expenditure to the total expenditure in each Province, during the preceding three years:—

Percentages of Provincial Expenditure on Nation-Building Activities to total Expenditure.

Province.	1944-45	1945-46 (R.E.)	1946-47 (B. E.)
Madras	20	22	29
Bombay	16	26	24
Bengal	17	27	22
Punjab	22	23	20
U. P.	28	20	21
Bihar	23	23	20
C. P. .. .. .	..	17	21
Sind	15	16	19
Assam	21	27	17
Orissa	9	12	14
N. W. F. P.	21	19	13

Expressed in terms of percentages, it is clear that we would not get an adequate idea as to the inwardness of the reconstruction and development programmes of each of the Provinces. There are also special features in the case of the individual Provinces which have got to be noticed. For example, in Madras irrigational works are given a prominence which most of the other Provinces do not give, and in the case of the U. P. rural

development becomes an impressively essential item of development or nation-building work. Otherwise, the main heads are almost identical in the case of all the Provinces.

In almost every one of the provincial budgets for the years 1944-45 to 1946-47, expenditure on education rose from Rs. 238 lakhs to Rs. 294 lakhs; in Madras from Rs. 366 lakhs to Rs. 580 lakhs; in Bengal from Rs. 259 lakhs to Rs. 328 lakhs, in the Punjab from Rs. 221 lakhs to Rs. 267 lakhs; in the United Provinces from Rs. 251 lakhs to Rs. 319 lakhs; in Bihar from Rs. 83 lakhs to Rs. 94 lakhs; in the Central Provinces from Rs. 70 lakhs to Rs. 97 lakhs; in Sind from Rs. 49 lakhs to Rs. 64 lakhs; in Assam from Rs. 51 lakhs to Rs. 63 lakhs; in Orissa from Rs. 32 lakhs to Rs. 53 lakhs; and in the North-West Frontier Province from Rs. 28 lakhs to Rs. 32 lakhs.

This phenomenal rise in expenditure on education is not available in the case of expenditure on medical relief and public health in all the Provinces, barring perhaps a few Provinces like Madras, Bengal and the Punjab. There are comfortable increases in expenditure on the co-operative movement in almost all the Provinces. Agricultural development has also received commendable attention on the part of Provincial governments, and in the case of the U.P., this expenditure was increased by over Rs. 1 crore between the years 1944-45 and 1946-47.

It is slightly difficult to distinguish one item of expenditure from another in the category belonging to nation-building activities, and to declare, with precision, that they constitute elements in the reconstruction and development programme of India. It is not necessary for our purpose here to pursue a supercilious and technical enquiry into the ingredients of reconstruction and development in any country. Nor is it necessary for us to try to demonstrate the overall importance of the fact that the education of the community would have an indelible impress upon the progress of the country, for skills, whether general or technical, acquired by the people, as a result of the initiative of the State, would certainly contribute to the toning up of the community, and that we must take into specific consideration this particular item of the provincial lists of expenditure in the sphere of nation-building activities.

The following is a consolidated statement of expenditure on industries in the Provinces:

Provincial Expenditure on Industries.
(In Lakhs of Rupees)

Province.	1944-45 (Accounts)	1945-46 (R. E.)	1946-47 (B. E.)
Bombay	15	21	33
Madras	65	80	96
Bengal	61	84	129
Punjab	31	36	40
U. P.	129	84	77
Bihar	34	27	21
C. P. .. .. .	..	..	..
Sind	2	3	5
Assam	3	4	4
Orissa	14	12	9
N. W. F. P.	1	1	1

The above are round figures, and in the case of the North-West Frontier Province, there was a decline of expenditure on industries by more than Rs. 30,000 in the years 1945-46 and 1946-47, as compared to 1944-45. It will be noticed that in the U.P. there was a precipitate decline in expenditure on industries, while in the case of Bihar and Orissa, the declines are conspicuous.

No one can over-emphasise the place of industrial development in any programme of reconstruction in India, but it is clear that almost all the programmes of industrial development taken in hand by Provincial governments have so far been in the region of cottage and medium scale industries. In view of the widespread belief in the Gandhian ethic, that the resuscitation of the rural assets of the land is a primary charge upon the State, this emphasis on the development of cottage and medium scale industries has come into being in this country during the past few decades in particular. With Congress Ministries in power in the vast majority of the Provinces of the land, it is natural that this emphasis has been adhered to in all programmes of reconstruction and development. In the case of Madras, as a typical example, the distribution of hydro-electric power to small and medium-scale industries has yielded an exceptionally good dividend, in terms of an increase in productive output, in

the wages bill, and in the general standard of life of the community in the Province. Again, Madras gives us an illustration of the manner in which irrigational works are taken in hand, as an essential ingredient of development and reconstruction policy.

According to the Neogy Report (page 72), the following multi-purpose projects were taken in hand during 1945-46:

Hydro-Electric Projects.

Name of Project.	Irrigation (In acres.)	Electric Power (In kilowatts.)
The Tungabhadra Project	300,000	120,000
The Mahanadi Project	2,500,000	200,000
The Damodar Valley Project	800,000	300,000
The Kosi River Project	3,000,000 (In Nepal & Bihar)	1,000,000
The Rihand Dam Project	Not known.	250,000

The following is a consolidated statement of provincial expenditure on five-year plans, (Neogy Report, page 71) according to the estimates of 1945-46:

Finance of Provincial Five-Year Plans.

(In crores of rupees)

Province	Total Expenditure.	Grants from Centre.	Provincial Funds.	Balance to be met from Provincial Loans	Estimated portion of loans which will be unproductive.
Madras	129	42	47.5	39.5	24.5
Bombay (1)	53	17.7	25	10.2	5.2
Bengal (2)	159	69	9.7	80.3	43
U. P.	108	47	31.5	29.5	6
Punjab (3)	116	24	34	58	6
Bihar	76	31	12	33	22
C. P.	31	14	13	4	2
Assam (4)	26.5	11.5	3	12	5
Orissa (5)	34	10	2.2	20.7	8.4
Sind	44	3.9	15	25.1	18
Total, excluding N. W. F. P. ..	776.5	270.1	192.9	312.4	140.1

(1) Total cost of plan will probably be increased to at least Rs. 60 crores.

(2) Has been warned that proposed expenditure appears to be beyond its resources.

(3) Has recently intimated that Provincial funds etc. may be only Rs. 2.6 crores instead of Rs. 3.4 crores.

(4) Wishes to increase expenditure by Rs. 16 crores.

(5) Government of India have suggested that a total expenditure of Rs. 26 crores will be more within Orissa's resources.

From the above table it will be seen that, out of a total of Rs. 777 crores of expenditure on Provincial Five-Year Plans, as much as Rs. 270 crores were derived from grants from the Central Government, and only Rs. 193 crores obtained from provincial resources, the balance of Rs. 312 crores being made up from provincial loans. Another aspect of this problem is that as much as Rs. 140 crores were sought to be expended on unproductive expenditure, normally expended from out of loans.

It will be seen that Central grants to Provinces for financing five-year plans are pivotal in character, and that without those grants it will be next to impossible for the Provinces to embark upon the schemes on hand. It is also clear that it would be outside the limits of provincial resources to supply funds from current revenue, for financing these plans of reconstruction and development. The overall impression of provincial finance on reconstruction and development seems to be that, as years roll by and as programmes become comprehensive and all-pervading, loan finance will come to occupy a *role* with implications which cannot be accurately anticipated today.

In other words, the fortunes of the future generations have got to be mortgaged today, in order that they might derive the benefit from activity of the present, which is calculated to raise the productive capacity of the country and the living standards of the community. Even under popular ministries, the financial policy of the Provinces has been one of orthodoxy and circumspection. The fears which the enemies of India sought to create, that popular government in the country would lead to rack-renting and bankruptcy, have been completely allayed by the results achieved from Provincial Autonomy since 1937. We venture to express the opinion that even larger recourse to loan finance, as the principal ingredient of reconstruction finance, would not lead popular ministries, both in the Provinces and at the Centre, into plunging the country into wasteful expendi-

ture, or even unnecessary expenditure, which has the effect of ultimately breaking the back of the community. If the experience of the recent past is any guidance, we are clear in our minds that reconstruction finance would not spiral to dizzy heights, but would definitely be within bounds of practical accomplishment.

The accompanying comprehensive statement on Provincial five-year plans is illustrative of the ramifications of reconstruction finance:

Estimated Costs of Provincial Five-Year Plans and Proposed Distribution of Expenditure, 1945-46
(In Lakhs of Rupees).

Heading.	Madras.	Bombay.	Bengal.	U.P.	Punjab.	Bihar.	C. P. and Berar.	Assam.	Orissa.	Sind.	Total.
Agriculture:	8,01	6,31	24,45	9,49	5,44	8,87	2,35	1,43	2,66	8,58	77,59
Agriculture ..	1,67	61	4,65	1,56	1,55	2,31	84	31	67	17	14,34
Veterinary & Live-stock ..	1,62	51	2,70	84	2,00	36	68	52	11	..	9,34
Forests ..	93	7	1,05	72	2	24	..	..	..	..	3,72
Fisheries ..	..	65	4,17	1,05	1,59	21	19	2,12	89	14	11,01
Co-operation ..	37	..	3	..	82	..	..	80	3,09	1,77	6,88
Rural Uplift ..	..	..	..	..	..	..	..	..	..	..	..
Total ..	12,60	8,15	37,05	13,66	11,42	11,99	4,06	5,18	7,65	11,12	122,88
Industries ..	2,44	67	3,74	2,86	5,00	2,74	7	75	2,10	27	20,64
Education ..	30,67	3,39	9,44	12,69	10,00	9,05	11,64	1,09	4,86	45	93,28
Health ..	14,08	4,62	22,58	18,32	11,99	9,55	4,49	7,51	2,00	4,15	90,38
Roads ..	20,77	20,80	23,54	30,72	12,49	13,60	7,00	5,32	4,00	8,83	146,89
Irrigation & Waterways ..	28,10	5,75	35,92	3,81	40,31	11,72	..	..	1,33	16,24	143,18
Electric Power ..	11,10	6,91	..	17,99	8,84	9,17	2,00	5,00	4,22	1,32	66,55
Miscellaneous ..	9,64	2,51	22,41	7,88	16,22	8,10	1,34	1,63	7,57	1,35	83,65
(Other public works, propaganda, mining, ports, administrations, buildings, re-settlement etc.) ..	..	..	..	..	..	..	..	..	..	..	..
Grand Total ..	129,40	52,80	159,48	107,93	116,27	75,92	30,60	26,48	33,82	43,75	776,45

According to the Neogy Report (pp. 68ff), Provincial reconstruction plans have been divided under twelve heads: irrigation; electric power; roads; ports; agriculture; veterinary and live stock; forests; fisheries; co-operation; industries; education; and medical and public health. In all these plans the suggestion that, in addition to attempting to attain general progress throughout a province, it would be better to follow 'the "concentrated area principle" has not been fully pursued. Still, it can be said that they have been drafted more or less on the lines indicated in the model draft of the Bombay Government.

Irrigation: The total expenditure for irrigation and waterways has been estimated at Rs. 143,18 lakhs, of which the Punjab will spend Rs. 40,31 lakhs; Bengal, Rs. 35,92 lakhs; Madras, Rs. 28,10 lakhs; Sind, Rs. 16,24 lakhs; and the remaining provinces, Rs. 22,61 lakhs.

Electric Power: All provinces have drafted plans for increasing the supply of electric power, and the total estimated cost would be nearly Rs. 66½ crores, or 8.7 per cent of the total developmental expenditure. It is estimated that by the end of 1950 an additional capacity of nearly 980,000 kw. would be installed.

Roads: Roads have been classified under two heads: national highways, Rs. 36 crores, and provincial, district and village roads, Rs. 147 crores, making a total of Rs. 183 crores. The expenditure on national highways will be met entirely by the central government, and the work will be executed by the provincial public works departments. The largest new construction of national highways will be undertaken in Bihar, the Punjab, and Bengal—260 miles, 110 miles and 100 miles respectively. The remaining Provinces are to concentrate on the development of the present national highways. In the case of the States, it is estimated that 264 miles of new national highways would be constructed, and 2,613 miles of the present national highways would be developed. The proposed expenditure, on provincial, district and village roads is nearly Rs. 147 crores, or 18.5 per cent of the total expenditure. During the first five-year period new construction of provincial highways and district roads would be about 17,509 miles, and the improvement of existing ones about 33,393 miles. About 29,990

miles of village roads are to be constructed or improved in the first five years.

Ports: Madras proposes to provide for an expenditure of Rs. 3.4 crores on development of ports, and on the construction of the Rameswaram Ship Canal. Orissa has only a comparatively minor scheme for developing the port of Chandbali.

Agriculture: Nearly Rs. 123 crores, or 16 per cent of the total expenditure of the provincial plans, is proposed to be devoted to agriculture and kindred subjects, i.e., animal husbandry, forestry, fisheries, etc. The actual percentages vary from 10 per cent each in the case of Madras and the Punjab, to 25 per cent in the case of Sind.

Veterinary and Live-stock: Provincial schemes are estimated to cost in all about Rs. 14½ crores. Bengal and Bihar propose to spend the largest sums, viz., Rs. 4.65 crores and Rs. 2.31 crores respectively. The schemes of the Provinces are broadly similar in character, and have provided for, firstly, the establishment of livestock breeding and demonstration farms; secondly, dairy and poultry development and wool production; thirdly, veterinary training and research; and, fourthly, construction and improvement of veterinary hospitals and dispensaries.

Forests: All the provinces have schemes for forest development, and they are estimated to cost Rs. 9½ crores, or 1.2 per cent of the total provincial expenditure. Bengal, the Punjab and Madras postulate the largest sums viz., Rs 2.7 crores, Rs. 2.0 crores, and Rs. 1.6 crores respectively. It is expected that quite a number of these forest schemes are estimated to be self-financing over a period of years.

Fisheries: With a view to developing India's fisheries, considerable amounts of money will have to be spent on training, research and experimentation. It is thought that the expenditure required will be beyond the resources of any individual Province. It is estimated that with the exception of the C. P., all Provinces have drawn up schemes at a cost of nearly Rs. 4 crores, of which Rs. 1.2 crores will be spent on marine fisheries.

Co-operation: All the Provinces have visualised the enormous importance of co-operative societies for bettering the economic life of India, and the expenditure proposed to be spent

under this head reaches the magnificent total of Rs. 11 crores. The plans provide for not only the expansion of credit facilities, but also the expansion of the co-operative principle for consolidation of holdings, marketing of produce, management of village forests, etc.

Industries: The Provincial Governments (excluding N.W.F.P.) have proposed to spend an aggregate of about Rs. 20.6 crores on schemes relating to provision of technical training and the development of cottage and small-scale industries, since the Central government have undertaken to plan the development of major industries. This represents 3 per cent of the total expenditure. Broadly speaking, as the Neogy Report says (page 91), about Rs. 11.0 crores will be devoted to technical training, and the rest to cottage and small-scale industries and to industrial research. The Punjab and Bengal propose to spend the largest sums *viz.*, Rs. 5 crores and Rs. 3.7 crores respectively. Sind and the C. P. have allotted very meagre amounts, *viz.*, Rs. 27 lakhs and Rs. 7 lakhs.

Education: The aggregate amount of money spent for education by all the provinces is about Rs. 93 crores, which is roughly 12 per cent of the total. The plans are based on the Sargent Report, with variations to suit individual provincial considerations. The Neogy Report (page 93) says: "Lack of trained teachers, no less than lack of finance, prevent the immediate introduction of compulsory free primary education for all. Provinces, therefore, necessarily plan to proceed gradually."

Medical and Public Health: The total expenditure estimated to be spent under this head by all the provinces is about Rs. 99 crores, which is roughly 12.6 per cent of the total expenditure, and the individual expenditure extends from 10 per cent to 17 per cent of their total expenditure.

The table on the next page indicates the consolidated position of Central and Provincial five-year plans, and the basis of financing the same:

Costs of Central and Provincial Five-Year Plans.

(In crores of rupees).

Subject	Central	Provincial	Total
Productive Schemes (a)			
Electrical development }	50 (b)	67 } 143 }	260
Irrigation			
Post and Telegraphs	56	....	56
Railways	230	....	230
Total ..	336	210	546
Other Schemes			
Industrial Development	15 (c)	21 (d)	36
Agriculture (including kindred subjects)	22	123	145
Roads	39	147	186
Education	21	93	114
Medical & Public Health (including Water supply and Drainage.)	12	99	111
Civil Aviation	25	....	25
Meteorology	5	....	5
Broadcasting	4	....	4
Miscellaneous (other public works, propaganda, mining, ports, administrative buildings, resettlement, etc.) (e)	40	83	123
Total ..	183	566	749
Grand Total ..	519	776	1,295

(a) Some of these schemes are not entirely self-financing.

(b) Estimated expenditure on certain regional projects. The division of the expenditure between the various administrations concerned has not yet been settled.

(c) Sindri Fertilizer Factory and Hindustan Aircraft.

(d) Mainly industrial training and development of cottage industries,

(e) Includes Labour—Rs. 20 crores, and Geological Survey—Rs. 2 crores.

PUBLIC DEBT AND STERLING RESOURCES.

The liabilities and assets of the country, in relation to the needs of reconstruction finances, must be examined, before we can establish the feasibility of the schemes on hand. According to the latest estimates of the Government of India, the public debt of the country, in so far as the Centre is responsible, was as follows:

Indebtedness of Centre.
(In Rupees)

<i>Details</i>	1945-46 (Accounts)	1946-47 (R.F.)	1947-48 (B.E.)
Permanent Debt ..	335,43,12,000	375,09,05,000	150,00,00,000
Floating Debt. ..	279,89,12,000	412,49,09,000	306,60,00,000
Funded Debt. ..	123,14,06,000	133,70,53,000	138,01,07,000
Total ..	788,46,30,000	921,28,67,000	594,61,07,000

As a corollary to the above, we give below, for ready reference, the debt position of the provinces.

Indebtedness of Provinces.
(In Lakhs of Rupees, on March 31, 1947.)

Province	Due to the Government of India.	Due to public.	Total.
Madras	3,56	11,50	15,06
Bombay	15,90	10,49	26,40
Bengal	4,48	22,01	26,48
U. P.	17,30	12,92	30,22
Punjab	12,44	19,08	31,52
Bihar .. .. .	.....	.....	.....
C. P. & Berar	2,31	2,73	5,04
Assam .. .. .	.....	3,50	3,50
N. W. F. P. .. .. .	.....	57	57
Orissa .. .. .	.....	22	22
Sind	1,86	1,66	3,52
Total ..	57,86	84,68	142,54

We regret that we are unable to obtain any satisfactory information relating to the indebtedness of even some of the principal States, for such information would have been of inestimable value to us in our inquiry.

The structure of the public debt of India, which is indicated above in round figures, affords food for thought, as to the manner in which re-construction finance of the future is definitely linked up with the resources available to the Government on the one part, and the debt obligations, whose implications cannot be escaped, on the other. Under the permanent debt of the Centre is included, in all the three estimates given

above, the First Development Loan (1970-75) of over Rs. 115 crores. The Second Victory Loan (1959-61) of over Rs. 108 crores is also included in this category. We have analysed the items covered by these loans under "permanent debt", and we find that the vast majority of these come in course of payment within a maximum period of twenty years from the date of inauguration of the Indian Union and Pakistan. Other items under this head relate to interest-free prize bonds interest-free defence bonds, etc.

Under the head "Floating Debt", treasury bills occupy the preponderating position. The securities issued to the International Monetary Fund and the International Bank for Reconstruction and Development, were shown as Rs. 139.4 crores in the revised estimates of 1946-47, and Rs. 6.6 crores in the budget estimates of 1946-47.

Under the head "Unfunded Debt", the principal ingredient is supplied by the Post Office Savings Bank deposits, which varied from Rs. 76 crores in 1945-46 and Rs. 95.5 crores in the budget estimates for 1947-48. National Savings Certificates supply the next important item under this head, varying between Rs. 23 crores and Rs. 24 crores during the same years. The State Provident Funds come next, ranging between Rs. 13 crores and Rs. 12 crores respectively. Post Office Cash certificates, Defence Savings Bank Deposits, Deposits of Service Funds, etc. bring up the rear under this head.

It is abundantly clear that in the field of reconstruction finance, loans are bound to play an increasingly important *role* than ever before in the fiscal history of this country. We have the endorsement of the Neogy Committee for this statement of ours. The Committee wrote (paragraph 18): "It is clear that a very large proportion of the funds required for development purposes will have to be raised by internal borrowing; but the possibility of external borrowing should also be kept in mind, so far as this is compatible with the preservation of national economic freedom". We have indicated already the extent of the financial implications of planning both in respect of the Centre, the Provinces and the States. It is certain that the Government of the Indian Union cannot possibly adopt the suggestion made in the Bombay Plan of "created money" for the

purpose of making possible these plans for the Centre and the unionised Units, for such a course would be fatal to the financial structure and stability of the country. The Neogy Committee fought shy (paragraph 19) of this question, and merely spoke of the need for the continuance of "the liberal expansionist financial policy" so far pursued by the Government of India in regard to development.

We hold that it is unthinkable that fiat money would supply the major grist to the mill of reconstruction finance. There may be extraordinary spending in all spheres to enable plans of economic development and reconstruction taking place, but this *natural process of expansion* of currency is nothing compared to the "created money" of the Bombay plan. We also hold that the existing level of currency in the land is already proving to be economically suicidal, and, that, if we do not misread the signs of the times, we are slowly and imperceptibly heading towards controlled deflation. When the bottom of deflation would be reached, we cannot predict at the moment. But we can confidently predict that, inside of five years, this inevitable process of deflation would find its mark. It is at that stage that the spending policies of the Union Centre, the Provinces and the States are likely to lead to an expansion of currency, in the fashion known to us since 1939, leading to the liberal and expansionist financial policy advocated by the Neogy Committee. But, we repeat again, the rise and fall in the currency curves, bearing upon the volume of employment and public spending, cannot, by any stretch of the imagination, be called "created money". It is, however, clear that loan finances cannot be avoided either today or tomorrow, if reconstruction programmes, which are intended to bring about an increasing *per capita* income and a betterment of the standard of life and living of the community, are to be made possible.

We must now examine the character and import of the currency resources of the country, meaning ultimately thereby the spending power in the hands of the community and the Government. At the end of June 1947, the sterling holdings of the Reserve Bank were of the order of Rs. 1,566 crores. As we write, negotiations are taking place in London between the officials of the Government of India on the one part, and the

British Treasury on the other, as regards the manner in which the sterling holdings of the country will be treated after the July 15, 1947, which was the deadline for the specific operation of the clauses of the Anglo-American Loan of 1944 regarding the convertibility of sterling into dollar. This will not be an appropriate place for a long discussion of the origin, growth and ultimate implications of India's sterling resources in London, but it is clear that in any scheme of reconstruction finance, as much as of trade and commerce for the country as a whole (including both the Indian Union and Pakistan), the inescapable grip of our sterling assets in London over our financial activity cannot be minimised.

Sterling had accrued to this country during the war period from the goods and services supplied by us to the British and other Allied Governments at prices which, even on the showing of a Select Committee of the British Parliament, were far below those paid by our civilian community. In other words, the sterling which has so far accrued to us represents only a modicum of the ultimate financial value of the goods and services delivered to the British Government from out of our controlled markets, and only after the greatest possible amount of privation on the part of the people. Mr. Winston Churchill's statement regarding "blood, sweat, toil and tears" applies to India more appropriately than to any other country in the world, if only for the reason that the economy of the land was mercilessly saddled to the chariot wheels of Britain, by a Government which, during the war period, did not have any roots in the will of the people. We say this for one reason, that when the final settlement of the sterling balances is to be arrived at, there would not be any disposition on the part of the representatives of this country to agree to their scaling down, leave alone repudiation,

The plea has been put forward on the part of Britain that the accrual of the sterling in London was almost immoral, and that India had derived greater benefits from the protecting arm of British military prowess, than what she had paid into the common pool which made victory possible. As against this demand for scaling the down of sterling balances, it is time that we in this country put forward counter-claims on Britain. We

have attempted to work out figures relating to this counter-claims of India, and we have arrived at the staggering total of Rs. 6,000 crores which Britain should, in addition to sterling balances, pay to us. This colossal figure has been arrived at on the basis of calculations relating to the cost of three million deaths of starvation at Rs. 400 crores (on the basis of the figures supplied by the Woodhead Commission); the loss of shipping assets at Rs. 8 crores; the cost of damage to property from enemy action Rs. 20 crores; and depreciation on railways Rs. 125 crores, roads Rs. 60 crores, motor vehicles Rs. 40 crores, and industries in general Rs. 400 crores. Then, there is the overall burden of defence expenditure of Rs. 2,500 crores, which has been saddled on the tax-payer of this country since war broke out. Railway expenditure for war purposes was estimated at Rs. 100 crores. The gross additions to centrally incurred civil expenditure arising out of war was Rs. 150 crores. Food and famine cost us Rs. 50 crores, and the Provincial governments spent Rs. 60 crores on civil defence. There are many other items which go into this figure of Rs. 6,000 crores, but we need not pursue this point here any further.

India must get back her sterling in London, for without it the stability of our national currency will be completely destroyed, in as much as sterling today supplies the preponderating portion of the backing to our note issue. Additional to this, without the recovery of sterling, whether it be in terms of goods and services exported to us from Britain, or in terms of repayment in sterling and gold as such, which would enable us to have access to international currency, particularly dollar, it would be impossible for us to secure a revival of our trade, leave alone the question of financing our reconstruction programme through purchases of capital goods from abroad.

The acquisition of sterling assets, meaning thereby the accrual in London of sterling as a backing to the note issue in India, by the Reserve Bank varied from Rs. 64 crores in the six-months period ending March 1940 to Rs. 511 crores in 1943-44, and from Rs. 1,363 crores in 1945-46 to Rs. 64 crores in the six months period ending March 1946. The sterling purchased by the Reserve Bank, representing deliveries under ready and/or forward contracts, including acquisition of dollar balances and

securities, U.S. Treasury payments etc., varied from Rs. 86 crores in the six months period ending March 1940, to Rs. 143 crores in 1943-44, and Rs. 813 crores in the six-months period ending March, 1946. Sterling payments by the British Government shot up from Rs. 16 crores to Rs. 357 crores, and ultimately to Rs. 1,632 crores during the same periods.

*As regards sterling disposals, repatriation schemes ate up varying amounts of sterling during the six and a half years from September 1939 to March 1946, beginning with a dribble of Rs. 22 crores in the six-months period ending March 1940, and rising to Rs. 411 crores in the six-months period ending March 1946. The sterling commitments account of the Government of India rose from Rs. 2 crores to Rs. 67 crores, and ultimately to Rs. 344 crores during the same periods.

A very small, but interesting, point relating to the disposal of sterling was its sale to the public, which was Rs. 2 crores in 1941-42; Rs. 5 crores in 1942-43; Rs. 2 crores in 1943-44; Rs. 5 crores in 1944-45; Rs. 61 crores in 1945-46; and Rs. 75 crores in the six-months period ending March 1947. It is extremely necessary for us here to note that the release of sterling to the public was only a fugitive, but very vital, index of the manner in which replenishment programmes of industry have been sought to be carried out, in spite of the greatest possible obstruction on the part of the Government, by the *entrepreneurs* in this country. Even two years after the defeat of Hitler, we in this country are still unable to have access to funds which lawfully belong to us, in order that our replenishment and reconstruction programmes are made possible. This is the reason why we hold that there cannot be any compromise as regards the speedy release and ultimate repayment of all the sterling which has accrued to us in London, for, without it, it would be next to impossible for us to carry through our programmes of reconstruction finance in the land.

There is bound to be considerable difficulty as regards division of sterling assets as between Indian Union and Pakistan. We are not here concerned with the methods of allocation between these two sovereign States in India, and with the computation whether Pakistan gets 17 per cent according to contributions to Central pool in respect of customs, income-

tax, excises etc.; 20 per cent according to population; or 24 per cent according to revenue, as yard sticks for division. It is, however, clear that sterling which comes back to India, and flows into either of these two sovereign States, remains with the people of India as a whole, as distributed between these two sovereign States. In other words, the implications of division of sterling assets as between the Indian Union and Pakistan cannot have any bearing at all upon Britain's debt to India, in the sense that it should not interfere with its speedy repatriation and final payment.

As we write these lines, the country is facing an enormous controversy regarding the principles which should govern the division of assets and liabilities between the Indian Union and Pakistan. All the yardsticks so far adopted as the basis for the division of liabilities and assets between the Indian Union and Pakistan, converge on point, *viz.*, that physical assets remain where they are, and that only debits and credits will have to be built-up between the two new sovereign States. Our estimate is that, on the basis of any fair approach to division, Pakistan, would find herself owing to the Indian Union some Rs. 1,000 crores. This is the price of Partition which Pakistan has to pay to the citizens of the Indian Union, whose fortunes are sacrificed at the altar of theocratic ideals and racial arrogance. The only feasible manner in which the new Pakistan State is to pay this considerable amount of money is to amortise it and to redeem it through annuities. In this connection, we recall the parallel of the land annuities paid by Irish Free State to Britain as a result of the Anglo-Irish Treaty of 1921, and which Burma undertook to pay India on the basis of the Howard-Nixon Report, after separation in 1937. How much validity any I.O.U. of Pakistan possesses cannot be measured today, when passions are supercharged on either side of the dividing lines to the east and the west, but it is clear that the financial obligations of Pakistan would supply a considerable portion of the reconstruction finance needed by the Indian Union, which suddenly finds itself confronted with the dismemberment of a polity and economy, which possessed continuity for thousands of years. This, however, is a domestic question pending between the Indian Union and Pakistan.

Whether these sterling credits remain a joint or a divided account as between the Indian Union and Pakistan, it is clear that they alone can give this country access to the outside world, in order that we might obtain our urgently required capital goods equipment and technical personnel, without which reconstruction and development would become impossible, at any rate difficult, for long decades to come. The convertibility of sterling into dollar, thanks to the default of Britain from coming to a settlement earlier than July 15, 1947, as enunciated in the Anglo-American Loan Agreement of 1944, has no meaning at all to us in this country, for we have to obtain access to dollar *via* sterling, and sterling remains frozen by Britain, on the plea that she is unable to effect releases at the speed and in the volume which we require for our reconstruction finance.

India is bound to have an adverse balance of trade with U.S.A. for some years to come, with the result that it would not be possible for her to acquire dollar through ordinary commercial channels. With sterling under moratorium, and with dollar unavailable in the ordinary course of the nation's trade, it is obvious that India would have enormous difficulty in finding the money for the purchase of capital equipment to make reconstruction possible. This leads us to a consideration of the urgency of a direct settlement between the Indian Union, as also of Pakistan, and the U.S.A., leading to the creation of dollar credits.

During the past three years, there has been a growing demand in this country for some sort of a direct governmental loan from the U.S.A.* The days of Imperial Preference in India are numbered. The U.S.A. is knocking at the doors of this country for parity of treatment with Britain in the sphere of tariffs. There is still an exportable surplus of considerable magnitude which the U.S.A. can purchase from this country. The U.S.A. had already given a four billion dollar loan to the

*Dr. Lanka Sundaram, had been consistently advocating such a loan, and has recently had the opportunity of popularising this idea before the National Foreign Trade Council and other commercial and professional bodies of the U. S. A., during his recent visit to that country. The correspondence which was exchanged between him and Representative Emanuel Celler of the U. S. A. Congress has created a considerable impression both among Americans and Indians on the vital urgency of a solution to this problem.

U.K., and the U.K. owes India five billions of dollars. The U.S.A. loudly protests her interest in the immediate development of backward areas in the world, for any impediments thrown in the way of development on a global basis would only lead us to the position enunciated in the *Philadelphia Charter*, that "poverty anywhere is a danger to prosperity everywhere". Even from the limited viewpoint of the self-interest of the U.S.A., it is clear that a satisfactory and speedy solution of India's sterling problem becomes important, for, when sterling thaws, the frozen arteries of the export trade of the U.S.A. to India would become mobile again.

This is the reason why we advocate a direct U.S.A. governmental loan to India, for no one in this country, especially at a time when we are reaching our freedom, would admit the re-entry of foreign investment or commercial capital in our midst, a proposition which was in the mind of Ambassador William Grady when he addressed his first press conference in New Delhi in July 7, 1947. Any such course would mean obstruction to our freedom struggle, and to our effort to stabilize our position in the economy of the world. A governmental loan, on the other hand, does not involve any such dangers. The U.S.A. can definitely give us a loan of one or two billion dollars, and we, for our part, can submit our sterling credits in London as the wherewithal for the servicing of this loan. Actually, the U.S.A. as creditor, and India as debtor, can ask, legitimately and with success, Britain to amortize our sterling credits, and utilise them for the servicing and the ultimate repayment of this suggested loan. Easy instalments can be worked out even on the basis which the U.S.A. had agreed to with reference to Britain, with the result that the latter would not be in a quandary as regards an easy and complete repayment of our sterling.

The Indian Union, as much as Pakistan, should not have any difficulty in accepting some sort of an international mixed tribunal, on which their own representatives would sit alongside of those of Britain and U.S.A., in order to see that the suggested American loan is not frittered away on unproductive projects, but is utilised specifically for the purchase of capital equipment and acquisition of technical personnel. We believe

that a scheme of this character, to which a considerable body of public opinion has pledged its support both in India and in U.S.A., would go a long way towards solving the problems of reconstruction finance which are threatening to become almost insuperable.

Incidentally, a scheme of this character has greater validity and chance of success, than the one adumbrated in the Bombay Plan regarding "created money", (of Rs. 3,400 crores) as an adjunct of reconstruction finance, which would certainly throw the people of this country from the frying pan to the fire. We have the experience of almost a decade in regard to the disastrous consequences of inflation, and no sane-minded person in this country would like to toy with new experiments in the field of applied finance, as the Bombay industrialists have tried to do.

Lest we be misunderstood, let us state here the point that today there is a complete and demoralising default of economic and commercial policy in India. With effect from July 1, 1947, the entire export-import policy of the Government of India has been completely altered. We have just commenced tightening up our belts, in order that superfluous consumer goods are not admitted entry into our midst, for such entry would, in the first place, destroy the chances of nascent Indian industry and, secondly, would make us bankrupt in dollar resources. Since we presume that India would be a net importing country during the next ten years or more, with the concomitant denial of foreign exchange through a favourable balance of trade, it is clear that the funds required for reconstruction finance would, in the first place, be not available in our midst and, in the second place, would not bring to us dollars, without which importation of capital goods etc., would become impossible. The "created money" of the Bombay Planners would necessarily be rupee money, and no foreign exporters would accept rupee money in payment of purchases which India seeks to make today and tomorrow. The days are since long past for Mohamad Bin Tughlaq and for insolvent national currencies, with the effigies of the State concerned going on a piece of leather or a piece of paper, as the case may be. Our national currency must have a greater backing than this, and this backing is only

possible if we build up international credit in the manner of the suggested American governmental loan.

We estimate that as much as 50 per cent of the total reconstruction finance of the country needed in the next ten years to come is available in the sterling assets of India in London, and this estimate compares with the projected Rs. 1,000 crores expenditure on reconstruction and development plans, notified earlier. Such a legitimate and important source of income cannot be tampered with. The architects of Pakistan might feel that they stand to gain from British assistance to their new State on the basis of a compromise on sterling, but it is clear that India's sterling credits constitute an indivisible whole, and that either of the newly constituted sovereign States in the country will not be permitted to temporize with this account.

We do not wish to go into the legal basis of note issue in this country by the Reserve Bank of India, with the backing of sterling, to its logical point, beyond stating that any attempt on the part of Pakistan to compromise on this issue with Britain will not become feasible. For, Pakistan must acquire all the rupees, meaning thereby currency notes by and large, which are presumed to be the equivalent of her share of the assets, and surrender them to the Reserve Bank of India, before it can demonitize the currency thus surrendered and have access to sterling in London. It is perfectly true that in political argument legal responsibility is completely forgotten by the protagonists to the controversy. But it is clear that Pakistan has not the means for compromising on sterling assets, even if she is prepared, as she is popularly believed to be, to surrender, at any rate a portion of our sterling, which might accrue to her eventually from the division of assets and liabilities, in order that Britain might prop her up in the economic, political and military spheres. It is now known that Pakistan citizens have only a paltry holding of Rs. 30 crores worth of our currency, compared to the Rs. 1,500 crores worth held by the citizens of the Indian Union!

We feel that we need not pursue this point here any further. Sterling remains, we repeat again, a joint and indivisible account, as between the Indian Union and Pakistan, and has got to be paid for in full by Britain, into a joint account, to be

divided between the Indian Union and Pakistan, on the volition of the people of this country. How soon Britain pays is a matter on which no one can write with precision at the present moment.

BORROWING AND AUDIT

• Section 162 of the Constitution Act vests the executive authority of the Federation (our Union Centre) with power to borrow "upon the security of the revenues of the Federation within such limits, if any, as may from time to time be fixed by Act of the Federal Legislature, and to the giving of guarantees within such limits, if any, as may be so fixed". Federal or Union borrowing must necessarily commit the States which are members of the Union, and the presumption exists that, since the States would have representatives in the Union Legislature as well as on the Union executive, Union borrowing automatically binds each individual State which is a member of the Union. •

Section 163 gives a Provincial Government power to borrow upon the securities of the revenues of the Provinces, within such limits as may from time to time to be fixed by an Act of the Provincial Legislature. It is also provided that the Federation may give guarantees in respect of Provincial loans raised on Provincial responsibility, in addition to making loans to a Province, in which case they become a charge on the revenues of the Federation. Provinces have, however, no power to borrow outside India, without the consent of the Federation. There are also provisions to safeguard the interests of the Provinces, in so far as it was laid down that Federal consent shall not be "unreasonably withheld" to any Province borrowing outside India, or to refuse to make a loan to, or to give guarantee in respect of a loan raised by a Province "if sufficient cause is shown" that such a loan is necessary for the maintenance of its financial equilibrium. It is, thus, clear that the Provinces have the right to raise loans on their own initiative subject to certain conditions, in addition to obtaining, as a matter of right, loans from Federation or the Union Centre.

As regards Indian States, Section 164 of the Constitution Act runs as follows: "The Federation may, subject to

such conditions, if any, it may think fit to impose, make loans to, or, so long as any limits fixed . . . are not exceeded, give guarantees in respect of loans raised by any Federated State." We are unable to build up a table of the public debt of States, though we are aware of the existence of the public loans raised by individual States, such as Hyderabad, Mysore, Travancore, etc. We are also aware of the fact that even though these loans of the States, as they exist today, are not generally quoted on the stock exchanges of Bombay, Calcutta and Madras, institutional holders in the Provinces, such as banks and insurance companies, have small moities thereof in their portfolios.

The right of the States to borrow from the public on the pledge of its own resources cannot be disputed. The right of the States which enter the Union to ask for grants and loans from Union finances is also admitted to be on a par with that of the Provinces to make similar requests. The right of the Union Centre to raise loans for the common benefit of all the constituent units, including the States, is also beyond dispute.

These propositions, however, raise the question whether a Union loan becomes chargeable on the resources of the States which are members of the Union. Obviously, the answer is in the affirmative. The States cannot claim that they are immune to the Union obligations in respect of the public debt of the Union. A trite example of the inescapable necessity for States which participate in the Union to shoulder Union burdens is in the field of planning and development, for schemes undertaken for the benefit of the Provinces and the States in common must be shared by each in an equal measure.

A final proposition arising out of this enquiry is that the States cannot have the right to pursue an independent borrowing policy without any reference to the Union Centre, if only for the simple reason that it is the Union Centre which is presumed to have the control of the money markets in the land. Anything done either by a Province or a State, which is a member of the Union, to upset the money markets of the country is reprehensible, and tends to weaken the structure of the Union.

It is obvious that, as in the case of the Provinces (*vide* Section 163 (3) of the Constitution Act), the States cannot

have the right normally to raise loans abroad. For, it is clear that access to international money markets would become a tremendous inducement to the units of the Union to indulge in reckless expenditure programme and would ultimately imperil the financial stability and security of the Union as a whole. In the case of the States, where the sovereignty of the Ruler might linger unto the last ditch, any access to the money markets of the world would be fraught with disastrous consequences. We have laid down the point, elsewhere in this enquiry, that the States share, in common with the Provinces, the burdens of deficit areas, and that the benefit of the same principle accrues to the States, inasmuch as the Provinces agree to underwrite the financial stability of the States which are members of the Union. On this principle of a totality of common risks and common responsibilities, States and Provinces must function within the overall control of the Union Centre, especially in regard to high economic and financial questions.

Section 171 of the Constitution Act runs as follows: "The accounts relating to the discharge of the functions of the Crown in its relations with Indian States shall be audited by the Auditor-General of India", and that annual reports on the accounts so audited shall be submitted to the Secretary of State. The functions of the Crown have now completely disappeared, and are replaced by those of the Indian States' Department of the Government of the Union. To the extent to which this Department functions in the States, or in relation to the States, we presume that the implications of this provision of the Constitution Act continue to be operative. Such of the States which adhere to the Indian Union must accept the principle of Union audit, very much on the lines on which the Provinces have agreed to it, though possessing the legal right of access to even foreign money markets. The codicil must, however, be recognised that Union audit would envelop the States, only to the extent to which the incoming Princes surrender their sovereignty in respect of and the generally categorised list of items of Union administration and policy.

TARGETS OF RECONSTRUCTION FINANCE

Reconstruction and development from the viewpoint of the Union Centre, or Pakistan, cannot have shape, form and mutability, as long as, or to the extent to which, the principle governing the accession of the States are not specifically laid down, and the general structure of the nation's economy enveloping these two component parts of the Union continue to remain unsettled, or fluid. It is to be feared that, at any rate as far as the accession of States to the Constituent Assembly and to the general set-up, political and economic, in and outside India, up to the moment of writing, is concerned, the Constitution-makers are, by and large, only attempting to take a broad leap into the future. The proposition, however, hits one in the eye that the substance of political and economic conditions in India today and tomorrow would certainly be altered, and render existing plans wholly or partially inoperative.

An eloquent illustration of the inconvenience of planning with any purposiveness is supplied by some of the assumptions behind the Second Report on Reconstruction Planning of the Reconstruction Committee of Council. What the Committee wrote in October 1945 has been rendered almost inoperative by July 1947, for most of the basic assumptions behind the Report have no longer any validity. The Committee stated, "that any constitutional or political changes which can be introduced, will not result in a radical departure from the present economic and financial arrangements." The Cabinet Mission Plan of May 16, 1946, administered a knock-out blow to this theory, followed by the Indian Independence Act of July 1947, as heralded by the Declaration of June 3, 1947. There are today an Indian Union and Pakistan to which the States may by and large adhere. There are some States which remain independent. The entire economy of the land is today subject to being thrown into the melting pot, and problem by problem will have to be taken in hand, so that industry and commerce, leave aside the larger general question of productive output in relation to the standards of living of the community, becomes readjusted to the changing circumstances of Partition, and in relation to the attitude of Princes, who may either elect to unionise or remain in isolated independence. The problems, as between the Indian

Union and Pakistan, are disconcerting enough, but those created by the States constitute a veritable Pandora's box by themselves. These posers are sufficient to show that planning on a dogmatic basis cannot be valid, and will be unsettled by the march of events, over which neither the planners nor the citizen can have any control.

* The Reconstruction Committee of the Council had pursued certain assumptions which have almost become inoperative inside of twenty months. They assumed a speedy rate of demobilisation after the conclusion of hostilities, and of a progressive reduction of the Defence Budget. Even two years after Hiroshima, there was not even a fifty per cent reduction in the cost of Defence services and the ancillary units recruited during the war period. As for the Defence budget, it was Rs. 406.85 crores in 1945-46, Rs. 288.72 crores in the revised estimates of 1946-47, and Rs. 204.37 crores in the budget estimates of 1947-48, which last figure compares to the basic normal budget of Rs. 36.77 crores of the inter-war period! .

Other assumptions of the Reconstruction Committee have also become equally inoperative. The world conditions, as were assumed in October 1945, do not as yet permit full production and employment, if only as a result of the desire of the Western Powers to keep, almost for ever, the countries with so-called backward economies as the happy hunting ground for their own exclusive benefit. As we write, the International Conference on Trade and Employment is still battling with this proposition, for today more than sixty per cent of the people of the world are located in these countries with backward economies, and they are making a tremendous and sustained bid to gain the right to self-preservation and improvement in their social and economic conditions.

Yet other assumptions of the Reconstruction Committee are there to be disposed of. The view that the people of India will agree to "full development and exploitation of the taxable capacity" has not become an accomplished fact. The first budget of the first Indian Finance Member is an illustration of the point. He has almost killed the goose which lays the golden egg. Such, again, is the position of the last assumption of the

Reconstruction Committee of Council regarding the control over the issue of capital.

We have devoted this much space to an examination of the assumptions of the Reconstruction Committee of Council, in order to underline the dangers of reconstruction or development, without first securing the absolute minimum conditions necessary for their success. In fact, we cannot make bricks without straw, and for our present purposes the straw concerned are, in the first place, the willingness of Provinces and States to function in the Union Centre, or Pakistan; and, secondly, a reasonable and uniform method for the entry of these Units, both Provinces and States, into an administrative framework for the Union or Pakistan.

It is not our desire merely to tear to pieces the Report of the Reconstruction Committee of Council on Planning and Development. But it certainly is our purpose to show that assumptions must be there which will have a reasonable certainty of becoming facts before planning and development are taken in hand. For instance, the Reconstruction Committee assumed that a round figure of Rs. 1,000 crores might be available for the first five year period, taking effect from the year 1947-48 and ending 1951-52, obviously for the Indian Provinces and the Centre. The Committee wrote: "Approximately half the total will consist of revenue surpluses, which will be available for financing such Central developing projects as are not financed by loans, and for making grants, recurring or otherwise," the balance of Rs. 500 crores being the assumed yield of loans, both Central and Provincial.

The question naturally arises whether the assumption of the Reconstruction Committee that, during the five year period 1947-48 to 1951-52, the Centre would have a revenue surplus of Rs. 500 crores, being an average of Rs. 100 crores each year, is correct. The table on the next page indicates the results reached by both the Centre and the Provinces as regards the revenue and expenditure positions during the past ten years.

Surpluses and Deficits of the Centre and Provinces.

(In Lakhs of rupees.)

Year.	Centre.	Eleven Provinces.
1938-39	— 64	— 83
1939-40 .. .. .	....	2,22
1940-41	— 6,53	1,63
1941-42	-- 12,17	3,31
1942-43	-- 111,78	7,83
1943-44	-- 189,90	14,85
1944-45	-- 160,55	9,68
1945-46	-- 123,89	15,76
1946-47 (R. E.)	— 45,28	— 8,23
1947-48	— 16,96	— 5,73
Total ..	— 667,70	40,58

We regret to say that the prognostications of the Reconstruction Committee are belied by the above figures, the pith of whose significance must necessarily supply the trend of inquiry into the coming five years. The revenue surpluses of all the Provinces have, during the preceding ten years, come to the paltry total of Rs. 41 crores, while those of the Centre show the colossal deficit of Rs. 668 crores. We must emphasise the point that these figures are paper figures, in the sense that they do not take in the full implication, e.g., in the case of the Centre, of loan finance etc. Yet, the figures given above have a tale to tell. While the war-time deficits of the Centre are being gradually reduced, the surpluses of the Provinces are also being reduced each year. This is as it should be, for Provincial revenues have become more or less regressive, while Provincial expenditure, with the advent of popular ministries, is going up, as it should be expected to go up. We cannot conceive of the realisation of the surpluses of the Centre and the Provinces during the coming five years, to the extent postulated by the Reconstruction Committee of Council, and in any case revenue surpluses of Rs. 500 crores in five years look to us to be something like the man in the moon.

Day by day the expenditure of the Provincial and Central Governments is increasing. Demobilisation and resettlement plans of the Centre are still a charge upon the Central Revenues

of the country—and a considerable one too. The gradual expansion, even within this five year period, of our diplomatic representation abroad, and our participation in international conferences, might make any difference between Rs. 5 to Rs. 10 crores a year of additional expenditure. Implementation of the Pay Commission's Recommendations, as far as the Centre alone is concerned, would mean a *plus* Rs. 30 crores a year of expenditure by the Centre. Since Bengal is partitioned, the yield from the jute export duty for the purpose of the Centre would be cut by more than half. Both the Centre and the Provinces are expanding their nation-building activities involving expenditure of dozens of crores of rupees annually. In Madras alone Rs. 6 crores were spent on food procurement this year. Prohibition would cost enormous sums of money, firstly in loss of revenue, and secondly in respect of enforcement costs. The abolition of the Salt Tax has made a gap of Rs. 9 crores a year in Central revenues. And if the prevailing unsettled conditions continue in the country, neither Defence expenditure, nor the expenditure on Police services, would show appreciable reductions. On the contrary, the tendency would be for them to rise.

When the full financial effects of the Partition of the country come to be known, the estimates of the Reconstruction Committee of Council would be proved to be completely outside the mark. These illustrations can be multiplied from various angles, but this need not be done here. Sufficient has been shown, however, to demonstrate the point that the assumption of the Reconstruction Committee that there will be a *revenue surplus* of about Rs. 100 crores a year for the eleven Indian Provinces and the Centre during the current five-year period will not become an actuality. We have, however, very little to say about the suggestion of the Reconstruction Committee regarding the loan programme of the Centre and the Provinces.

The financial potentialities and problems of States, virtually constitute a *terra incognita*. Revenue and expenditure statements are not available, at any rate in an intelligible form, and with an auditor's certificate, for all these States. We are not suggesting that there is any departure from honesty in the published accounts of the financial position of each individual

State. The Political Department of the Government of India, which has been recently liquidated, alone knew the facts, if at all any one knew them. We have, however, sampled the budgets of two dozen States, from the latest available Administration Reports, and we incorporate below the results achieved.

The following is a statement of the Revenue and expenditure-position of 23 States:—

Surpluses and Deficits of Selected States.

(In thousands of Rupees)

State	Year	Revenue	Expenditure	Surplus or Deficit
Kashmir	1944-45	4,63,95	4,22.20	41,75
Bhawalpur	1944-45	1,68,33	.....	.....
Kapurthala	1944-45	39,50	25,09	14,41
Gwalior	1942-43	3,20,43	2,22,15	98,28
Rampur	1943-44	84,24	81,73	2,51
Jaipur	1942-43	1,96,96	1,44,84	52,12
Bikaner	1943-44	2,20,98	1,39,66	81,32
Jodhpur	1937-38	1,68,85	1,30,36	38,49
Udaipur	1945-46	4,40	3,91	58
Bharatpur	1944-45	64,98	64,28	70
Mayurbhanj	1944-45	46,98	37,07	9,91
Cooch-Behar	1943-44	70,76	49,28	21,48
Baroda	1944-45	4,34,26	3,73,78	61,48
Cambay	1943-44	12,41	10,24	2,17
Nawanagar	1943-44	1,10,15	1,08,18	1,97
Kolhapur	1943-44	1,15,08	75,77	39,31
Bhavnagar	1942-43	80,23	83,59	- 3,36
Bhopal	1941-42	90,27	84,03	6,24
Hyderabad	1938-39	8,92,64	8,90,59	2,05
Indore	1943-44	2,83,27	1,91,84	91,43
Mysore	1944-45	10,01,38	11,22,60	-1,21,31
Travancore	1944-45	6,11,25	6,11,25	.....
Cochin	1942-43	1,70,60	1,44,39	26,21
Total Surplus				4,67,74

The above table relating to selected States, which are of primary importance to our study, has a very interesting bearing upon projection. It is true that the years to which these figures relate are not identical. It is equally well admitted that figures for single years are only random selections which do not constitute a yardstick. Still, in these twenty three States only two, *viz.*, Bhavnagar and Mysore, have deficits, while every other State has a surplus. The States are always chary

of deficit finance, for autocracies cannot function on borrowing, and do not encourage confidence in the people.

If these two dozen big States in the country can only muster less than Rs. 5 crores in a year, it is obvious that the entire Princely Order cannot hope to put up, from out of current revenue surpluses, even Rs. 10 crores a year. We believe that these suppositions are approximations, but they are approximations which serve as a pointer. It is no doubt true that each Prince and princeling has fabulous wealth, and the Nizam, according to popular belief which is not wide of the mark, is reputed to hold wealth in his hands, which is sufficient to underwrite overnight the entire finance needed for the implementation of the Bombay Plan! But this wealth of the Princes is comparable to that of Maidas, for it cannot be expected to go into current or long-term expenditure intended for the public good. Actually, since the powers, prerogatives and perquisites of the Princely Order are to be drastically curtailed, before they are permitted to enter the Indian Union or Pakistan, the tendency would be for the members thereof to hold on to the hoarded wealth. The privy purse of a Prince, as much as the civil list of his *darbar*, would soon have its wings and frills clipped off, with the advent of popular governance in the States. This would be an additional reason for us to assume that the Princely Order would not only hold on to the wealth on hand, but would even make a quick conversion of fixed properties into liquid assets.

Once the States enter the Union or Pakistan as integral units, the immediate five-year plans of the country, for the Centre, the Provinces and the States, have got to be revised from Rs. 1,000 crores of the Reconstruction Committee of Council to possibly Rs. 2,000 crores. We must here repeat the stress we have already laid upon the lack of revenue surpluses for the Centre, the Provinces and the States. The net result would be that the country would have to take increasing recourse to loan finance, to an extent not so far recognised both in official and non-official circles.

FINANCIAL POWERS OF FEDERAL GOVERNMENTS

We append below selections from the constitutions of selected Federations in the world, in order to demonstrate the manner in which the financial position of the Federal Centre in each of the countries concerned is secured.

COMMONWEALTH OF AUSTRALIA, 1900

(As amended 1907, 1910 and 1929)

Article LI:—The Parliament shall, subject to this constitution, have power to make laws for the peace, order, and good government of the Commonwealth with respect to:—

- (1) Trade and commerce with other countries, and among the States.
- (2) Taxation; but so as not to discriminate between States or parts of States.
- (3) Bounties on the production or export of goods, but so that such bounties shall be uniform throughout the Commonwealth.
- (4) Borrowing money on the public credit of the Commonwealth.
- (5) Postal, telegraphic, telephonic, and other like services.
- (12) Currency, coinage, and legal tender.
- (13) Banking, other than State banking; also State banking extending beyond the limits of the State concerned, the incorporation of banks, and the issue of paper money.
- (14) Insurance, other than State insurance; also State insurance extending beyond the limits of the State concerned.
- (15) Weights and measures.
- (16) Bills of exchange and promissory notes.
- (32) The control of railways with respect to transport for the naval and military purposes of the Commonwealth.

(33) The acquisition, with the consent of a State, of any railways of the State on terms arranged between the Commonwealth and the State.

(34) Railway construction and extension in any State with the consent of that State.

Article LIII:—Proposed laws appropriating revenue or moneys, or imposing taxation, shall not originate in the Senate but a proposed law shall not be taken to appropriate revenue or moneys, or to impose taxation, by reason only of its containing provisions for the imposition or appropriation of fines or other pecuniary penalties, or for the demand or payment or appropriation of fees for licences, or fees for services under the proposed law.

The Senate may not amend proposed laws imposing, taxation, or proposed laws appropriating revenue or moneys for the ordinary annual services of the Government.

Article LV:—Laws imposing taxation shall deal only with the imposition of taxation, and any provision therein dealing with any other matter shall be of no effect.

Laws imposing taxation, except laws imposing duties of customs or of excise, shall deal with one subject of taxation only; but laws imposing duties of customs shall deal with duties of customs only, and laws imposing duties of excise shall deal with duties of excise only.

Article LXXXI:—All revenues or moneys raised or received by the Executive Government of the Commonwealth shall form one Consolidated Revenue Fund, to be appropriated for the purposes of the Commonwealth in the manner and subject to the charges and liabilities imposed by this constitution.

Article LXXXVI:—On the establishment of the Commonwealth, the collection and control of duties of customs and of excise, and the control of the payment of bounties, shall pass to the Executive Government of Commonwealth.

Article LXXXVIII:—Uniform duties of customs shall be imposed within 2 years after the establishment of the Commonwealth.

Article LXXXIX:—Until the imposition of uniform duties of customs:—

- (1) The Commonwealth shall credit to each State the revenues collected therein by the Commonwealth.
- (2) The Commonwealth shall debit to each State—
 - (a) The expenditure therein of the Commonwealth incurred solely for the maintenance or continuance, as at the time of transfer, of any department transferred from the State to the Commonwealth,
 - (b) The proportion of the State, according to the number of its people in the other expenditure of the Commonwealth.
- (3) The Commonwealth shall pay to each State month by month the balance (if any) in favour of the State.

Article XC:—On the imposition of uniform duties of customs, the power of the Parliament, to impose duties of customs and of excise and to grant bounties on the production or export of goods, shall become exclusive.

On the imposition of uniform duties of customs, the laws of several States imposing duties of customs or of excise, or offering bounties on the production or export of goods, shall cease to have effect, but any grant of or agreement for any such bounty lawfully made by or under the authority of the Government of any State shall be taken to be good if made before the 30th day of June, 1898, and not otherwise.

Article XCII:—On the imposition of uniform duties of customs, trade, commerce, and intercourse among the States, whether by means of internal carriage or ocean navigation, shall be absolutely free.

Article C:—The Commonwealth shall not, by any law or regulation of trade or commerce, abridge the right of a

State or of the residents therein to the reasonable use of the waters of rivers for conservation or irrigation.

BRAZIL

(10th Nov. 1937, as amended to 12th Oct. 1942)

Article VIII:—Each State is to organise its own services to meet its own particular interests and must pay for them out of its own resources.

Sole paragraph. A State which, for three consecutive years fails to collect sufficient revenue to maintain these services, shall be transformed into a territory until its financial capacity shall have been re-established.

Article X:—The State shall have the obligation to provide the necessary measures, within their respective jurisdictions, to carry out such commercial treaties as the Union may enter into. Should they fail to do this within a reasonable time, the legislative power for such measures will devolve upon the Union.

Article XV:—The Union will have sole jurisdiction:

- (1) To maintain relations with foreign countries, to nominate the members of the diplomatic and consular corps, to enter into treaties and international conventions.
- (2) To authorise the production of and to supervise the commerce in war material of whatever nature.
- (6) To maintain the postal services.

Article XVI:—The Union shall have the sole jurisdiction to legislate on the following matters:

- (6) Federal finances, questions of currency, of credit, of exchanges and of banking.
- (7) Foreign and inter-state commerce, exchange and transfer of funds abroad.
- (8) Monopolies and nationalisation of industries.

- (9) The weights and measures, standards, title and guarantee of precious metals.
- (13) Custom houses and warehouses; maritime port and river police.

Article XX:—The Union will have sole jurisdiction:

- (1) To decree taxes
 - (a) On the importation of merchandise from abroad;
 - (b) On the consumption of any kind of merchandise;
 - (c) On income or receipts of whatsoever nature;
 - (d) On the transfer of funds abroad;
 - (e) On services executed by its Government, business under its control, and its instruments or contracts regulated by Federal law.
 - (f) In the territories, those which are allowed by the States by the Constitution.

Article XXIII:—The States shall, subject to the limitation stated in article XXXV letter (d), have exclusive jurisdiction:

- (1) To decree taxes on:
 - (a) All territorial property, except urban; and
 - (b) The transfer of property in “*causa mortis*”
- (2) To collect taxes on State services:
 - (a) Tax on sales shall be uniform, irrespective of the source, purpose or type of merchandise.
 - (b) The tax on industries and professions shall be assessed by the State, and collected by the State and the municipality in equal parts.
 - (c) In exceptional cases, and with the consent of the Federal Council, the export tax may be temporarily increased.

Article XXIV:—The States may create other forms of taxation. Double taxation is, however, forbidden, and the tax decreed by the Union will prevail where the jurisdiction is concurrent. It is within the province of the Federal Council, either on its own initiative or at the

request of the tax-payer, to declare that there is double taxation, and suspend the collection of the State tax.

Article XXV:—The National Territory shall constitute one single unit, from the commercial, economic and customs point of view; no customs barriers or other traffic restrictions may be established; States, as well as municipalities, are therefore forbidden to collect, under any denomination whatsoever, inter-state, inter-municipal, transit or transport taxes, which will hinder the free circulation of goods and persons and the vehicles which transport them.

Article XXVIII:—Besides the attributes given to them by, article 23, paragraph 2, of the present Constitution and those which may be transferred to them by the State, the municipalities shall have:

- (1) License taxes.
- (2) Tenement tax, as well as urban land tax.
- (3) Taxes on public amusements.
- (4) Taxes on municipal services.

Article XXXIV:—It is forbidden to the States, to the Federal District and to the municipalities:

- (b) To establish tax discrimination or of any other sort between goods or merchandise because of its source or origin;
- (c) To contract foreign loans without the previous consent of the Federal Council; and
- (d) To place direct or indirect taxes upon the production or commerce including the distribution and exportation of national coal and liquid fuels and lubricants of any origin.

Article XXXVI:—Labour is a social duty. Intellectual, technical and manual labour has the right to the protection and special care of the State.

DOMINION OF CANADA

(1867)

Article XCI:—The exclusive legislative authority of the Parliament of Canada extends to all matters coming within the classes of subjects next hereinafter enumerated: that is to say:—

- (1) The public debt and property.
- (2) The regulation of trade and commerce.
- (3) The raising of money by any mode or system of taxation.
- (4) The borrowing of money on the public credit.
- (5) Postal services.
- (7) Militia, military and naval services, and defence.
- (14) Currency and coinage.
- (15) Banking, incorporation of banks, and the issue of paper money.
- (17) Weights and measures.
- (20) Legal tender.

Article XCII:—In each Province the Legislature may exclusively make laws in relation to matters coming within the classes of subjects next hereinafter enumerated: that is to say:

- (2) Direct taxation within the Province in order to the raising of a revenue for provincial purposes.
- (3) The borrowing of money on the sole credit of the Province.

Article CXII:—All duties and revenues over which the respective Legislatures of Canada, Nova Scotia and New Brunswick before and at the union had and have power of appropriation, shall form one Consolidated Revenue Fund, to be appropriated for the public service of Canada in the manner and subject to the charges in this Act provided.

Article CXX:—All assets connected with such portions of the public debt of each Province as are assumed by that Province shall belong to that Province.

- Article CXXI*:—Canada shall be liable for the debts and liabilities of each Province existing at the Union.
- Article CXXXII*:—The customs and excise laws of each Province, shall, subject to the provisions of this Act, continue in force until altered by the Parliament of Canada.
- Article CXXXIII*:—Where customs duties are, at the Union, leviable on any goods, wares or merchandises in any two Provinces, those goods, wares and merchandises may, from and after the Union, be imported from one of those Provinces into the other of them, on proof of payment of the customs duty leviable thereon in the Province of exportation, and on payment of such further amount (if any) of customs duty as is leviable thereon in the Province of imposition.
- Article CXXXV*:—No lands or property belonging to Canada or any Province shall be liable to taxation.
-

THE GERMAN REICH

(*August 11, 1919*)

- Article VI*:—The Reich has exclusive legislative power as regards:—
- (1) Foreign relations.
 - (4) Military organisation.
 - (5) The monetary system.
 - (6) Customs, as well as uniformity in the sphere of customs and trade, and freedom of commercial intercourse.
 - (7) Posts and telegraphs, including telephones.
 - (9) Labour laws, the insurance and protection of workers and employees, together with Labour Bureaux.
 - (13) The formation of associations for dealing with natural resources and economic undertakings, as

well as the production, preparation, distribution and determination of prices of economic commodities for common use.

- (14) Commerce, the system of weights and measures, the issue of paper money, banking affairs and the system of exchanges.
- (15) Traffic in foodstuffs and luxuries as well as in articles of daily necessity.
- (16) Industry and mining.
- (17) Insurance matters.
- (18) Navigation, and deep sea and coastal fishery.
- (19) Railways, inland navigation, motor traffic by land, water and air, as well as the construction of high-roads, so far as this is concerned with general traffic and home defence.

Article VIII:—Further, the Reich has legislative power as regards taxes and other revenues in so far as they are appropriated wholly or in part to its purposes. Should the Reich appropriate taxes or other revenues hitherto appertaining to the various States, it must take into consideration the maintenance of the vitality of those States.

Article IX:—Where there is need for the issue of uniform regulations, the Reich has legislative power as regards:

- (1) Sanitary administration.
- (2) The maintenance of public order and security.

Article X:—The Reich may by legislation lay down fundamental principles governing:—

- (1) The rights and duties of religious associations.
- (2) Education, including higher education and scientific literature.
- (3) The law as to the conditions of service of officials of all public bodies.
- (4) The land laws, the distribution of land, land settlement and small holdings, the tenure of landed property.

Article XI:—The Reich may by legislation lay down fundamental principles governing the admissibility and

mode of collection of State taxes, in so far as they are requisite either for the purpose of preventing:—

- (1) Loss of revenue or injury to the commercial relations of the Reich.
- (2) Double taxation.
- (3) Charges for the use of public means of communication and their accessories, which are excessive and constitute a hindrance to traffic.
- (4) Assessments which are prejudicial to imported goods, as opposed to home products, in dealings between the separate States and parts of a State.
- (5) Bounties on exportation; or for the purpose of protecting important social interests.

Article LXXVIII:—The conduct of foreign affairs is the exclusive concern of the Reich.

In affairs regulated by State legislation, the States may conclude agreements with foreign States. These agreements require the consent of the Reich.

Conventions with foreign States as to the alteration of the frontiers of the Reich are concluded by the Reich, with the consent of the State concerned. Alterations in the frontier may be effected only by a law of the Reich, except in the case of a simple rectification of the borders of uninhabited portions of a district.

In order to guarantee representation of the interests of individual States arising from their special economic relations with foreign States or their proximity thereto, the Reich undertakes the requisite arrangements and measures in agreement with the State concerned.

Article LXXIX:—The defence of the Reich is a matter for action by the Reich. The military organisation of the German people is regulated uniformly by means of a law of the Reich, regard being had to the individual conditions of each State.

Article LXXXI:—All German merchant shipping constitutes a united commercial fleet.

Article LXXXII:—Germany forms one customs and commercial district enclosed by one common customs frontier.

The customs frontier coincides with the foreign frontier. To seaward it is formed by the shore of the mainland, with the islands belonging to the territory of the Reich. On the sea or on other bodies of the water, deviations may be made in the course of the customs frontier.

All natural products as well as products of manufacture and industry in which there is free trade within the Reich, may be imported, exported or sent in through transit, across the frontier of the States and local authorities. Exceptions may be allowed by a law of the Reich.

Article LXXXIII:—Customs and duties upon articles of consumption are administered by authorities of the Reich.

In the administration of taxes by the authorities of the Reich arrangements shall be made so as to ensure to the various States the protection of special State interests within the domain of agriculture, trade manufacture and industry.

Article LXXXIV:—The Government of the Reich regulates by law:—

- (1) The organisation of the administration of taxes in the States, so far as it required for the purpose of uniform and equal execution of the laws of the Reich on taxation;
- (2) The organisation and powers of the authorities entrusted with the superintendence of the execution of the laws of the Reich on taxation;

Article LXXXV:—All receipts and expenditure of the Reich must be estimated for each financial year and be shown in the Budget.

Article LXXXVII:—Funds may be obtained by way of loan in case of special necessity, and, as a rule, only for expenditure on productive undertakings.

Article LXXXVIII:—The postal and telegraph services, together with the telephone services, are exclusively the affairs of the Reich.

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Article LXXXVIII:—The postal and telegraph services, together with the telephone services, are exclusively the affairs of the Reich.

Postage stamps are uniform for the whole Reich,

Article LXXXIX:—It is the duty of the Government of the Reich to assume ownership of the railways serving for general traffic, and to manage them on a uniform traffic system.

The rights of States to acquire private railways shall be transferred upon demand to the Government of the Reich.

Article XCII:—Notwithstanding the incorporation of their Budget and accounts with the general Budget and accounts of the Reich, the railways of the Reich shall be administered as an independent, economic undertaking responsible for defraying its own expenses, inclusive of interest and a sinking-fund for the railway debt, and also for accumulating a reserve. The amount of the sinking-fund and reserve, as well as the purposes to which the reserve is to be applied, shall be regulated by means of a special law.

Article XCV:—In the supervision of rates, uniform and low railway rates are to be aimed at.

Article XCVI:—All railways, including those not serving for general traffic, must comply with the requirements of the Reich as to the use of railways for the purpose of State defence.

Article CLIV:—The right of inheritance is guaranteed in accordance with the provisions of the Civil Law.

The share in any inheritance which accrues to the State is determined by law.

Article CLV:—The distribution and use of land shall be supervised by the State in such a way as to prevent abuse and with a view to ensuring to every German a healthy dwelling and to all German families, particularly those with many children, a dwelling and economic homestead suited to their needs.

Increment in the value of landed property, not accruing from any expenditure of labour and capital

upon the land, shall be devoted to the uses of the community.

Article CLVI:—The Reich, may, by legislation, without prejudice to the payment of compensation and subject to appropriate application of the visions governing expropriation, transfer to public ownership private economic undertakings which are suitable for socialization. It may itself undertake, or assign to the States or local authorities a share in the management of such undertakings and associations, or otherwise ensure to itself a determining influence therein.

Further, the Reich may, by legislation, in case of pressing necessity and in the economic interests of the community, oblige economic undertakings and associations to combine, on a self-governing basis, for the purpose of ensuring the co-operation of all productive factors of the nation, associating employers and employees in the management, and regulating the production, manufacture, distribution, consumption, prices and the import and export of commodities upon principles determined by the economic interest of the community.

Industrial and agricultural co-operative societies and federations thereof may be incorporated into the public economic system, at their own request and with due regard to their constitution and special characteristics.

Article CLIX:—Freedom of association for the maintenance and improvement of labour and economic conditions is guaranteed to every one and for all occupations. All agreements and measures tending to restrict or obstruct such freedom are illegal.

SWISS FEDERATION, OF MAY 29, 1874

(Revised upto March 15, 1931)

Article XXVII:—Subventions shall be granted to the Customs to aid them in carrying out their obligations in respect of primary education.

Article XXVIII:—Customs duties are within the province of the Confederation which may impose import and export taxes.

Article XXIX:—The collection of Federal customs must be regulated in accordance with the following principles:

(1) Import taxes.

(a) Materials necessary to the industry and agriculture of the country must be taxed as lightly as possible;

(b) The same principle applies to commodities necessary for the maintenance of life; and

(c) Articles of luxury must be subject to the heaviest taxes.

(2) Export taxes must be as moderate as possible.

(3) Legislation on customs will contain suitable provisions for the continuance of commercial and market intercourse across the frontier.

The foregoing provisions do not preclude the Confederation from taking exceptional measures temporarily to meet abnormal circumstances.

Article XXX:—The yield of customs duties belongs to the Confederation.

Article XXXI:—The freedom of trade and industry is guaranteed throughout the Confederation.

Article XXXII:—The Cantons are authorized to collect the import duties on wines and other spirituous liquors referred to in Article 31, Clause (a) (which refers to the import duties of wines and other alcoholic beverages) subject in all cases to the following restrictions:—

(a) The collection of these duties must not impede the free transit of goods; commerce must be hin-

dered as little as possible and may not be subjected to any other tax;

- (b) If commodities imported for consumption are re-exported from the Canton, the duty paid on import must be refunded without further charge;
- (c) Commodities produced in Switzerland must be taxed at a lower rate than those of foreign origin; and
- (d) The import duties on wines and other spirituous liquors produced in Switzerland may not be increased in Cantons where such duties now exist, nor may such duties be imposed by Cantons which do not collect them at the present time.

Article XXXVI:—Throughout Switzerland posts and telegraphs are within the province of the Confederation. Revenues from posts and telegraphs belong to the Federal Treasury.

Postal and telegraphic charges must be fixed on the same principle and as equitably as possible in every part of Switzerland.

UNION OF SOUTH AFRICA, 1909

(Amended in 1937)

Article LXXV:—Subject to the provisions of this Act and the assent of the Governor-General-in-Council, the Provincial Council may make ordinances in relation to matters coming within the following classes of subjects:—

- (1) Direct taxation within the Province in order to raise a revenue for provincial purposes.
- (2) The borrowing of money on the sole credit of the Province with the consent of the Governor-General in-Council and in accordance with regulations to be framed by Parliament.
- (3) Education, other than higher education, for a period of 5 years and thereafter until Parliament otherwise provides.

Article CXXIV:—The Union shall assume all debts and liabilities of the Colonies existing at its establishment, subject, notwithstanding any other provision contained in this Act, to the conditions imposed by any law under which such debts or liabilities were raised or incurred, and without prejudice to any rights of security or priority in respect of the payment of principal, interest, sinking fund, and other charges conferred on the creditors of any of the colonies, and may, subject to conditions and rights, convert, renew, or consolidate such debts.

UNITED STATES OF AMERICA

(1787)

Section VIII:—The Congress shall have power :

- (1) To lay and collect taxes, duties, imposts, and excises, to pay the debts and provide for the common defence and general welfare of the United States; but all duties, imposts, and excises shall be uniform throughout the United States.
- (2) To borrow money on the credit of the United States.
- (3) To regulate commerce with foreign nations, and among the several States, and with the Indian tribes.
- (4) To establish an uniform rule of naturalization and uniform laws on the subject of bankruptcies throughout the United States.
- (5) To coin money, regulate the value thereof, and of foreign coin, and fix the standard of weights and measures.
- (6) To provide for the punishment of counterfeiting the securities and current coin of the United States.
- (12) To raise and support armies, but no appropriations of money to that use shall be for a longer term than two years.

Section IX.—(4) No capitation or other direct tax shall be laid, unless in proportion to the census or enumeration hereinbefore directed to be taken.

(5) No tax or duty shall be laid on articles exported from any State.

Section X.—(2) No State shall, without the consent of the Congress, lay any imposts or duties on imports or exports, except what may absolutely necessary for executing its inspection laws, and the net produce of all duties and imposts, laid by any State on imports or exports, shall be for the use of the Treasury of the United States; and all such laws shall be subject to the revision and control of the Congress.

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