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**Bombay Finance (1921-1946)**

**By**

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## AUTHOR'S PREFACE

THE present study was undertaken in 1938 at the instance of Mr. D. R. Gadgil, and was carried out at the Gokhale Institute of Politics and Economics under his general guidance and supervision. My transfer to Willingdon College, Sangli, in June 1940, caused a good deal of delay in the completion of the study, as I could work only during vacations. It was not till June 1946 that I could hand over my manuscript to the Institute which has kindly agreed to publish it. In the meanwhile I was awarded a scholarship by the Watumull Foundation of Los Angeles (Calif.), for advanced studies in the U. S. A., and I left India in July, entrusting the task of seeing the book through the press to my pupil and friend, Mr. N. V. Sovani.

While I was collecting materials for the present study it was suggested to me that I should present the financial structure and developments in the Province with a view to serving the practical needs of legislators and other public men interested in the financial process. While, however, I have kept this object in view, my approach has been primarily analytical rather than descriptive. Thus, I have attempted to set forth the financial problems and policies of the Provincial Government in their wider economic setting, and have endeavoured, whenever possible, to discover the relationship between the cyclical movements in prices and incomes with the changes in the financial structure. Indeed, in my original plan, I had intended to divide my study into periods corresponding to the several phases of the economic cycle so as to discover, what may be called, the "cycle-sensitivity" of the Provincial revenue-and-expenditure system. But as I proceeded in my study, I found that Provincial Finance did not exhibit any close or direct relationship with the phases of the economic cycle, except perhaps the depression phase (1930-35). Such a relationship could, indeed, be established in the case of the Central Government Finances, since the chief Central taxes, the Income Tax, Customs and Excises are highly sensitive to the cyclical changes in the price-and-income structure. The system of Provincial Finance, however, is not responsive to cyclical fluctuations in an equal degree, its main revenue heads, Land Revenue and Excise, being more dependent on administrative and political policy than upon price changes. Yet, these and other revenue heads such as Stamps, Forest, the Scheduled taxes, etc., show a good deal of influence of the wider economic movements, and it has been my endeavour to exhibit this influence at each period.

The plan of the work is as follows: In Part I, I have given a descriptive account of the financial structure of the Province during the period 1921-22 to 1946-47. It contains a somewhat detailed survey of the financial relations between the Central and Provincial Governments, with special reference to the division of the revenue and expenditure heads. This part also embodies an account of each tax and expenditure head of the Provincial Government.

Part II attempts to trace the financial developments in the Province during the following periods: (i) 1921-22 to 1935-36, the period of the Reforms; (ii) 1936-37 to 1939-40 the period of Provincial Autonomy, during the major part of which the popular ministries were in office; (iii) 1940-41, during which period the administration was carried on by the Governor with the help of his Advisors. In each of these periods, I have set forth financial problems and policies, and have endeavoured to assess the achievements by those who were in charge of financial management.

It is not easy for me to express my intellectual debt to Mr. D. R. Gadgil, who has guided me at all stages in my undertaking. Nor, again, can I thank adequately my friend, Mr. N. V. Sovani, who has helped and encouraged me all along. While, however, I recognise my obligations to these kind friends, they are, of course, in no way responsible for any of the facts and opinions stated herein. I must also thank most warmly Messrs. Dev and Kale, of the Servants of India Society's Library, and Mr. Pendse, of the Gokhale Institute, for their unfailing courtesy and assistance. I should also express my obligations to Mr. Bhide, who, as Assistant Keeper of Records, helped me in every way while I was working at the Government Record Office in 1941.

I thank the University of Bombay for the substantial financial help it has granted towards the cost of publication of this book.

University of Pennsylvania, }  
Philadelphia (PA), }  
September 13, 1946. }

T. M. JOSHI

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*I dedicate this book to my parents and to my uncles,  
V. M. Joshi and N. M. Joshi.*

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## CHAPTER I

### FINANCIAL RELATIONS

§ 1. *Historical:* A highly centralised system of government was established by the Charter Act of 1833 which vested complete powers of legislation, administration and finance over the entire territories in India in the Governor-General in Council at Fort William in Bengal. As a result, the Presidencies of Bombay and Madras lost their independent position and became merely administrative agencies. In the field of finance, this meant that the Presidencies collected the taxes and spent the proceeds in the name of the Governor-General of India. Such a state of affairs soon proved to be highly injurious, particularly because it led to "irresponsible extravagance"<sup>1</sup> on the part of Provincial Governments. It was, therefore, felt that unless the Provincial Governments were given independent powers in administration and finance, no improvement in the situation could be looked for. The necessity of relaxing central control was felt particularly strongly after the Mutiny of 1857, which imposed a severe burden on Indian finances, and thus rendered the problem of economy in expenditure highly urgent. In the course of the next decade, schemes for delegating financial powers to the Provinces were prepared by Mr. Wilson, the Finance Member, and his successors. Lord Mayo, the Governor-General, was convinced of the need for such delegation, and his famous Resolution of 1870 marks the beginning of a continuous process of functional and financial devolution from the Central to the Provincial Governments. Lord Mayo's scheme, which came into effect in 1871, provided that certain administrative departments such as Education, Medical Services, Jails, Police, etc., should be under the control of the Provincial Governments, while the receipts from these departments, plus some "assignments" from the Central revenues, were to form the Provincial resources. This arrangement, called by Dr. Ambedkar, "budget by assignments," lasted till the year 1877. It was found, however, that it gave rise to glaring inequalities among Provinces, while it denied them adequate resources for developing the de-

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<sup>1</sup> Ambedkar: "Evolution of Provincial Finances," 1925, p. 29.

partments under their charge. During 1877-82, therefore, a new arrangement was brought into operation at the instance of Sir John Strachey. It was felt that the Provinces ought to be afforded a direct incentive to increase their revenues through an efficient system of collection, for which purpose, certain revenue heads ought to be assigned to them. The Provinces, therefore, were assigned the following revenue heads: excise, stamps, and the licence tax. This system of "assigned revenues" was modified in 1882, when the proceeds of Land Revenue and Income Tax came to be shared between the Central and Provincial Governments. This system of "divided heads" or "shared revenues" was made on a quinquennial basis in 1882; it was made quasi-permanent in 1904, and permanent in 1912.

Though financial decentralization was effected in this way, the Provinces chafed under the system of minute control which the Central Government exercised over their budget estimates, taxation, expenditure and borrowing. The Provincial estimates were incorporated in the Central Government's budget, after being scrutinized and modified by the Central Finance Department. In the sphere of taxation and expenditure, the Provinces had no inherent legal right, as the Acts of 1853 and 1858 gave the Government of India complete control over them. All proposals of fresh taxation and expenditure had to be referred to the Government of India and the Secretary of State for approval. In the matter of routine expenditure also, the Central Government's control, exercised through the several "codes of instruction," was full and detailed. Further, the Provinces possessed no independent powers of borrowing, since legally they were not masters of their revenues. Lastly, accounts, audit, cash balances, ways and means and resource operations were all under the jurisdiction of the Central Government.

The minute control of the Central Government described above was the subject of several protests from the Provincial Governments in the early years of the present century. In 1909, the Secretary of State appointed the Royal Commission on Decentralization to go into the whole question of financial relations between the Central and Provincial Governments and to make recommendations. The Commission, while recognising the evils resulting from the system of "divided heads," was unable to recommend any sudden or violent change in the system; they, however, suggested that excise and forests should be provincialized by gradual stages. The Commission thought that as long as the system of

“divided heads” was in operation, no large or effective relaxation of Central control over Provincial estimates, taxation, expenditure and borrowing, could be thought of, since such a devolution of financial powers would naturally depend upon the broader changes in the general constitutional structure. The Decentralization Commission, however, favoured relaxation of Central control in a large number of minor matters, so as to avoid vexatious interference with the financial administration in the Provinces. Upon their recommendation some measure of financial devolution was effected by Government Resolutions during the years 1910-1917, but on the whole the financial system remained predominantly centralized.

§ 2. *The Joint Report Scheme:* In August 1917, the Secretary of State for India made an important announcement in which he declared that “the policy of His Majesty’s Government with which the Government of India are in complete accord, is that of . . . the gradual development of self-governing institutions with a view to the progressive realization of responsible government in India as an integral part of the British Empire.”<sup>2</sup> Mr. Montagu, the Secretary of State, and Lord Chelmsford, the Viceroy, in their Joint Report on Constitutional Reforms, pointed out that “the Provinces are the domain in which the earlier steps towards the progressive realization of responsible Government should be taken. Some measure of responsibility should be given at once, and our aim is to give complete responsibility as soon as conditions permit. This involves at once giving the provinces the largest measure of independence, legislative, administrative and financial, of the Government of India, which is compatible with the due discharge by the latter of its own responsibilities.”<sup>3</sup> Naturally, the old financial structure, based upon the principle of detailed control over Provincial finance by the Central Government, seemed grossly unsuited to the new constitutional arrangements contemplated. In particular, the system of “divided heads” obviously needed drastic modification, and even abolition; for, as the Joint Report observed:

“If Provincial Autonomy is to mean anything real, clearly the provinces must not be dependent on the Indian Government for the means of provincial development. Existing settlements do, indeed, provide for the ordinary growth of expenditure, but for any large or costly innovations, provincial governments depend

<sup>2</sup> “Report on Indian Constitutional Reforms,” 1919, p. 1.

<sup>3</sup> *Ibid.*, p. 124.

upon doles out of the Indian surplus. Our idea is that an estimate should first be made of the scale of expenditure for the upkeep and development of the services which clearly appertain to the Indian sphere; that resources with which to meet this expenditure should be secured to the Indian Government; and that all other resources should then be handed over to the provincial governments, which will thenceforth be held wholly responsible for the development of all provincial services. This, however, merely means that the existing resources shall be distributed on a different basis. . . .”<sup>4</sup>

The Joint Report recommended that this basis must be the principle of “separation of revenues.” Under the then existing scheme, the “divided heads” were: land revenue, stamps, excise, income-tax, and irrigation. Out of these, land revenue (and, along with it, the expenditure on irrigation and famine relief) must obviously be provincialized, since it is “so intimately connected with the whole administration of rural areas.”<sup>5</sup> As regards stamps, the Joint Report recommended their division into two well-marked sub-heads, viz., general and judicial; the former, in the interest of uniformity to be central, while the latter, provincial. The excise revenue was to be made provincial throughout India. In regard to the income-tax, the Joint Report recommended that it should be completely centralised for several reasons; among others, the desirability of uniform rates throughout the country, and the impossibility of assigning the income-tax proceeds to the Provinces according to the principle of origin.

Such a scheme of re-allocation of revenues, it was estimated by the Joint Report, would give rise to a deficit of Rs. 13,63 lakhs in the Central Government’s budget, while it would afford the Provinces a “gross surplus” of Rs. 15,64 lakhs. It was, therefore, recommended that the Provinces should surrender 87 per cent of their “gross surplus” in the form of contributions to the Central revenues. Table No. 1 gives the relevant figures.

This scheme of allocation of revenues naturally involved the separation of Central and Provincial Budgets, and a general relaxation of Central control over Provincial finance. The Joint Report recommended that Provinces should be given independent powers in the field of taxation, expenditure and borrowing, consistent with the general responsibility of the Government of India for the stability of Indian finances.

<sup>4</sup> *Ibid.*, p. 130.

<sup>5</sup> *Ibid.*, p. 131.

TABLE NO. 1

## GROSS PROVINCIAL SURPLUS AND PROVINCIAL CONTRIBUTIONS

(Source: *Report on Indian Constitutional Reforms*, p. 134)

(In Lakhs of Rupees)

Province	Gross Provincial Surplus	Provincial Contributions (87 Per Cent of Gross Surplus)	Net Provincial
Madras	491	428	63
Bombay	101	88	15
Bengal	79	69	10
United Provinces	375	327	48
Punjab	250	218	32
Burma	161	140	21
Bihar and Orissa	45	39	6
Central Provinces	41	36	5
Assam	21	18	3

The Joint Report scheme of allocation of revenues met with considerable opposition from the Provinces. Industrial provinces, like Bombay, protested against the centralization of the income-tax, and claimed a share in its proceeds. Other provinces like Madras and the United Provinces objected to the disproportionate burden of contribution which they were called upon to pay. These protests were repeated at the Simla Conference held in October 1919, and finally, the Government of India decided to submit the whole question to expert investigation. At their instance, the Secretary of State appointed the Financial Relations Committee with Lord Meston as President.

§ 3. *The Meston Scheme*: The Financial Relations Committee was to advise on:

- the contributions to be paid by the various Provinces to the Central Government for the financial year 1921-22;
- the modifications to be made in the Provincial contributions with a view to their equitable distribution until there ceases to be an all-India deficit;
- the future financing of the Provincial Loan Account;
- whether the Government of Bombay should retain any share of the revenue derived from the income-tax.

The Committee considered it outside their scope to suggest any modification of the general scheme of redistribution or revenues suggested by the Joint Report. As regards the centralization of the income-tax, it agreed with the Joint Report, though it doubted "if it will be possible permanently to exclude the local governments from some sort of direct taxation upon the industrial and commercial earnings of their people."<sup>6</sup> As for the centralization of General Stamps, the arguments of the Joint Report did not weigh much with the Meston Committee, and it recommended that the entire stamp revenue should be provincial.

Under this new arrangement, the amount of the Central deficit was estimated at Rs. 10 crores, composed of Rs. 6 crores as previously estimated by the Government of India, and 4 crores due to the provincialization of General Stamps. This Central deficit, reduced to Rs. 9.83 crores as a result of certain minor financial adjustments, was to be made good by provincial contributions. These were to be of two types, initial and standard. The initial contributions were to be fixed with reference to the immediate needs of the Central Government, but they were not to be such as to force a Provincial Government to resort to fresh taxation. The Committee believed that no province should be forced to do so because of a "purely administrative re-arrangement." It is not easy to share this anxiety to avoid fresh Provincial taxation, particularly because it compelled the Committee to abandon the equitable principle of "capacity to pay" as the basis of contributions. The basis which the Committee adopted was "increased spending power" obtained by a province as a result of the new arrangement. This was not really very different from the Mont-Ford Joint Report basis of "gross surplus" which the Committee rejected; but they claimed great virtue for it. Firstly, "increased spending power" which a province acquired was really a "windfall," resulting from the greater measure of devolution, and therefore, a just basis for contribution. Secondly, "on this basis the system of contributions appears in a less invidious light. The Central Government in the course of 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 a result of this reconstruction, it withholds from each province a certain proportion of the increased resources which it is intended that the provinces should eventually obtain. The Central Government does not come in as raiding the

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<sup>6</sup> "Report of the Financial Relations Committee," 1920, p. 4.

hard-won surplus of a province; nor ought the Central Government to be represented, if our proposals be accepted, as the pensioner of the Provinces.”<sup>7</sup>

The basis of contributions being thus fixed, the next question was, What part of “the increased spending power” should be sliced off for Central purposes? A flat rate on all Provincial figures was not acceptable to the Committee, because it would cause hardship to poor Provinces. The Committee, therefore, proceeded to consider the case of each Province on its own merits and arrived at the following scheme (Table No. 2):

TABLE NO. 2

### INCREASED SPENDING POWER AND CONTRIBUTIONS OF PROVINCES

(Source: *Report of the Financial Relations Committee*, p. 8.)

(In Lakhs of Rupees)

Province	Increased Spending Power	Contribution	Increased Spending Power Left After Contributions Are Paid
Madras	576	346	228
Bombay	93	56	37
Bengal	104	63	41
United Provinces	397	240	157
Punjab	289	173	114
Burma	246	64	182
Bihar and Orissa	51	—	51
Central Provinces	52	22	30
Assam	42	15	27

The Committee frankly admitted that these figures of “initial” contributions could not be regarded as ideal from the point of view of financial adjustment. Rather, they were to be looked upon as representing a workable arrangement based upon “considerations of established programmes of taxation and expenditure, and of legislative and administrative expectations and habits that cannot, without mischief, be suddenly adjusted to a new and more equitable ratio of contribution.”<sup>8</sup>

After having arrived at the “initial” contributions, the Meston Committee proceeded to work out the “standard” contributions.

<sup>7</sup> *Ibid.*, p. 7.

<sup>8</sup> *Ibid.*, p. 10.

In their view, equity required that these latter should be fixed with reference to two considerations. The first was the indirect contribution which a province may already be making to the Central exchequer by way of customs, income-tax, etc., an estimate of which was recognised to be a difficult statistical procedure. The second consideration in fixing the standard contributions was the "capacity to pay" of each province, which also raised difficult problems of statistical computation. The Committee claimed to have made the best use of the available statistical material bearing on these two considerations, and arrived at the results embodied in Table No. 3.

TABLE NO. 3

STANDARD PROVINCIAL CONTRIBUTIONS (PER CENT)  
TO THE CENTRAL DEFICIT

(Source: *Report of Financial Relations Committee*, p. 10)

Madras	17
Bombay	13
Bengal	19
United Provinces	18
Punjab	9
Burma	6½
Bihar and Orissa	10
Central Provinces	5
Assam	2½
Total	100

The Committee further observed that the "process of transition from the initial to the standard rates should be continuous, beginning in the second year of contribution and proceeding in six equal steps." These are summarised in Table No. 4.

§ 4. *Modifications by the Joint Parliamentary Committee:* The Meston Scheme described above was generally acceptable to the Joint Parliamentary Committee which considered the Government of India Bill of 1919. The Committee, however, suggested two modifications:

- (i) that the Provinces should be given a share in the growth of revenues from the income-tax, so far as that growth was attributable to an increase in the amount of the income assessed;
- (ii) that the initial contributions should in no case be increased, while gradual reduction should be the means



of attaining the standard contributions recommended by the Financial Relations Committee.

TABLE NO. 4

PER CENT CONTRIBUTIONS TO DEFICIT IN SEVEN CONSECUTIVE YEARS, BEGINNING WITH THE FIRST YEAR OF CONTRIBUTION

(Source: Report of Financial Relations Committee, p. 11)

(Rounded off to Even Halves)

Province	1st Year	2nd Year	3rd Year	4th Year	5th Year	6th Year	7th Year
Madras	35 1/2	32 1/2	29 1/2	26 1/2	23	20	17
Bombay	5 1/2	7	8	9 1/2	10 1/2	12	15
Bengal	6 1/2	8 1/2	10 1/2	12 1/2	15	17	19
United Provinces	24 1/2	23 1/2	22 1/2	21	20	19	18
Punjab	18	16 1/2	15	13 1/2	12	10 1/2	9
Burma	6 1/2	6 1/2	6 1/2	6 1/2	6 1/2	6 1/2	6 1/2
Bihar and Orissa	—	1 1/2	3	5	7	8 1/2	10
Central Provinces	2	2 1/2	3	3 1/2	4	4 1/2	5
Assam	1 1/2	1 1/2	2	2	2	2	2 1/2
	100%	100%	100%	100%	100%	100%	100%

§ 5. *The Financial Settlement Under the Government of India Act, 1919:* The Financial Settlement which was finally embodied in the Devolution Rules framed under Section 45A of the Government of India Act, 1919, may be summarised as follows:

I. The Principal "Central Subjects" were as follows: the Defence of India; External Relations; Relations with Indian States; Communications including Railways, Aircraft, Inland Waterways, Shipping and Navigation; Major Ports; Posts, Telegraphs and Telephones including Wireless Installations; Customs, Cotton Excise Duties, Income-Tax, Salt, and Other Sources of All-India Revenue; Currency and Coinage; Public Debt of India; Audit; Civil Law; Commerce, including Banking and Insurance; Trading Companies and Other Associations; Control of Production and Development of Industries such as is expedient in the public interest; Opium, Petroleum and Explosives; Geological Survey; Control of Mineral Development; Inventions and Designs; Copyright; Emigration; Criminal Law and Procedure; Central Police Organization; Arms and Ammunitions; Central Agencies and

Institutions of Research; Ecclesiastical Administration; Survey of India; Archaeology; Meteorology; Census and Statistics; All-India Services; Public Service Commission; etc.

II. The Provincial Subjects were divided into two categories, viz., Reserved and Transferred, the former being in charge of Executive Councillors and the latter in that of Ministers responsible to the Legislative Councils.

In the following list of the principal Provincial Subjects, the transferred subjects are shown by an asterisk: \*Local Self-Government; \*Medical Administration; \*Public Health and Sanitation; \*Education; \*Public Works; Water Supplies and Irrigation; Land Revenue Administration; Famine Relief; \*Agriculture; \*Civil Veterinary Department; \*Fisheries; \*Co-operative Societies; \*Forests; \*Excise on Alcoholic Liquors and Intoxicating Drugs; Administration of Justice; Judicial and Non-Judicial Stamps, subject to Central Legislation; \*Registration of Deeds and Documents; \*Registration of Births, Deaths, and Marriages; \*Development of Industries and Industrial Matters; \*Stores and Stationery; \*Adulteration of Foodstuffs; \*Weights and Measures; Ports; Inland Waterways; Police; Excluded Areas; Criminal Tribes; Prisons; Sources of Provincial Revenue; Borrowing Money on the Sole Credit of the Province; etc.

III. The source of Provincial revenue were as under:

- (i) Balances standing at the credit of the Province.
- (ii) Receipts in respect of Provincial subjects including Land Revenue, Excise, Stamps, Forests, Registration, Irrigation, and receipts from fees earned by administrative departments such as Education, Justice, etc.
- (iii) A share in the Income-Tax, to be determined in the manner provided by Rule 15, introduced at the instance of the Joint Parliamentary Committee.

Devolution Rule 15 ran:

"Whenever the assessed income of any year subsequent to the year 1920-21 exceeds in any Governor's Province or in the Province of Burma, the assessed income of the year 1920-21, there shall be allocated to the local Government of that Province an amount calculated at the rate of three pies in each rupee of the amount of such excess."

- (iv) Recoveries of loans and advances given by the local government and of interest paid on such loans.

- (v) Payments made to the local government by the Governor-General in Council or by other local governments, either for services rendered or otherwise.
- (vi) The proceeds of any taxes which may be lawfully imposed for provincial purposes.

The Provincial Legislative Councils were empowered to impose, without the sanction of the Governor-General, the following taxes contained in Schedule I under the Scheduled Taxes Rules:

- (1) A tax on land put to uses other than agricultural.
- (2) A tax on succession or on acquisition by survivorship in a joint family.
- (3) A tax on any form of betting or gambling permitted by law.
- (4) A tax on advertisements.
- (5) A tax on amusements.
- (6) A tax on any specified luxury.
- (7) A registration fee.
- (8) A stamp duty other than duties of which the amount is fixed by Indian legislation.

The Provincial Legislative Councils were also empowered, without the previous sanction of the Governor-General, to impose or to authorize a local authority to impose, any tax contained in Schedule II. This included:

- (1) A toll. (2) A tax on land or land values. (3) A tax on buildings. (4) A tax on vehicles or boats. (5) A tax on animals. (6) A tax on menials and domestic servants. (7) An octroi. (8) A terminal tax. (9) A tax on trades, professions and callings. (10) A tax on private markets. (11) A tax imposed in return for specific service rendered, such as: (a) a water rate; (b) a lighting rate; (c) a scavenging, sanitary or sewage rate; (d) a drainage tax; (e) fees for the use of markets and other public conveniences.

IV. Provincial Contributions. Under Devolution Rule 17 the Provincial contributions for the year 1921-22 were fixed as follows:

<i>Province</i>	<i>Contribution in Lakhs of Rupees</i>
Madras	348
Bombay	56
Bengal	63
United Provinces	240
Punjab	175
Burma	64
Central Provinces and Berar	22
Assam	15

It was further provided by Rule 18 that "from the financial year 1922-23 onwards, a total contribution of 983 lakhs, or such smaller sum as may be determined by the Governor-General in Council, shall be paid to the Governor-General in Council by the local governments mentioned in the preceding rule." It was also provided that if the total contribution was less than the sum mentioned above, the initial provincial contributions would be reduced, whenever they exceeded the following proportions:

Madras, 17/90ths; Bombay, 13/90ths; Bengal, 19/90ths; United Provinces, 18/90ths; Punjab, 9/90ths; Burma, 61½/90ths; Central Provinces and Berar, 5/90ths; Assam, 2½/90ths.

Rule 19 empowered the Governor-General to call upon any Province to pay a contribution in excess of that provided under the foregoing rules, in case of emergency.

V. Famine Insurance. The local governments were to make the following annual assignments for expenditure upon the relief of, and insurance against, famine:

<i>Province</i>	<i>Rupees</i>
Madras	6,61,000
Bombay	63,60,000
Bengal	2,00,000
United Provinces	39,60,000
Punjab	3,81,000
Burma	67,000
Bihar and Orissa	11,62,000
Central Provinces	47,26,000
Assam	10,000

"The annual assignment shall not be expended save upon the relief of famine or the construction of protective irrigation works or other works for the prevention of famine. Any portion of an

assignment which is not so spent shall be transferred to the famine insurance fund of the Province."

VI. Relaxation of Central control over Provincial financial administration: The Provinces were given separate budgets, for the preparation of which Finance Departments were to be established. These departments were charged with the general function of financial management including loans, the famine insurance fund, the scrutiny of proposals for fresh taxation and expenditure, the preparation of the estimates of revenue and expenditure to be submitted to the legislature, re-appropriation of money from major, minor or subordinate heads within a grant voted by the legislature, the framing of financial rules for the guidance of other departments, etc.

The Central Government's control over Provincial expenditure and taxation was considerably relaxed. In respect of "Transferred Subjects," the Governor-General and the Secretary of State were formally divested of their powers of "superintendence, direction and control"; in regard to expenditure on "Reserved Subjects," these powers were retained, but exercised infrequently. In the field of taxation, the Governor-General's sanction was required for imposing any new tax, but this condition was waived in the case of a number of taxes included in the scheduled lists mentioned above.

In the matter of borrowing, the Provincial Governments were given power to raise loans on the security of revenues allocated to them, subject to certain rules, called the "Local Government (Borrowing) Rules."

While, however, the Central Government's control was relaxed in the fields mentioned above, that Government remained as the sole custodian of the revenues of the whole of India. It was provided that "all money derived from sources of provincial revenue shall be paid into the public fund of which the Governor-General in Council is custodian, and is credited to the credit of the Province." Similarly the Central Government was in charge of ways and means and resource operations on behalf of the Provinces, and, therefore, controlled the entire cash balances of the country. Further, the general system of accounts and audit remained in charge of the Central Government.

It will be seen from the account of the financial settlement given above that a good deal of financial devolution was effected

under the Act of 1919. That part of the settlement which was based on the Meston Committee's recommendations, (viz., the allocation of revenues, and the contributions payable by the Provinces), however, met with considerable opposition from the Provinces during the working of the Reformed Constitution.

§ 6. *Criticism of the Financial Settlement of 1919.* The Meston Settlement came in for a good deal of criticism. It was said to have offended against the canons of adequacy and equality which are regarded as basic in any scheme of distribution of revenue between Central and Provincial governmental units. The test of adequacy requires that the revenues assigned to the Central and Provincial governments must be adequate for the functions assigned to them. The canon of equality is satisfied when the several Provincial units find themselves in a fairly equal financial condition as a result of any settlement. The financial arrangements under the Act of 1919 did not satisfy these principles.

In the first place, some Provinces, particularly the advanced Provinces like Bengal and Bombay, suffered from a severe inadequacy of resources throughout the period of the working of the reformed constitution. Most of the Provinces had deficit budgets during the initial period and had to resort to retrenchment and additional taxation.<sup>9</sup> Bengal had a large deficit in the very first year, and upon its representation the Government of India granted that Province a remission of its contribution of Rs. 63 lakhs for three years. While moving the resolution to this effect in the Central Legislative Assembly, Sir Malcolm Hailey, Finance Member with the Government of India, observed:

"We have examined the case both narrowly and critically, and

<sup>9</sup> The Report of the Indian Statutory Commission (1927) gives the following table in lakhs of rupees:

Province	Estimates by Meston Committee of Increased Spending Power Gained by the Provinces Under Its Scheme	Actual Surplus (+) or Deficit (-) in 1921-22
Madras	+228	-99
Bombay	+37	-191
Bengal	+41	-215
United Provinces	+157	-148
Punjab	+114	-171
Burma	+182	+14
Bihar and Orissa	+51	-15
Central Provinces	+30	-24
Assam	+27	-24

it appears certain that with every economy Bengal must have a deficit of not less than Rs. 120 lakhs. Even if we made no allowance for any extra expenditure for improvements in the transferred subjects such as are desired by Ministers... Bengal would have that deficit even if it provided the bare minimum expenditure required to carry on the ordinary administration of the Province."<sup>10</sup>

As a result of the financial stringency, the development of nation-building departments in Bengal was slower than what it could have been.

In Bombay, also, financial stringency was felt acutely. There were, of course, several reasons for this, among others, the costly development programme, increase in the salaries of public servants, etc. But one of the most important factors that contributed to the financial difficulties was the fact that the staple revenues were intrinsically inexpansive, while the functions demanded increasing outlays. This point was stressed by several Finance Members in Bombay, particularly by the veteran Sir Henry Lawrence, who was in charge of Finance for the first six years of the Reform period. Sir Henry blamed the Meston Committee for having adopted a wrong estimate regarding the trends of the principal heads of revenue. The Committee took the figures for the period 1912-13 to 1920-21 and showed that Bombay's revenues had expanded in the following manner:

Excise	102.57 per cent
General Stamps	119.13 " "
Land Revenue	32.00 " "
All Provincial Heads	52.53 " "

The Meston Committee apparently believed that such a rate of increase would continue after 1921, and that, therefore, Bombay would experience no difficulty in meeting the increased expenditure which would have to be incurred under the reformed constitution. The Committee, however, should have taken into account the fact that the period 1912-13 to 1920-21 was one of rising prices, and, therefore, the rate of increase in the revenues recorded in that period could not be regarded as normal and permanent. How completely the Committee miscalculated the probable trend of revenues was shown by the continuous decline of Land Revenue, Stamps and Excise. (Table No. 5.)

<sup>10</sup> Quoted in the Bengal Government's Memorandum to the Indian Statutory Commission, p. 82.

The decline in the principal heads of revenue described above compelled Bombay to resort to retrenchment on the one hand and to additional taxation on the other. We shall describe later the efforts of that Government in these directions. It will be shown that the Meston Settlement considerably narrowed the scope of additional taxation by centralizing the most fruitful and expanding sources of revenue, viz., the income-tax and customs. It was pointed out, particularly by Sir Henry Lawrence, that the province was making a very large *indirect* contribution to the Central revenues by way of income-tax, customs duties, etc., so that its own field of taxation was considerably restricted. This accounted to a certain extent for the paucity of additional taxation in Bombay during the Reform period.

TABLE NO. 5

## DECLINING RECEIPTS FROM THE PRINCIPAL REVENUE SOURCES IN BOMBAY DURING THE REFORMS

(Source: *Bombay Budget, 1935-36*)

(In Lakhs of Rupees)

	1921-22	1928-29	1935-36
Land Revenue	437.2	386.9	371.7
Excise	422.8 <sup>21</sup>	383.4	343.1
General Stamps	164.4	168.4	155.8

The second main defect of the Meston Settlement was that it offended against the principle of equality. It brought into existence glaring inter-provincial inequalities in respect of the financial position. Broadly speaking, it gave vastly increased spending power to the agricultural Provinces like Madras, U. P., and the Punjab, while the industrial Provinces like Madras and Bengal found themselves in financial difficulties.

This inter-provincial disparity was enhanced by two factors: first, the failure of the Devolution Rule 15 which was meant to afford relief to the industrial Provinces; and, second, the abolition of Provincial Contributions in 1927-28.

(a) We have noted that Devolution Rule 15 was introduced at the suggestion of the Joint Parliamentary Committee who in-

<sup>21</sup> The Excise Revenue for the year 1922-23 is here taken, since the receipts for 1921-22 are abnormal for certain accounting reasons.



tended it to afford relief to industrial Provinces which had suffered as a result of the centralization of the income-tax. The rule provided that the Provinces should receive a share of the income-tax calculated at the rate of three pies in the rupee on the amount of the assessed income of any particular year over the assessed income of the year 1920-21. Under this rule Bengal received Rs. 95,000 in 1921-22, and nothing thereafter. Bombay got Rs. 14.7 lakhs in 1921-22 and Rs. 3 lakhs in 1922-23, and nothing in subsequent years. Obviously the rule failed to afford the intended relief to the industrial Provinces. Here again, the real cause of the failure was the adoption of an unsuitable "datum line" for the purpose of calculation. For calculating the "excess" of the assessed income, the basic year adopted was 1920-21, which was the "crest" or the "peak" of the post-war boom. It could, therefore, hardly be expected that the assessed income for subsequent years should greatly exceed that for the year 1920-21. If some other "datum line" had been adopted, the Provincial share would have been much larger, as Table No. 6 shows.

TABLE NO. 6

THE SHARE OF INCOME-TAX OF THE GOVERNMENT OF BOMBAY IF THE DATUM LINE HAD BEEN FIXED IN THE MANNER SHOWN IN COLUMN 1

(Source: *Bombay Government's Memorandum to the Indian Statutory Commission*, p. 639)

(In Lakhs of Rupees)

	1921-22	1922-23	1923-24	1924-25	1925-26	1926-27
1. Average assessed income for three pre-war years: Rs. 19.09.	85	86	64	50	49	46
2. Average assessed income for war years: Rs. 27.80.	71	75	51	37	34	32
3. Average assessed income for three post-war years: Rs. 51.34.	34	38	14	—	—	—
4. Average assessed income for 10 pre-Reform years: Rs. 51.34.	64	68	44	30	27	23
5. Assessed income for 1919-20: Rs. 30.09.	36	40	16	2	—	—

(b) While, thus, the industrial Provinces could not obtain the increased income under the Devolution Rule 15, the agricultural Provinces got a large windfall when the Provincial contributions were abolished in 1927-28. We have seen that these contributions were based upon "increased spending power" which the

Provinces had obtained as a result of the financial settlement. In effect, therefore, they had a tendency to equalize the financial position of the several Provinces. Thus, the Provinces like Madras, U. P., and the Punjab, which had obtained large increases in their spending power, had to pay correspondingly large amounts by way of contribution to the Centre, while Bombay and Bengal had to pay comparatively smaller amounts. When, therefore, the contributions were remitted in 1927-28, the inequality among Provinces was enhanced.

The inter-provincial financial disparities referred to above were reflected in the expenditure trends, especially in respect of the "nation-building" departments like Education, Medical and Public Health, Agriculture, Industries, etc. (Table No. 7.)

TABLE NO. 7

## EXPENDITURE ON SOCIAL SERVICES IN PROVINCES UNDER THE REFORMS

(Source: *Growth of Federal Finance in India*, P. J. Thomas, 1939, p. 517)

(In Lakhs of Rupees)

		Education	Medical	Public Health	Agriculture	Industries	Total
Bombay	1921-22	171	45	29	25	8	278
	1935-36	180	47	24	20	6	277
Bengal	1921-22	119	51	23	15	11	219
	1935-36	130	49	36	15	15	245
Madras	1921-22	143	57	27	20	20	267
	1935-36	254	89	24	28	22	417
U. P.	1921-22	151	23	29	25	9	237
	1935-36	202	32	28	26	12	299
Punjab	1921-22	87	31	10	27	6	161
	1935-36	158	44	10	39	17	268

§ 7. *Sir Walter Layton on the Meston Settlement.* The two principal defects of the Meston Settlement mentioned above were recognised by Sir Walter Layton, the financial expert attached to the Simon Commission. He observed:

“(a) Although the Provinces have expanding needs, the sources of revenue assigned to them are insufficient and show no signs of adequate growth, whereas the Central sources of revenue which have to meet comparatively stationary needs are expanding or capable of expansion.

“(b) It has treated the Provinces unequally by giving some of them a much greater proportionate increase of revenue than others.

“(c) It has given practically no power to the Provinces to tax industrial activities, and has, therefore, handicapped the industrial Provinces as contrasted with the agricultural ones.”<sup>12</sup>

§ 8. *Revision of the Meston Settlement:* The Government of Bombay carried on a ceaseless campaign against the Meston Settlement and emphatically urged its revision on several occasions. In its well-written Memorandum to the Indian Statutory Commission, the Government of Bombay set forth its criticisms and proposals of revision of the Settlement in a most convincing manner. In particular, it stressed its claim for a larger share in the proceeds of the income-tax, in view of its great contribution to those proceeds through its industrial and commercial activities. Sir Walter Layton recognised this claim in his scheme of federal finance, in which he recommended that 50 per cent of the income-tax should be allocated to the Provinces according to the principle of “origin.” The Scheme also embodied some proposals to assist the poorer Provinces by granting them a share in the Central excise revenue, determined with reference to population. The Layton Scheme, in spite of its general soundness, was, however, neglected at the Round Table Conferences, when the Peel and Percy Committees were appointed to go into the question of federal finance and to make recommendations. The two Committees concocted a most complicated scheme of distribution of revenues between the Central and Provincial governments, involving a system of contributions and counter-contributions. Though this scheme did not materially influence the final settlement as embodied in the Government of India Act of 1935, it recognized categorically the claim of the Provinces for a substantial share of the income-tax.

<sup>12</sup> “Report of the Indian Statutory Commission,” Vol. II, 1928, p. 214.

## CHAPTER II

### FINANCIAL RELATIONS UNDER THE NEW CONSTITUTION

§ 1. *The Government of India Act, 1935*: The Government of India Act of 1935 embodied a federal constitution based upon the principle of Provincial Autonomy. It contains a scheme of allocation of functions and revenues between the Central (Federal) and Provincial Governments so as to afford a large measure of independence to the latter. This scheme is examined with special reference to Bombay in this and the following chapters; this chapter deals with the allocation of revenue and expenditure heads; and the next, with the question of loans and cash balances.

§ 2. *Federal and Provincial Subjects*: Under the Act of 1935 governmental functions were divided into three categories: federal, provincial, and concurrent. The Federal Legislative List includes, among others: Defence, Ecclesiastical Affairs, Currency and Coinage, Posts and Telegraphs, Broadcasting, Federal Public Services, Survey of India, Imports and Exports, Federal Railways, Maritime Shipping and Navigation, Arms and Ammunition, Insurance, Banking, Excise (except on alcoholic drugs and other intoxicants), Taxation of Income (other than agricultural income), Customs, Succession Duties (other than those on agricultural land); Stamp Duties on bills of exchange, Cheques, etc; Terminal Taxes, etc; and fees in respect of federal matters.

The following constitute the major items in the Provincial Legislative List: Public Order, Justice, Police, Local Government, Public Health and Sanitation, Education, Communications such as are not mentioned in the Federal Legislative List; Agriculture, Veterinary and co-operation, Forests, Trade and Commerce within the Province, Development of Industries, Excise on alcohol, hemp, opium, etc; Amusements, Gambling and Betting; Land Revenue; Taxes on Agricultural Income; Succession Duties in respect of agricultural land, etc.

The Concurrent Legislative List contained: Criminal Law and Procedure, Civil Procedure, Marriage and Divorce, Wills, Trusts, Contracts, Arbitration, the Professions, Newspapers, Books and Printing Presses, Lunacy, Prisons, Prevention of Cruelty to Animals, Criminal Tribes, etc.

§ 3. *Federal Revenues:* The foregoing three lists were included in Schedule VII of the Act. The distribution of revenues was contained in Chapter I, Part VII of the Act. Under it the "revenues of the Federation" were as follows:

- (i) Taxes on Income other than agricultural income (provided that a prescribed percentage of the proceeds shall be assigned to the Provinces).
- (ii) Corporation Tax.
- (iii) Duties on Salt (if, however, an Act of the Federal Legislature so provides, the whole or part of the net proceeds of such duties was to be distributed among Provinces and States according to such principles as may be formulated by the Act).
- (iv) Customs Duties, including export duties (in respect of the latter, it was provided that half or more of the export duty on jute was to be assigned to the Provinces in which jute was grown).
- (v) Excise Duties on Tobacco, and other goods manufactured or produced in India, (except alcoholic liquors, opium, Indian hemp, etc.)
- (vi) Taxes on the capital value of assets, exclusive of agricultural land.
- (vii) Income from Railways, Posts and Telegraphs, the Reserve Bank, etc.
- (viii) Fees in respect of matters coming within the Federal Legislative List.

§ 4. *Provincial Revenues:* The several items which constituted the Provincial revenues could be classified as under:

- (A) Provincial share of the taxes levied and collected by the Federation.
  - (i) The Provincial share of the income-tax (50 per cent as fixed by the subsequent Order-in-Council).
  - (ii) Provincial share of the Jute Export Duty (62½ per cent as fixed by the subsequent Order-in-Council).
  - (iii) Salt duties and other excises except on alcoholic liquors and narcotic drugs (whole or such part of the net pro-

ceeds as shall be determined by an Act of the Federal Legislature).

(B) Taxes levied and collected by the Federation but assigned to the Provinces:

- (i) Duties in respect of property other than agricultural land.
- (ii) Stamp duties on bills of exchange, cheques, promissory notes, etc.
- (iii) Terminal taxes on goods and passengers carried by railway or air.
- (iv) Taxes on railway fares and freights.

(C) Taxes levied and collected by Provinces:

- (i) Land Revenue and Irrigation receipts.
- (ii) Excise duties on—
  - (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 (b).
- (iii) Taxes on agricultural income.
- (iv) Taxes on lands and buildings, hearths and windows.
- (v) Duties in respect of succession to agricultural land.
- (vi) Taxes on mineral rights subject to any limitations imposed by any Act of the Federal Legislature relating to mineral development.
- (vii) Capitation taxes.
- (viii) Taxes on professions, trades, callings and employments, subject to the provisions of Section 124 A(1) of the Government of India Act.
- (ix) Taxes on animals and boats.
- (x) Cesses on the entry of goods into a local area for consumption, use, or sale therein.

- (xi) Taxes on luxuries including taxes on entertainments, amusements, betting and gambling.
- (xii) Dues on passengers and goods carried by inland waterways.
- (xiii) Tolls.
- (xiv) Forests.
- (xv) Stamp duties in respect of documents other than those specified in the Federal Legislative List (e.g. bills of exchange, cheques, promissory notes, etc.)
- (xvi) Taxes on the sale of goods and on advertisements.
- (xvii) Fees in respect of any matter, included in the Provincial Legislative List, but not including fees taken in any Court.

§ 5. *The Niemeyer Award:* In January 1936 Sir Otto Niemeyer was appointed to make recommendations in respect of (a) the allocation of the Income-Tax to the Provinces; (b) the share of the Jute Export Duty to be given to the jute-growing Provinces, and (c) grants-in-aid to Provinces from the Central revenues. Sir Otto Niemeyer's recommendations and the effect given to them by subsequent "Orders-in-Council" are given below.

Sir Otto Niemeyer's inquiry and recommendations were based upon two fundamental considerations. On the one hand he 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. My first object, accordingly, has been to examine the present and prospective financial position of the Provinces and to determine the extent to which special assistance would be needed in order to achieve the above aim." While thus it was first necessary to enable the Provinces to start "on an even keel," it was equally important to see that the solvency of the Central Government was not jeopardised, since "the financial stability and credit of India as a whole must remain the paramount consideration."<sup>1</sup>

After laying down the foregoing principles, Sir Otto proceeded to examine the position of the Provinces so as to find out whether

<sup>1</sup> Indian Financial Inquiry Report, 1937, p. 2.

and to what extent financial assistance should be given to them out of Central revenues. In this connexion he noted that certain Provinces had already gained as a result of the re-arrangement of the Provinces under the new Constitution. Thus Bombay had received an annual relief to the extent of approximately Rs. 90 lakhs from the separation of Sind;<sup>2</sup> Madras and Bihar had gained Rs. 20 lakhs and Rs. 8 lakhs respectively from the separation of Orissa. The newly constituted Provinces, and some older ones, would undoubtedly need financial assistance if they were to balance their budgets. After examining the individual cases, the following grants were recommended:

- (i) Sind: Rs. 105 lakhs for the first ten years, to be diminished by Rs. 25 lakhs a year for the next 20 years, by Rs. 40 lakhs a year for the next 5 years, by Rs. 45 lakhs a year by the next succeeding 5 years, and thereafter until the whole barrage debt is repaid by Rs. 50 lakhs a year.
- (ii) Orissa: The total assistance proposed was Rs. 57 lakhs in the first year, Rs. 53 lakhs in the next four years, and thereafter Rs. 50 lakhs a year.
- (iii) Assam: Rs. 45 lakhs a year.
- (iv) North-West Frontier Province: The Province had been receiving an annual subvention of a crore of rupees from the Central Government since 1932; it was recommended that this should be raised by Rs. 10 lakhs a year for the first 5 years.
- (v) Other Provinces: Bengal, Rs. 75 lakhs; Bihar, Rs. 25 lakhs; Central Provinces, Rs. 15 lakhs; United Provinces, Rs. 25 lakhs.

The financial assistance mentioned above was to be given, in the case of some Provinces, through the cancellation of the pre-Autonomy debt owed by the Provinces to the Central Government. This would mean an annual saving for the Provinces of the following order: Bengal (Rs. 33 lakhs); Bihar (Rs. 22 lakhs); Assam (Rs. 15½ lakhs); North-West Frontier Province (Rs. 12 lakhs); Orissa (Rs. 9½ lakhs); Central Provinces (Rs. 15 lakhs).

Further, a part of the assistance contemplated above was to be given in the form of an increase in the percentage of the Jute Export Duty assigned to the jute-growing Provinces. The Govern-

<sup>2</sup> As a matter of fact, the gain was only 75 lakhs.



ment of India Act had fixed the Provincial share at 50 per cent; this was to be raised to 62½ per cent, as a result of which Bengal would gain Rs. 42 lakhs, Bihar Rs. 2½ lakhs, Assam Rs. 2½ lakhs, and Orissa slightly over Rs. ¼ lakh.

Even after the cancellation of debt and increase in the share of the Jute Export Duty, some direct help had to be given in some cases in order to complete the scheme of assistance outlined above. For this purpose, Sir Otto Niemeyer recommended the following direct subventions from the Central Revenues:

United Provinces: Rs. 25 lakhs, for a fixed period of five years.

Assam: Rs. 30 lakhs.

N.-W. F. Province: Rs. 100 lakhs, subject to reconsideration at the end of five years.

Orissa: Rs. 40 lakhs with Rs. 7 lakhs additional in the first year, and 3 lakhs additional in each of the next four years.

Sind: Rs. 105 lakhs for 10 years with Rs. 5 lakhs additional in the first year, then diminishing as indicated above.

The next question was that of the assignment of a share in the proceeds of the income-tax to the Provinces. In this connexion Sir Otto Niemeyer had to balance and reconcile two considerations. "On the one hand, there is the vital necessity of safeguarding the financial stability of the Centre. On the other hand, having regard to the obvious future needs of the Provinces and in order to maintain a reasonable adjustment of relative burdens between the various units, it is clearly very desirable that the maximum practicable distribution should be achieved."<sup>3</sup> After balancing these considerations Sir Otto recommended that 50 per cent of the income-tax should be assigned to the Provinces.

This being settled, the next question was "what amount of this 50 per cent and for what periods should temporarily be retained by the Federation" [Section 138(2)]? In this connexion Sir Otto pointed out that during the initial period the Central Government would have to make certain financial adjustments arising out of the inauguration of the new Constitution, such as the Separation of Burma, the entry of the States into the Federation, etc. For this reason the Central Government would be justified in re-

<sup>3</sup> *Ibid.*, p. 11.

taining a part of the Provincial share of the income-tax for a period of five years. The sum so retained might be the whole of the Provincial share, or "such sum as is necessary to bring the proceeds of the 50 per cent share accruing to the Centre, together with any General Budget receipts from the Railways upto 13 crores, whichever is less."<sup>4</sup>

The third question relating to the income-tax was that of the distribution of the Provincial share among the Provinces. In regard to this Sir Otto Niemeyer pointed out that no particular basis of distribution suggested (e.g. population, origin, etc.) was completely satisfactory. The basis of "origin" or "residence" would be favourable to the industrial Provinces, but it would not constitute a scientific criterion for distribution, since residence is largely a matter of accident. The population basis, on the other hand, would satisfy the poor Provinces, but would penalise the more advanced ones. The two bases, therefore, would have to be properly co-ordinated in a practical and equitable scheme of distribution of the proceeds of the income-tax among the Provinces. In view of this, the following percentages were recommended: 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). These percentages would have to be slightly altered after the entry of the States into the Federation.

The foregoing recommendations were brought into effect by "the Government of India (Distribution of Revenues) Order, 1936."

§ 6. *The Provinces Under the New Settlement:* We have now described the main features of the allocation of revenues between the Central and Provincial Governments as laid down by the Government of India Act, 1935, and by the subsequent Orders-in-Council based upon the Niemeyer recommendations. We must now examine the position of the Provinces in general and of Bombay in particular under this financial settlement.

It will be noted that the new financial Settlement reintroduced the system of "shared revenues," which was formally given up in 1919. It has been found from our own experience, as well as that of other federal constitutions, that a clear-cut separation of revenues is not always possible. It is well, therefore, that no such

<sup>4</sup> *Ibid.*, p. 12.

attempt was made in the financial arrangements under the new Constitution.

The new financial Settlement embodied some changes which were favourable to the Provinces, especially the industrially advanced ones. Thus, firstly, the Provincial share of the expanding central taxation had been increased; and secondly, the Provincial sphere of taxation had been widened, so as to enable the Provinces to tax some of the expanding sources within their territorial limits. While, however, the Provinces generally gained in these two ways, there were several difficulties in the full realization of this benefit by the Provinces. These two points are discussed in some detail below:

I. The first point relates to the increased share of the Provinces in the proceeds of Central taxation. Here we have to note three things:

- (a) The Act laid down' [Section 140(17)] that duties on Salt, Federal duties of Excise, shall be levied and collected by the Federation, but if an Act of the Federal Legislature so provides, the whole, or any part of the net proceeds of the duties shall be distributed among the Provinces. Similarly, Section 137 provided that duties in respect of succession to property other than agricultural land, certain stamp duties, terminal taxes, and taxes on railway fares and freights, shall be levied and collected by the Federation, but that their net proceeds shall be distributed among the Provinces and States, if any, in accordance with such principles as may be formulated by an Act of the Federal Legislature. It was clear, however, that nothing could come out of these provisions until the Federation part of the Constitution came into existence.
- (b) In regard to the sharing of the Jute-Export Duty by the jute-growing Provinces [Section 140(2)], it was made effective by the Government of India (Distribution of Revenues) Order of 1936. Under the arrangement the Jute-growing Provinces had received the sums as shown in Table No. 8.
- (c) The third, and the most important "shared" revenue was the income-tax. In regard to this, the fixation of the Provincial share at 50 per cent had been generally well-received. But most Provinces complained about the

TABLE NO. 8

PROVINCIAL RECEIPTS FROM JUTE EXPORT DUTY  
SINCE 1937-38

(Source: Reports on Currency and Finance, Reserve Bank  
of India.)

(In Lakhs of Rupees)

Province	1937-38	1938-39	1939-40	1940-41	1941-42	1942-43
Bengal	237.81	221.27	221.97	159.17	165.55	119.09
Bihar	13.66	17.12	19.34	14.48	16.14	10.92
Orissa	1.94	0.92	0.92	0.88	1.00	0.65
Assam	11.75	11.69	13.39	10.59	12.48	9.64

provision relating to the retention of their share by the Centre for the first few years. The provision that the Centre should retain the whole, or such part of the Provincial share, as together with the Railway contribution, would bring its share to Rs. 13 crores, was particularly criticised by the Provinces, since it made the accrual of their share dependent upon Railway receipts over which they had no control.<sup>5</sup> As a result of these protests, the provision was modified with effect from April 1939. According to the revised Order-in-Council, the sum which the Central Government might retain out of the Provincial share was to be Rs. 4½ crores a year during the period 1939-42. This revised order immensely benefited the Provinces, especially Bombay and Bengal, as figures in Table No. 9 show.

We now turn to the second point referred to above, viz., the widening of the sphere of Provincial taxation. Under the Meston Settlement, the Provinces, particularly the industrial ones, had been denied the opportunities of taxing the expanding sources of income arising out of the professional, industrial and commercial activities. The Provincial Legislative List under the Act of 1935, however, mentioned at least two important items of such a nature, viz., taxes on the sale of goods and on advertisements; and taxes on professions, trades, callings, and employments. These two types of taxation, however, raised important legal issues regarding the jurisdiction of Provincial Governments.

In 1938 the C. P. and Berar Government imposed a tax on the retail sale of motor spirit and lubricants. The Government of

<sup>5</sup> Cf. Correspondence between the Local Governments and the Government of India on the Recommendations of the Niemeyer Report.

TABLE NO. 9

TOTAL PROVINCIAL RECEIPTS OF INCOME-TAX SINCE  
1937-38

(Source: Reports on Currency and Finance, Reserve Bank of India.)

(In Lakhs of Rupees)

Province	1937-38	1938-39	1939-40	1940-41	1941-42	1942-43	1943-44
Bombay	25.00	30.00	53.80	60.00	147.80	218.00	390.00
Bengal	25.00	30.00	55.80	60.00	147.80	218.00	390.00
Madras	18.75	22.50	41.85	45.00	110.85	163.50	292.50
Punjab	10.00	12.00	22.32	24.00	59.12	67.20	156.00
U. P.	18.75	22.50	41.85	45.00	110.85	163.50	292.50
C. P.	6.25	7.50	13.95	15.00	36.95	54.50	97.50
Bihar	12.50	15.00	27.90	30.00	73.90	109.00	195.00
Orissa	2.50	3.00	5.58	6.00	14.78	21.80	39.00
N.-W. F. P.	1.25	1.50	2.79	3.00	7.39	10.90	19.50
Assam	2.50	3.00	5.58	6.00	14.78	21.80	39.00
Sind	2.50	3.00	5.58	6.00	14.78	21.80	39.00

India, however, objected to this measure on the ground that it amounted to an excise duty, which, being included within its own legislative sphere, was *ultra vires* of the Provincial Legislature. The Federal Court, however, upheld the right of the Provincial Government to impose sales taxes, and in this connexion, it made a distinction between Excise Duties and Sales Taxes. The Federal Court observed:

"The Central legislature will have the power to impose duties on excisable articles before they become a part of the general stock of the Province, that is to say, at the stage of manufacture or production, and the Provincial legislature an exclusive power to impose a tax on sales thereafter."<sup>6</sup>

The Employment Tax also raised similar controversies in regard to the jurisdiction of the Provincial and Central Governments. In 1939-40 the United Provinces Legislature imposed a progressive Employment Tax on all salaries in excess of Rs. 2,500 a year. Such a tax, obviously, was nothing more or less than a "special" income-tax, and as such, coming within the Central sphere. The point was referred to the Secretary of State, at whose instance, the Government of India Act of 1935 was modified so as to remove all doubts regarding the jurisdictions of the Provincial and Central Governments. Provincial Legislative List now includes "taxes on

<sup>6</sup> Quoted by B. V. Narainswami Naidu: *The Madras General Sales Tax Act, A Study*, 1940, p. 28.

professions, trades, callings, and employments, subject, however, to the provisions of Section 124 A(1) of the Government of India Act." This Section runs: "That the total amount payable in respect of any person to the Province or to any one municipality, district board, local board, or other local authorities in the Province by way of taxes on professions, trades and callings and employments shall not after 31st day of March, 1939, exceed Rs. 50 per annum."

In 1939 Madras and Bombay also imposed sales taxes. The Madras Sales Tax was objected to by the Central Government and the issue was taken to the Federal Court. The Federal Court decided in favour of the Madras Government. It observed: "The sales tax on a manufacturer or producer cannot be distinguished from a tax on other sales and therefore it was within the competence of the Provincial Legislatures." (Cf. Federal Law Journal of India, Vol. VI, 1945.)

§ 7. *Bombay Under the New Settlement:* The Government of Bombay were not satisfied with the financial arrangements made under the Act of 1935, and particularly with the recommendations of Sir Otto Niemeyer. In their telegram to the Government of India on the Niemeyer Report, they observed:

"While fully accepting paramount need for financial stability at Centre and necessity for so equipping all Provinces as to give them a reasonable prospect of reaching and maintaining financial equilibrium, Government of Bombay feel strongly that case of this Presidency does not appear to have received the consideration it merited, inasmuch as no steps have been proposed to correct position in which Province of Bombay has been involved by reason of inequity and inherent unsoundness of Meston Settlement including falsification of forecast made by Meston Committee, the complete failure of anticipations of Percy Committee, the cost of development schemes in Bombay City undertaken at behest of Secretary of State, and long drain on Presidency proper caused by its association with Sind. The financial difficulties caused by these circumstances and more recent economic disturbances common to all Provinces have been met by Bombay Government enforcing most rigid retrenchment supplemented by emergency taxation. The retrenchment measures have produced an approximate immediate annual saving of some 150 lakhs, but it has been clearly recognized from the beginning that a very large proportion of this retrenchment is unobtainable. The additional emergency taxa-

tion at present yields 72½ lakhs annually in Presidency excluding Sind.”<sup>1</sup>

Though, in this way, perfect justice could not be said to have been done to Bombay, it is obvious that, on the whole, the Province was much better off under those arrangements than it was during the Reform period. The two outstanding gains to the Province were the separation of Sind, and the share of the income-tax. The former was wrongly estimated in the Niemeyer Report at Rs. 90 lakhs; the exact figure contained in the Bombay Budget for 1936-37 was Rs. 76 lakhs. But the latter was by no means a mean figure, and Bombay had good reason to be grateful for it. In regard to the income-tax, Bombay's share during the first three years was not very large. But since 1939, when the revised order regarding the retention of the Provincial share by the Centre came into effect, Bombay's share has been substantial, as shown in Table No. 9.

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<sup>1</sup> Correspondence, *op. cit.*, p. 3.

## CHAPTER III

### FINANCIAL RELATIONS: LOANS AND CASH BALANCES

§ 1. *Provincial Borrowing:* Before the Reforms the Provincial Governments had no independent borrowing powers. Loans were given to them by the Central Government out of the Provincial Loans Account. The Act of 1919 recognised independent borrowing powers on the part of Provinces on the security of their own revenues. The sanction of the Governor-General was, however, required for loans raised in India, and that of the Secretary of State for loans raised abroad. The power of borrowing was to be exercised in accordance with the so-called "Local Government Borrowing Rules," framed under the Act of 1919. These rules allowed the Local Governments to raise loans on the security of their revenues for the following purposes:

(a) To meet capital expenditure on the construction or acquisition (including the acquisition of land, maintenance during construction and equipment) of any work or permanent asset of a material character in connexion with a project of lasting public utility, provided that: (i) the proposed expenditure is so large that it cannot reasonably be met from current revenues, and (ii) if the project appears to the Governor-General in Council unlikely to yield a return of not less than such percentage as he may from time to time by order prescribe, and arrangements are made for the amortization of the debt;

(b) to meet any classes of expenditure on irrigation which had under the rules in force before the passing of the Act been met from loan funds;

(c) for the giving of relief and the establishment and maintenance of relief works in times of famine or scarcity;

(d) for the financing of the Provincial Loans Account; and

(e) for the repayment and consolidation of loans raised in accordance with these rules or the repayment of advances made by the Governor-General in Council."

During the first few years of the working of the Reformed Constitution, many Provinces raised loans under these rules. Bombay, for instance, borrowed large sums of money for the development schemes. It was, however, found that the Provinces



could not borrow on as easy terms as the Central Government could, and hence, the Provinces found it increasingly advantageous to borrow from the Central Government. In order to regularise such Provincial loans out of the Central Exchequer, a Provincial Loans Fund was instituted in 1925. The Provincial Governments, thereafter, resorted to this Fund for loans, instead of borrowing in the open market.

Under the new Constitution, the right of the Provinces to raise loans on the security of their own revenues had been recognised. The Act of 1935, laid down, under Section 163:

“(1) Subject to the provisions of this section the executive authority of a Province extends to borrowing upon the security of the revenues of the Province within such limits as may from time to time be fixed by the Act of the Provincial Legislature and to the giving of guarantees within such limits, if any, as may be so fixed.

“(2) The Federation may, subject to such conditions, if any, as it may think fit to impose, make loans to, and so long as any limits fixed under the last preceding section are not exceeded, give guarantee in respect of loans raised by, any Province and any sums required for the purpose of making loans to a Province shall be charged on the revenues of the Federation.

“(3) A Province may not without the consent of Federation borrow outside India, nor without the like consent raise any loan if there is still outstanding any part of a loan made to the Province by the Federation or by the Governor-General in Council, or in respect of which a guarantee has been given by the Federation or by the Governor-General in Council.

“Its consent under this subsection may be granted subject to such conditions, if any, as the Federation may think fit to impose.

“(4) A consent required in the last preceding section shall not be unreasonably withheld, nor shall the Federation refuse, if sufficient cause is shown, to make a loan to, or give a guarantee in respect of a loan raised by, a Province, or seek to impose in the matters aforesaid any condition which is unreasonable and, if any dispute arises whether a refusal of consent, or a refusal to make a loan to or give guarantee, or any condition insisted upon, is not justifiable, the matter shall be referred to the Governor-General and the decision of the Governor-General in his discretion shall be final.”

Under the foregoing rules the Provinces could borrow independently in the open market. Upon the inauguration of Provincial Autonomy, therefore, the old Provincial Loans Fund was wound up (31st March, 1937), and all Provincial debts to the Central Government were "consolidated" in accordance with the recommendations of Sir Otto Niemeyer.

At the commencement of Provincial Autonomy, the Bombay Government owed to the Government of India a debt of Rs. 33.15 crores. This was made up as follows: (a) Rs. 10.61 crores borrowed from the Central Government in order to be re-lent to the Bombay Municipal Corporation. (b) Rs. 4.12 crores borrowed and then advanced to the Bombay Improvement Trust. This and the foregoing were the responsibility of the Bombay Corporation. (c) Rs. 18.42 crores of "pre-Autonomy" debt. The total debt had been consolidated at the rate of 4½ per cent and made repayable over a period of forty-five years. The annual debt charge on account of this comes to a little less than a crore of rupees. The principal elements of this debt were: (i) Rs. 7.44 crores of the Bombay Development loan. (ii) Rs. 4.62 crores on account of Irrigation works. (iii) Rs. 4.89 crores on account of P. W. D. works such as buildings, bridges and water-works. (iv) Rs. 1.47 crores representing advances taken for financing the Provincial Loans and Advance Account. This was re-lent to cultivators, minor Municipalities and housing societies.

§ 2. *Cash Balances*: Besides balancing the total revenue and expenditure for a year, a government has to make arrangements to meet expenditure from day to day and month to month at numerous different centres. These are called "ways and means" and "resource" operations. The expenditure of a government is, generally speaking, uniformly distributed over the year; the revenue receipts, on the other hand, tend to be large in some months and small in others. In India, for instance, from January to June, the receipts are fairly heavy, and exceed the normal disbursements; for the next three or four months, the receipts decline and a deficit has to be faced. In order to enable the government to meet such a situation, "cash balances" are required to be maintained in the interest of solvency. Obviously the size of the balances must depend upon a variety of considerations, such as the volume of disbursements, the size of the country, the development of banking, etc. Financial prudence consists in having a cash balance which is neither so small as to endanger safety, nor so large as to involve waste of resources.

Before the inauguration of Provincial Autonomy, the Central Government was solely responsible for the resources and ways and means of operations. Through its treasury system, and through the branches of the Imperial Bank, the Central Government provided funds at every centre sufficient for its disbursements. Again, it was the sole custodian of the all-cash balances of the country, and was responsible for meeting all expenditures on behalf of the Central and Provincial Governments. Before the Reforms the Central Government required the Provincial Governments to maintain minimum cash balances at their credit. The latter were not allowed to have a budget deficit, particularly such as to involve a reduction of their cash balance below the minimum level. After the Reforms these restrictions were abolished, but the position of the Central Government as the custodian of all balances was retained. Thus, Devolution Rule 16 prescribed that all Provincial revenues were to be paid into the Central Government's Public Account, while the "Treasury Orders" framed under Rule 16 laid down the procedure regarding the payment, withdrawal, transfer, and disbursement of public funds. Further, under Devolution Rule 29, the Provinces were required to maintain the Statutory Famine Fund with the Central Government. All these funds, along with others such as the revenue surpluses of past years, the unexpended balances of loans, Depreciation Funds, Road and Rural Development Fund, etc. formed the "Treasury Balances" of the Government of India. Further, the Government also held cash in the Gold Standard Reserve and the Paper Currency Reserve.

The size of the Indian Treasury balances has long been a much-discussed topic. In the early years of the present century, the Government was severely criticised for holding unduly large cash balances in their treasuries and in the Presidency Banks. The Chamberlain Commission of 1913 also held that the balances were unusually large, but that there were "accidental" causes to explain this. The fact, however, was undoubtedly responsible for monetary stringency and consequent high level of money rates. The situation was a bit improved when, after the inauguration of the Imperial Bank, the Central Government transferred the major part of its Treasury balances to that institution, which was allowed to use them under certain restrictions. Similarly, in 1923, the Controller of Currency was authorised to issue currency notes of the value of 12 crores of rupees against bona fide "hundis" when the bank rate rose to 6 per cent or more.

With the inauguration of Provincial Autonomy, the Central

Government divested itself of the responsibility for ways and means and resource operations on behalf of the Provinces. The Provinces, therefore, have been required to make their own arrangements in this regard. Naturally there followed a "decentralization of balances," i.e. the Central Government turned over to the Provincial Governments all the cash balances which it held on their behalf, including their Famine Funds, Depreciation Funds, the unspent amounts of the Road and Rural Development Funds, and several other deposits. The Provinces are now required to make their own arrangements regarding the custody and management of their cash balances with the Reserve Bank. Under these arrangements the Provincial Governments had to keep a minimum balance with the Reserve Bank, and to maintain cash or "till money" in their treasuries. The remaining balances were used for writing off a part of the Provincial debt as recommended by Sir Otto Niemeyer. Arrangements were also made for obtaining "ways and means" advances from the Reserve Bank whenever there was a shortage of funds. Under such circumstances, the Provincial Governments were also empowered to issue Treasury Bills, or to raise loans of a more permanent character.

Under this new arrangement Bombay's cash balance position has been as follows: The Government is required to keep a minimum balance of Rs. 30 lakhs with the Reserve Bank, and another Rs. 14 lakhs as "till money" in the treasuries. Besides these, the Bombay Government holds a number of earmarked balances, of which the amounts at the commencement of Provincial Autonomy were as follows:

	Lakhs of Rupees
1. Central Road Development Fund	41.29
2. Provincial Road Fund	4.24
3. Press Depreciation Reserve Fund	1.69
4. Nasik Distillery Depreciation Fund	5.05
5. Undischarged Bombay Development Loan	2.47
6. Grants received for specific purposes	4.36

The Government had a "free balance" of Rs. 63 lakhs on the 1st of April, 1937. Besides this and the foregoing cash balances, Bombay had Rs. 59 lakhs in the Famine Fund and Rs. 12½ lakhs in the Nasik Distillery Depreciation Reserve Fund, both held in Government of India securities. Another Rs. 4.74 lakhs belonging to the Provincial Road Fund were held in Treasury Bills.

## CHAPTER IV

### THE STRUCTURE OF THE REVENUE SYSTEM

§ 1. *The Principal Sources of Revenue:* The purpose of this chapter is to give a general description of the structure of the Bombay tax system in order to enable the reader to follow the analysis of financial developments presented in Part II. The next chapter is devoted to a similar description of the Expenditure System. These two chapters may be regarded as an introduction to the study of Bombay's finance during the period 1921-22 to 1945-46.

During the two administrative periods covered by these years, the revenue system of Bombay has embodied the following principal heads: (i) A Share of the Income-Tax. (ii) Land Revenue. (iii) Excise on Alcoholic Liquors, Opium and Hemp, etc. (iv) Stamps. (v) Registration. (vi) Forest. (vii) Motor Vehicles Taxes. (viii) Other duties e.g. tobacco duties, electricity duty, etc. (ix) Minor taxes, viz., entertainment tax, and betting tax. (x) Irrigation Revenue. (xi) Departmental Receipts.

§ 2. *Taxes on Income:* Under Devolution Rule 15 framed under the Government of India Act of 1919, the Provincial Government was to receive from the Central Revenues "a sum calculated at the rate of three pies in the rupee on the amount by which the assessed income of the year exceeds the assessed income of the year 1920-21." As pointed out earlier, this rule failed to afford any relief to the industrial Provinces intended by the Joint Parliamentary Committee at whose instance it was introduced. As already observed, Bombay received under this rule Rs. 14.7 lakhs in 1921-22, Rs. 3 lakhs in 1922-23, and nothing during the subsequent years of the Reform period. The obvious reason for the failure of this rule was the choice of the year 1920-21 as the basic year for calculating the excess of assessment. That year was almost the peak of the post-war boom, and therefore, the income-tax assessment had almost reached its maximum level. The assessment for 1921-22 showed some excess, but since that year it dropped off very rapidly.

The failure of this rule affected Bombay's financial position very adversely. The Bombay Government, therefore, made strenuous attempts to get the whole position revised so that it

could obtain more revenue out of the income-tax proceeds. The case of industrial Provinces like Bombay for a larger share in the income-tax was favoured by the financial assessor attached to the Indian Statutory Commission, and by the Peel and Percy Committees of the Round Table Conferences. Under the financial settlement of the Act of 1935, the Provinces receive 50 per cent of the proceeds of the income-tax, Bombay's share of the Provincial pool being 20 per cent. Under the "Government of India (Distribution of Revenues) Order, 1936," the Centre was to retain for the first period of five years, the whole of the Provincial share, or such part of that share as would, together with the contribution of Railways as determined by the separation convention of September 1924, bring the Central Government's share upto Rs. 13 crores. This rule by which the accrual of the Provincial share of the income-tax was made dependent upon the Railway contribution was greatly resented by the Provinces. It was, therefore, modified with effect from April 1939. The revised order provided that the sum to be retained by the Centre out of the Provincial pool shall be a fixed sum of Rs. 4½ crores during each of the years 1939-40, 1940-41 and 1941-42. The same rule applies to the next three years. Bombay's share of the income-tax was only Rs. 25 lakhs in 1937-38; it increased to Rs. 55.8 lakhs in 1939-40, and subsequently, during war years, it has gone up by leaps and bounds owing to the general increase in the income-tax revenue. The highest level was reached in 1944-45, in which year it was Rs. 531.20 lakhs. The revised estimate for 1945-46 is Rs. 454.00 lakhs, while the budget figure for 1946-47 is Rs. 392.80 lakhs. It will be seen that today the income-tax constitutes one of the most important sources of Provincial revenue.

§ 3. *Land Revenue*: This was a "divided head" before the Act of 1919; since the Reforms it has been wholly assigned to the Provinces.

Receipts under land revenue include the "portion of land revenue due to Irrigation," which latter is deducted and shown under "Irrigation." Till 1933-34, "land revenue" included an entry called "assessment of alienated lands less quit-rents." This entry, amounting to nearly a crore of rupees, did not represent actual collections, but the revenue which would have accrued to the Government if it had not "alienated" certain lands by way of personal and political gifts to Inamdars, Sardars, religious bodies and others. This, therefore, was merely a book entry, it being again shown on the expenditure side under "General Adminis-

tration." This arrangement unnecessarily inflated both sides of the public account, and as the Thomas Committee justly pointed out, vitiated inter-provincial comparisons in respect of the burden of the land tax. At the instance of the Accountant General, both these entries have been omitted with effect from 1933-34. The figures in Table No. 5 and No. 6 are adjusted accordingly.

During the Reform period, the land revenue system as a whole came in for a good deal of discussion. An inquiry into the system of assessment and revision was made by a committee in 1926, and the Government presented in 1928 the Land Revenue Code (Amendment) Bill in order to bring the processes of assessment and revision under statutory regulation. The Bill, however, failed, to pass owing to non-official opposition, particularly in respect of the "basis of assessment." In the Autonomy period, the Congress Ministry revived the measure and put upon the statute book the Land Revenue Code (Amendment) Act of 1939. In order to enable the reader to have a connected view of all these controversies and problems, a historical review of the Land Revenue system, a descriptive account of the system of settlement and revision, the attempted legislation of 1928, and the amending Act of 1939, have been presented in Appendix A.

§ 4. *Excise.*<sup>1</sup> Under the Acts of 1919 and 1935 excises in liquors and intoxicating drugs constitute a Provincial source of revenue. The receipts under this head include:

- (1) "Still-head" duty on the manufacture of country-spirit, and receipts from the sale of country-spirit, the rights for which are auctioned annually.
- (2) Tree tax and licence fees in respect of "toddy."
- (3) Excise duty and licence fees in respect of Indian made "foreign liquor."
- (4) Licence fees for the sale of imported "foreign liquor."
- (5) Receipts in respect of opium. The drug is purchased from the Government of India's Depot at Ghazipur and then sold to retail vendors at a price which includes the cost price, a duty, and some profit to the Provincial Government. The retail sale licences are also auctioned annually.

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<sup>1</sup> Cf. Appendix A for a connected account of Excise Policy and Administration.

- (6) Receipts from the duty and licence fees in respect of hemp and other drugs (*ganja, bhang, charas, etc.*).

In order to bring about uniformity of excise administration, the Bombay Government took up the excise revenue in certain Indian States on lease, and paid them compensations for the same. These latter are shown as a part of excise expenditure.

Excise policy and administration have also been the subject of fierce controversies. In the nineteenth and early twentieth centuries, the Government's excise policy was criticised on the ground that it placed the considerations of revenue above those of restriction of consumption. The prevailing sentiment in favour of Prohibition gathered force under the Reforms, and the Government adopted that policy through such measures as rationing, etc. As a result, the excise receipts dwindled considerably from 1924. Though this policy was relaxed in the depression period, the excise revenue did not recover its original level. In the Autonomy period, the Congress Ministry once again adopted a thorough-going programme of Prohibition, involving a loss of more than a crore and a quarter of rupees annually. Subsequently, the Prohibition rules were relaxed, and the revenue has shown a marked increase. The record figure of Rs. 789.17 lakhs was reached in 1945-46 (revised), the budget figure for 1946-47 being Rs. 682.67 lakhs.

§ 5. *Stamps*: Stamps are classified into two groups viz., non-judicial and judicial. The former group of stamps is governed by the Indian Stamp Act of 1899 and its several amendments; the latter by the Indian Court Fees Act, 1870, and its amendments. These two groups must be discussed separately.

(A) *Non-Judicial Stamps*. The Indian Taxation Inquiry Committee (1926) has well observed: "Stamp duties do not themselves constitute a separate tax, but are a method of collecting taxes of different kinds. Almost any tax can be collected through them and many taxes which have no sort of connexion with one another are so collected. The term "stamp duties" is, however, commonly used to denote, not all the taxes which are collected by means of stamps, but the duties on deeds and other instruments which are imposed under the stamp law."<sup>2</sup>

The original Indian Stamp Act of 1869 was based upon the English model, though the rates of duty were in several cases higher than those in the English Act. The Act of 1869 was ex-

<sup>2</sup> Report of the Indian Taxation Inquiry Committee, Vol. I, 1926, p. 220.



tended and elaborated in 1879, while a complete statute was passed in 1899. Under this latter Act, which was modelled on the British Stamp Act of 1891, stamp duties are leviable on several types of instruments, classified into three groups:

- (1) Instruments relating to transfers of property (viz. Administration bonds, deeds of adoption and other instruments connected with inheritance, deeds of gift and settlements, deeds of partition, sale certificates, conveyances, releases, bail bonds, transfers of bonds and mortgages, etc.).
- (2) Instruments relating to commercial transactions (viz. Agreements relating to deposit of title deeds, instruments of hypothecation of movable property, articles of association of companies, bills of exchange, promissory notes, cheques, bonds, deeds of partnership, receipts, etc.).
- (3) Instruments relating to other transactions (viz. Certified copies of certain documents, instruments relating to transactions on the Stock Exchange such as contract notes, conveyances or transfer of stocks or marketable securities, etc.).

Under the Government of India Act of 1919, "stamps" (judicial and non-judicial) was made a Provincial subject (reserved), subject to legislation by the Indian Legislature. The Provincial Legislature, however, was empowered to vary rates of duty subject to certain restrictions. This power was used in 1922 when an amending Act was carried through the Legislative Council, enhancing the stamp duties. The enhanced duties were, in the first instance, applicable for four years, but they were continued throughout the Reform period. In 1926 the Provincial Legislature passed an Act raising the stamp duty on instruments relating to transfers of property in the town and island of Bombay. In 1927 the Indian Finance Act removed the one-anna duty on cheques, which caused a loss of about 2½ lakhs of rupees for Bombay. In 1932 the Bombay Finance Act provided for the application of the enhanced stamp duty on transfers of property to the cities of Ahmedabad, Poona and Karachi. In the original Finance Bill of 1932, a proposal was made to levy a stamp duty on documents relating to forward transactions in the commodity markets and in the stock exchange, but owing to administrative difficulties the proposal was dropped.

Under the Government of India Act of 1935 stamp duties were included in the Federal, Provincial, as well as Concurrent Legislative Lists. The Federal List mentioned stamp duties in respect of bills of exchange, cheques, promissory notes, bills of lading, letters of credit, policies of insurance, proxies and receipts. The revenue, however, belonged to the Provincial Government. The Provincial List included "the rates of stamp duty in respect of documents other than those specified in List I." In the Concurrent Legislative List was mentioned "stamp duties other than duties or fees collected by means of judicial stamps, but not including rates of stamp duty."

(B) Judicial Stamps: Judicial Stamps are really "fees" charged for instituting judicial procedure in civil, criminal and revenue courts. The difference between a tax and a fee can be shown thus: a tax is a compulsory contribution levied for general services of government, characterised by an absence of *quid pro quo*; a fee, on the other hand, is a payment for a special measurable benefit offered by government. Judicial stamps are fees since they enable the payer to obtain the benefit of judicial procedure. Such levies, however, were condemned by jurists like Bentham and economists like Mill. The former laid down the maxim that "justice must not be sold"; the latter held that "court fees" were a tax on redress and therefore a premium on injury."<sup>3</sup> In this country, however, judicial fees have been defended on the ground that they are necessary to check the tendency to excessive litigation which is found in certain classes. This, for instance, was urged as a ground at the time of the original introduction of court fees in India by the Bengal Regulation XXXVIII of 1795. During the next seventy-five years fees were extended and elaborated by a series of Regulations and Acts. In 1870 was passed the Indian Court Fees Act, which, along with its amendments, governs the levy of judicial stamps in India.

With the introduction of the Reforms of 1919, "judicial stamps" became a Provincial subject. "subject to legislation by the Indian Legislature as regards amount of court-fees levied in relation to suits and proceedings in the High Courts under their original jurisdiction." The Reformed Legislative Councils in several Provinces passed amending Acts varying the rates of court-fees. In Bombay the Court-Fees Amendment Act, tenable for two

<sup>3</sup> See "A Note by the Legal Adviser to the Indian Taxation Inquiry Committee on Fees Levied Under the Indian Court Fees Act, 1870." (Report, Vol. II. p. 159.)

years, was passed in 1922, which enhanced the court fees in respect of suits above the value of Rs. 500. The Act expired in 1924 but it was revived in 1926, when another amending Act was passed raising the fees on suits of more than Rs. 5,000 in value. Under the Bombay Finance Act of 1932, court-fees were raised in respect of suits above the value of Rs. 1,000.

The revenue from "Judicial Stamps" includes, besides court-fees, the receipts from Probate Duties. Under the existing Court-Fees Act, a duty of 2 per cent is levied on Probates and Letters of Administration in respect of property of which the value exceeds Rs. 1,000, but does not exceed Rs. 10,000. The duty is  $2\frac{1}{2}$  per cent on property worth more than Rs. 10,000, but less than Rs. 50,000; it is 3 per cent on property exceeding Rs. 50,000 in value. A similarly graduated duty is levied on certificates of succession under the Indian Certificate Succession Act of 1889. The question of converting these duties into generally applicable Succession Duties or Inheritance Taxes has long been a vexed question. It was fully investigated by the Taxation Inquiry Committee (1926), which made concrete proposals regarding the institution of inheritance taxes under the peculiar circumstances of Indian succession. In the Bombay Legislative Council Sir Chunilal Mehta, Finance Member, introduced a Succession Duty Bill in 1927, which sought to impose such duties. The Bill, however, was thrown out by the Council.

The revenue from "Stamps" fluctuated between Rs. 150 lakhs and Rs. 175 lakhs during the period of the Reforms. During 1936-37 to 1945-46 stamp revenue increased from Rs. 146.99 lakhs to Rs. 257.00 lakhs. The budget estimate for 1946-47 is Rs. 249.28 lakhs.

§ 6. *Forests*: "Forests" has been a Provincial subject under the Acts of 1919 and 1935.

Till 1933 the forest area of the Presidency was 14,869 square miles. The area was reduced by about 650 square miles, as a consequence of the transfer of the Dangs to the Central Government in July 1933. With the separation of Sind, the forest area has been further reduced to about 13,000 square miles. For the purpose of administration, the area under forests is divided into three "circles," each of which is in charge of a "Conservator." The functions of the Department are described as under: "(a) The protection, conservation, and development of forests. (b) The exploitation and utilization of the forests so as to obtain the maxi-

imum yield consistent with their permanent maintenance and the supply of the people's needs in the matter of forest produce. This function includes the construction of roads for the opening up of inaccessible forest areas. (c) The conduct of research into silviculture and other problems affecting regeneration and development of forests."<sup>4</sup>

In the performance of these functions the Forest Department comes into close relations with certain Central Government Departments, such as the Survey of India, Railways, the Forest Research Institute at Dehra Dun and so on. Further, its activities have also to be co-ordinated with those of other Provincial departments such as the Revenue, Public Works, Agriculture, Excise and Police.

The revenue from forests is derived from the sale of forest produce which is classified into (a) major forest produce and (b) minor forest produce. The former includes timber, poles, sleepers, firewood, charcoal, sandalwood, and bamboos; the latter consists of myrobalans, lac, bark, leaves, grass and grazing, cinnamon, honey, rosha grass, fruits and pods, and mhowra seed. The forest revenue averaged Rs. 75 lakhs during the period 1921-22 to 1930-31; during the depression years, however, the revenue declined by about Rs. 20 lakhs. During 1936-37 to 1940-41 the revenue averaged Rs. 45 lakhs, but subsequently, owing to war demand, the prices of forest produce rose and the receipts increased enormously. In 1944-45 (accounts) the revenue was Rs. 313.81 lakhs, while the revised estimate for 1945-46 was Rs. 229.43 lakhs, and the budget estimate for 1946-47 is Rs. 151.07.

§ 7. *Registration*: Under this head are credited receipts from fees charged for registration and copying of documents under the Indian Registration Act of 1908. Under the Act of 1919, "Registration of deeds and documents" was made a Provincial Subject (transferred), "subject to legislation by the Indian Legislature." Under Section 80 A of that Act, however, the Provincial Legislature was empowered to amend the Registration Act "in its application to the Presidency so far as it does not affect the general trade and commerce or any other central subject."

Under the Indian Registration Act (1908) the registration of certain documents is optional, while that of others is compulsory. The former category includes (a) instruments (other than instruments of gift and wills) relating to rights in property of the value of less than one hundred rupees; (b) leases of immovable prop-

<sup>4</sup> *Reviews of Administration in the Bombay Presidency, 1933, "Forests," p. 1.*

erty for a period of less than one year; (c) instruments relating to rights in movable property; (d) wills. Registration is compulsory in respect of (a) instruments of gift of immovable property; (b) other non-testamentary instruments relating to immovable property worth more than one hundred rupees; (c) leases of immovable property from year to year, or for any term exceeding one year, or reserving a yearly rent; (d) non-testamentary instruments transferring or assigning any decree or order of a court relating to rights in immovable property of the value of one hundred rupees or more.

The rates of fees charged for registration must necessarily be arbitrary, since they cannot be related to the value of the service rendered. In fact, "the registration of documents greatly increases the security of contracts, property rights and trade, and the value of this security is out of all proportion greater than the cost of maintaining the system." The present scale of registration fees is graduated according to the value of the property or contract. The scales were raised in 1931 and in 1933. A charge is also made for copying the documents registered. The receipts under "Registration" varied between 12 and 16 lakhs of rupees during the Reform period.

Under the Act of 1935, the Concurrent Legislative List included "transfer of property other than agricultural land; registration of deeds and documents." The revenue from this source was nearly Rs. 15 lakhs up to 1941-42, but subsequently it has increased to Rs. 26.16 lakhs (1946-47 budget).

§ 8. *Tolls and Motor Vehicles Taxes:* The next important source of revenue consists of levies on traffic. These may be described under two heads: (i) Road tolls and (ii) Motor vehicles taxation. (i) The toll system was applied to Bombay in 1864 under the Government of India Act of 1851. Since that time tolls have been a source of Provincial and local revenue. The system, however, was from the very start unpopular, and in 1908, the Government of Bombay declared itself in favour of abolishing the tolls. This policy was pursued with vigour till 1914, by which year all tolls on Provincial roads were abolished. In 1922, however, some of these tolls were re-imposed for financing the maintenance of roads. These tolls yielded a sum of nearly 9½ lakhs of rupees till 1933.<sup>5</sup> In that year the toll system was extended upon the recommendation of the Reorganization Com-

<sup>5</sup> Shown under "XXX, Civil Works" till 1936-37.

mittee presided over by Mr. Thomas. From 1933-34 to 1935-36 the receipts from tolls amounted to an average of 16 lakhs of rupees. In the budget for 1936-37 a provision of 9½ lakhs of rupees was made for abolishing tolls.

(ii) The second source of revenue has been the receipts from motor vehicles taxation. The Indian Motor Vehicles Act conferred rule-making powers upon the Provincial Governments under which the latter imposed motor registration and licence fees. The receipts under this head were nearly Rs. 2 lakhs till 1930-31. In that year the fees were considerably raised, so as to produce an additional revenue of 10 to 11 lakhs of rupees annually. The motor vehicles were also subject to the Municipal wheel taxes, and the tolls on Provincial and local roads. It was, therefore, thought desirable to substitute a consolidated levy, as recommended by the Indian Road Development Committee (1928). In March 1935 Khan Bahadur Cooper proposed such a consolidated tax in his Motor Vehicles Tax Bill, but it had to be dropped owing to the opposition on the part of the representatives of Municipalities and local bodies. In September 1935, however, a somewhat less comprehensive measure was proposed and passed. This was the Bombay Motor Vehicles Act which imposed taxes on motor cycles and motor cars used for transport of goods and motor cars used for the transport of passengers. The Act lowered the registration and licence fees leviable under the Indian Motor Vehicles Act and at the same time abolished the tolls. The wheel tax, however, was allowed to be levied by the Municipalities and local bodies, which were also compensated for the loss of tolls. The Act also provided that if the proceeds of the tax exceeded 26.57 lakhs of rupees per year, the excess should be entered into a separate fund to be utilised for the construction, maintenance, and improvement of roads. The Act came into effect in April 1936. In 1939, the Indian Motor Vehicles Act was passed, by which motor registration has been made perpetual involving a loss of re-registration fees. Since 1936-37 the receipts under the Indian and Provincial Motor Vehicles Acts have been slightly over 40 lakhs of rupees annually.\*

§ 9. *Other Duties:* (i) *The Electricity Duty:* This duty was imposed during the period of financial stringency caused by the depression. The Electricity Duty Act of 1932 made provision for

\* Till 1930-31 the receipts from registration and licence fees were shown under "XIX, Police" and during 1931-36 under "XXVI, Miscellaneous Departments." Later, a separate account head, "XII, Receipts from Motor Vehicles Taxes," has been opened.

the levy of a surcharge on the consumption of electrical energy used for lights and fans to be collected from the suppliers. Exemptions were granted to government, railways, local authorities, hospitals, etc., and to consumers of less than 12 units a month. The receipts from this duty were nearly Rs. 9 lakhs a year for the period 1930-1936. (The receipts were shown under the account head "XXXV, Miscellaneous.")

By the Finance (Amendment) Act of 1939 the rates of electricity duty were raised, except in the case of cinemas and theatres. The exemption granted in the case of consumers of less than 12 units was withdrawn, and such consumers were subjected to a duty of one anna per unit. Consumers of more than 12 units were to pay an additional charge of one-half anna per unit. These higher rates were made applicable to Bombay in the first instance, where the Electric Supply Company was prevailed upon to lower its own rates correspondingly, so that the burden of higher rates might not fall on the consumers. The higher duties, however, might be extended to other urban areas by notification.

Since 1936-37 the receipts under this head have been shown under the account head "XIII, Other Taxes and Duties." The receipts were Rs. 10.06 lakhs in 1936-37.

(ii) Tobacco Duties: In 1857 the Tobacco Duty (Town of Bombay) Act was passed, by which tobacco imported into the town of Bombay was subjected to a "Municipal duty" of Rs. 7-8-0 per maund along with a fee of one rupee for the licence of retail sale. In 1932 an amendment to this Act was passed, which enhanced the Municipal duty to Rs. 30 per maund. The receipts from this measure were, however, to be turned over to the Bombay Corporation in order to enable it to bear the increased liabilities on account of the amalgamation of the Bombay Improvement Trust with it.

In 1933 was passed the Bombay (District) Tobacco Act, under which a licence fee for the sale of tobacco in the Province (other than the City of Bombay) was imposed.

Since 1936-37 the receipts from these duties have averaged Rs. 19 lakhs a year. Out of this, nearly Rs. 16 lakhs, representing the net receipts from the Town of Bombay Tobacco Duty, were paid to the Bombay Municipality in the first two years. Since 1938-39, however, this grant-in-aid to the Municipality has been reduced by Rs. 5 lakhs. The reason given by the Finance Mem-

ber was that the original grant was intended to enable the Bombay Municipality to meet the deficit in the Bombay Improvement Trust Budget; as the finances of that body had improved in the meanwhile, the grant for the purpose was justifiably reduced. In April 1943, the Central Government imposed an Excise Duty on tobacco, out of the proceeds of which the Provinces are given shares.

§ 10. *Minor Taxes:* The Government of India Act of 1919 permitted the Provincial governments to impose, without the previous sanction of the Governor-General, a number of minor taxes included in "Schedule I." This Scheduled Taxes List included the following:

- (i) A tax on land put to uses other than agricultural.
- (ii) A tax on succession or acquisition by survivorship in a joint family.
- (iii) A tax on betting or gambling permitted by law.
- (iv) A tax on advertisements.
- (v) A tax on amusements.
- (vi) A tax on any specified luxury.
- (vii) A Registration fee.
- (viii) A stamp duty, other than duties of which the amount is fixed by Indian legislation.

The following "scheduled taxes" were imposed in Bombay during the Reform period:

(i) *Entertainments Duties:* This was imposed in 1922 in order to meet the additional expenditure on education under the Bombay Primary Education Act, 1922. The yield of these duties between 1922-1936 was nearly 8 lakhs per year.

(ii) *Betting Tax:* In 1925 the Totalisator Tax was introduced; it was extended to bookmakers in 1931. This tax yielded a revenue of 10 to 11 lakhs of rupees till 1935-36.

During the Autonomy period these taxes have been continued, and their receipts have been shown under "XIII, Other Taxes and Duties."



§ 11. *Irrigation Revenue.*<sup>7</sup> Irrigation accounts are of two main categories: revenue account and capital account. Irrigation works are also divided into two types, viz. (i) works for which capital accounts are kept and (ii) works for which capital accounts are not kept. The former are again subdivided into (A) Irrigation and (B) Navigation, Embankment and Drainage Works. Each of these categories is, for the purpose of accounts, shown either as (i) productive works, or (ii) unproductive works. "If the net revenue from a capital work is expected to repay after ten years from its completion the annual interest charges on the capital invested, i.e., sum at charge at 4 (6) per cent or at such other rate as may be fixed by Government from time to time, the work is considered as "productive," otherwise it is treated as "unproductive." If any work for which a capital account is kept and which is classed as productive fails at any time after the expiry of ten years from its completion in three successive years to yield the relevant return, it is transferred to the "unproductive" class. Similarly, if a work, though classed as unproductive, succeeds in yielding for three years the relevant return prescribed for a productive work, it is transferred to the productive class."

Let us now see how the capital and revenue accounts of Irrigation works are made up. The capital account consists of (1) Capital Expenditure, including all initial expenditure and such further expenditure as is necessary for the full development of an irrigation project. This is shown under "68 (55) Construction of Irrigation, Navigation, Embankment and Drainage Works." If, however, capital expenditure is met from the Famine Fund, or from the ordinary Revenue, these deductions are made under these two heads from "58" (55), and they are shown under 19 A and 19 B (16 A and 16 B).

The Irrigation Revenue Account consists of two sources: (i) "XVII" (XIII), "Works for which capital accounts are kept." Under this revenue head are entered the gross receipts of irrigation works for which capital accounts are kept, minus the expenses and maintenance charges, so as to show the net revenue. (ii) Under "XVIII" (XIV) are shown the gross receipts of all irrigation works for which capital accounts are not kept. Against

<sup>7</sup> This is a summary of "A Note on the System of Capital and Non-Capital Accounts of Irrigation Works" which appears every year in the Budget Memorandum. Though the general system of irrigation accounts under the Reforms and under Provincial Autonomy is the same, there have been changes in the numerical order of account heads. In this note the account heads under the Reforms are shown in brackets.

the revenue entered here is to be set off the gross expenditure incurred on such works shown under "18" (15), "Other Revenue Expenditure." If, however, any such expenditure for protective irrigation works is met out of the Famine Fund, that amount is deducted from "18" ("15"), and shown under "18(1)" [15(1)].

Let us now examine the actual revenue under the two account heads on the revenue side. Taking the first, viz., "Irrigation, Navigation, Embankment and Drainage works for which capital accounts are kept," we have to note that under this head the net revenue is shown by deducting the working expenses from the gross revenue. The gross revenue is made up of (a) direct receipts, i.e. "sale proceeds of water supplied for irrigational and non-irrigational purposes, the sale-proceeds from canal plantations and other canal produce, and (b) the portion of land revenue due to irrigation. This latter forms a part of the gross land revenue, but it is deducted from the land revenue and shown under the head, "Irrigation."

During the Reform period the revenue from irrigation works for which capital accounts were kept varied from year to year, the average being about Rs. 40 lakhs.

During the Autonomy period the gross and net revenue under irrigation works declined owing to the separation of Sind, as a result of which "the portion of land revenue due to irrigation" fell by 80 to 90 lakhs of rupees per year.

§ 12. *Administrative Receipts:* It is needless to say that administrative departments such as justice, jails, police, education, medical, public health, agriculture, industries, etc., are primarily spending departments. These departments, however, get certain receipts which are credited to the revenue side of the public account. Under some systems of public accounting, administrative receipts form a part of the appropriation granted to the departments for its expenditure. In the British financial system, they are called "appropriations-in-aid." Under the Indian system of accounts, however, a spending department is not entitled to use its receipts for expenditure purposes; these receipts are surrendered, and go to the revenue side of the account.

The principal receipts of administrative departments are as follows:

- (i) Administration of Justice: Income from fees, magisterial fees, etc.

- (ii) **Education:** Income from fees in Government arts and professional colleges, secondary schools, etc.
- (iii) **Medical:** Medical school and college fees, hospital receipts, contributions, etc.
- (iv) **Public Health:** Income from the sale of sera, vaccines, etc.
- (v) **Police:** Miscellaneous fees and fines, receipts under the Arms Act, contributions for Railway Police, etc.
- (vi) **Jails and Convict Settlements:** Sale proceeds of jail manufactures and other miscellaneous items.
- (vii) **Agriculture:** Receipts on account of agricultural research and propaganda, receipts from fees, etc., from Agricultural College and schools, audit fees, etc. received by the Co-operative Department.
- (viii) **Industries:** Receipts from fees for inspection of weights and measures.
- (ix) **Miscellaneous Departments:** Income from miscellaneous fees. Till 1935-36, receipts from registration and house fees for motor vehicles were included under this head.
- (x) **Civil Works:** Receipts include rents for Government buildings, tolls on roads, etc.

## CHAPTER V

### THE SYSTEM OF PUBLIC EXPENDITURE

§ 1. *Introductory:* Normally the accounting of public expenditure is "subjective" and not "objective," i.e., the accounts relate to the activities of administrative departments, rather than to services and purposes. Thus, for instance, under "Education" we find the figures of expenditure relating to the Education Department, and not those of expenditure on education as a whole considered as a service provided by Government. We find, therefore, that certain expenditures which belong to education as a service are included among the disbursements of other departments, eg., the expenditure on the Agricultural College is shown under Agriculture, that of the Medical College under "Medical," etc. As a result of this system some regrouping of departmental expenditure becomes necessary when one has to analyse public expenditure with a view to exhibiting its distribution among the several objective services provided by Government.

In this chapter the public expenditure of Bombay is described on the departmental basis. The following are the principal expenditure heads in the Bombay Budget.

§ 2. *Direct Demands on Revenue:* This head includes the expenditure incurred in connexion with the collection of the several taxes and other revenue sources. The most important item is, of course, the charges in connexion with the collection of land revenue. It is to be remembered that it is obviously impossible to make a clear-cut separation of the expenses connected with the land revenue establishments, in the districts and lower administrative units, from those incurred on non-revenue establishments, since the duties of the Collector and lower revenue staff are not confined to land revenue collection. As a matter of fact, the whole administrative and magisterial system of the district hinges upon the Collector and the lower revenue staff. Regarding the scope of the functions of the Revenue Department, it has been justly said: "Anything affecting the general welfare of the people comes within its scope and it is consequently concerned in some way or other with all problems connected with the different branches of the administration. It supplies Government with a judgment on projects and schemes from the point of view of general administration as contrasted with the narrower views of specialised de-

partments. It administers all branches of Government for which a separate department is not necessary. It carries out work for other departments for which these departments do not have the necessary staff and for which it would be uneconomical to appoint a separate staff so long as that of the revenue department is available. More especially when people in bulk have to be dealt with or information for the collection of which no special machinery exists is required, it is done through this department."<sup>1</sup>

For accounting purposes, the total expenditure incurred on "Land Revenue and General Administration" is divided under two heads. Under "Land Revenue" are included the charges in connexion with the District Administration, Survey and Settlement, Land Records, etc. The expenditure incurred on the Headquarters Establishments (e.g., the salaries and allowances of the Governor, Councillors, and Ministers and Commissioners, the expenditure of the Secretariat Establishment, etc.) is shown under "General Administration." During 1921-36 there were several transfers of expenditure from "Land Revenue" to "General Administration" and *vice versa*; hence, the year to year figures under these two heads are not comparable. If, however, the two expenditure heads are added together, the total figure may afford a basis for comparison from year to year.

The expenditure head "Direct Demands on Revenue" includes, besides charges of land revenue collection, the expenditure incurred on the following departments: Excise, Stamps, Forest, and Registration. Charges incurred in connexion with the collection of the "Scheduled taxes" were also included under this head under the Reforms. Since 1936-37 charges in connexion with "Other duties and taxes" (the Entertainments Duties, the Betting taxes, Tobacco Duties, Electricity Duties, etc.), and those in connexion with the Motor Vehicles Acts are also included under this head.

§ 3. *Irrigation*: On the expenditure side the Irrigation Revenue Account includes interest on works for which capital accounts are kept, other revenue expenditure financed from ordinary revenues, revenue expenditure on protective irrigation works financed from the Famine Relief Fund, etc.

§ 4. *Debt Services*: At the commencement of the Reforms the Bombay Government was burdened with Rs. 9.8 crores of pre-Reform Irrigation Debt, as well as Rs. 3.16 crores of "ordinary" debt initially taken from the Government of India but re-lent to

<sup>1</sup> "Reviews of Administration," Vol. I, Land Revenue and General Administration, 1933, pp. 2, 3.

local bodies, agriculturists, etc. In 1920 Bombay borrowed about Rs. 9 crores for development schemes, a good part of which was re-lent to the three Corporations in Bombay, viz., the Bombay Municipality, Port Trust, and Improvement Trust. In the course of the next few years, Bombay increased its debt immensely on account of the large irrigation programmes in the Deccan and Sind, and development schemes in Bombay. Large sums were also borrowed from the Central Government in order to be re-lent to the three corporations in Bombay.

At the commencement of Provincial Autonomy Bombay's debt position was as follows:

- (1) The Bombay Development Loan matured on 1st November, 1935, when the liabilities of the Government and the three Presidency Corporations were as follows:

	Rs. (Lakhs)
Government	2,96.40
Bombay Port Trust	1,447.53
Bombay Municipality (Municipal Account)	1,25.00
Bombay Municipality (Improvement Account)	3,70.00

By realising the securities in the Government and Municipal Sinking Fund, repayment of Rs. 2,63,63 lakhs was made. The remaining was converted into a loan borrowed from the Provincial Loan Fund. Out of this Rs. 1,47.53 lakhs was re-lent to the Port Trust, and Rs. 82.67 lakhs and 3,70.00 lakhs to the Bombay Municipality in the Municipal account and the Improvement account respectively. This process of repayment and conversion of the Development Loan meant a saving of Rs. 22 lakhs a year in debt charges.

- (2) Bombay owed Rs. 6,15.64 lakhs on account of the Pre-Reform Irrigation Debt.

(3) In the Reform period Bombay had borrowed large sums for irrigation and other purposes, which stood at about Rs. 9,60 lakhs on the 1st of April, 1937. The interest charges on account of these loans came to Rs. 80.88 lakhs.

- (4) Bombay Government had further borrowed nearly Rs. 15 crores from the Central Government and had re-lent the sum to

**Bombay Port Trust, Bombay Municipality and the Improvement Trust.**

Upon the recommendation of Sir Otto Niemeyer, a scheme of debt consolidation was adopted at the commencement of Provincial Autonomy. The scheme included the following elements of debt:

(i) The Pre-Reform Irrigation Debt: Rs. 6,15.64 lakhs. This amount was reduced by Rs. 3,99.37 lakhs, the balance available to the credit of Bombay after the decentralisation of balances. The remaining sum of Rs. 2,16.27 lakhs was included in the debt consolidation scheme.

(ii) Post-Reform Debt of Rs. 16,27.94 lakhs, including the converted Bombay Development loan.

(iii) Three long-dated loans advanced to the Improvement Trust, totalling Rs. 4,12.34 lakhs.

The total consolidated debt amounted to Rs. 22,56.55 lakhs bearing a uniform flat rate of 4.56 per cent. It is repayable to the Government of India in the form of bi-annual equated payments of principal and interest over 45 years.

§ 5. *General Administration*: Under this head are included those charges which relate to the Headquarters, e.g. the salaries and allowances of the Governor, Councillors (under the Reforms), Ministers and Commissioners; the expenditure in connexion with the Secretariat Establishments, and some charges relating to general establishments in the districts. As already observed, there have been several transfers of expenditure items between this head and Land Revenue, so that for purposes of comparison it is convenient to combine the figures under these two heads. Another important point to be noted in connexion with the figures under this head is that upto 1933-34, it included the entry "assessment of alienated lands less quit rent," corresponding to the same entry on the revenue side under "Land Revenue." As these were merely book entries, they were omitted with effect from 1933-34.

§ 6. *Administration of Justice*: The apex of the judicial administration of the Presidency is the High Court, which has original jurisdiction in Bombay City and appellate jurisdiction over the whole Province. In the districts and lower units, there are the courts of the District and Sessions Judges, Subordinate Judges, etc. There are also Small Causes Courts in important

towns like Bombay, Poona and Ahmedabad. When Sind was a part of the Bombay Presidency, there was also the Court of the Judicial Commissioner for Sind.

The expenditure of the Department was in the neighbourhood of Rs. 70 lakhs during the period of the Reforms. From 1936-37 to 1941-42 it ranged round about 85 lakhs; but subsequently it has shown an increase. In the 1946-47 budget the expenditure is estimated at Rs. 88.65 lakhs.

§ 7. *Jails and Convict Settlements*: The prisons in the Presidency are classified into several types such as Central Prisons, District Prisons, special prisons, lock-ups, temporary prisons, Borstal Schools, etc. In 1921-22 the expenditure on this department amounted to Rs. 31.3 lakhs. Since then, several economies were effected in the administration of the department after careful inquiries by special officers, as a result of which the expenditure was brought down to about Rs. 22 lakhs by 1935-36. During the same period, the cost per prisoner was also reduced from Rs. 175 to Rs. 125. Since 1935-36, the expenditure of the department averaged Rs. 16.5 lakhs till 1939-40. During the war period the expenditure has tended to increase, the budget figure for 1946-47 being Rs. 39.58 lakhs.

§ 8. *Police*: "The police force in the Bombay Presidency consists of two distinct bodies, the stipendiary and the village police. The stipendiary force is divided into several branches, namely, the Bombay City Police, District Police, Railway Police, and Criminal Investigation Department."

While the primary function of the police department is the prevention and detection of crime and the maintenance of peace and order, it performs several other duties imposed upon it by law, and entrusted to it for administrative reasons, e.g., control of traffic, censorship of plays and other performances, aid to refugees and pilgrims, passport and naturalization inquiries, etc.

The expenditure on the Police Department at the commencement of the Reforms increased by nearly 60 lakhs owing to the higher scales of pay sanctioned for all cadres. In 1921-22 the expenditure amounted to Rs. 1,90.6 lakhs; by 1929-30 it was brought down to Rs. 1,76 lakhs by means of retrenchment effected on the recommendations of the Retrenchment Committee (1922) and of several Retrenchment Officers appointed from time to time.

<sup>1</sup> "Reviews of Administration," No. VIII, Police, 1933, p. 1.



In 1930-31, however, the departmental expenditure increased by about Rs. 14 lakhs on account of the Civil Disobedience Movement. In 1932 the Reorganization Committee made several suggestions for retrenchment, but the Government rejected most of them.

During 1935-1940, the expenditure on the Police Department ranged between Rs. 1,40 and Rs. 1,50 lakhs a year. In subsequent years the expenditure has increased by more than a crore of rupees. The Budget for 1946-47 estimates the expenditure on this department at Rs. 3,26.53 lakhs.

§ 9. *Ports and Pilots*: Under the Devolution Rules "major ports" were made a Central subject, and "minor ports" a Provincial one. Certain charges in connexion with the administration of the minor ports, have since 1921-22 been a part of Provincial expenditure.

§ 10. *Scientific Departments*: Expenditure under this head includes the upkeep of Provincial Museums and donations to scientific societies.

§ 11. *Education*: The principal items of expenditure under "Education" are as follows:

(i) *Primary Education*: The policy of entrusting the management of primary education to local bodies was adopted in 1889 when such bodies were set up at the instance of Lord Ripon. The finance for primary education was met partly out of the local fund cess (one anna on every rupee of land revenue) and partly out of grants from the Provincial Government. Originally the latter was a fixed sum of about Rs. 2½ lakhs, but later the Government agreed to contribute one-half of the total expenditure on primary education incurred by local bodies. "By 1921 the grants from Government to district local boards had increased to nearly Rs. 59 lakhs, or 87 per cent of the total expenditure of the Boards on primary education."<sup>3</sup>

With the inauguration of the Reforms, "Education" was made a Provincial transferred subject, in charge of a responsible minister. The first Education Minister, Dr. (now Sir) R. P. Paranjpye appointed the Compulsory Education Committee (1921-22) to examine the question of compulsory primary education in the Presidency and to make recommendations regarding its introduction. The Committee chalked out a programme for the

<sup>3</sup> Bombay Government's Memorandum to the Indian Statutory Commission, p. 22.

adoption of compulsory primary education in Municipal and non-Municipal areas within a period of five and seven years respectively. In 1923 was passed the Primary Education Act, which vested the control of primary education in the elective "School Boards" of local authorities, the Government retaining the duties of inspection and supervision. Under the Act of 1923 local authorities were to prepare schemes for the introduction of compulsory primary education and to submit them to the Government for scrutiny. In the case of a scheme accepted by Government, the latter provided half the recurring and non-recurring extra cost in the case of Municipalities, and two-thirds in the case of the district local boards, in addition to the amount of the "datum line" grant, i.e. the grant paid by Government in the year before the transfer.

Under Provincial Autonomy, Primary Education again received a fresh fillip. The Congress Ministry reviewed the whole position in regard to the control of primary education and passed the Primary Education (Amendment) Act (1938) which transferred the control of primary education from the local bodies to the Government. The expenditure on primary education, which was Rs. 1,01.76 lakhs in 1936-37 increased to Rs. 1,30.80 lakhs by 1939-40. During the war period the expenditure has increased by about Rs. 30 lakhs.

(ii) *Secondary Education*: In regard to this the Government's policy has been to maintain "model high schools" in the districts, and to give grants-in-aid to schools conducted by private bodies. The Reorganization Committee considered that the need for maintaining "model schools" no longer existed, and that, therefore, the Government should adopt the policy of gradually transferring Government secondary schools to private bodies having adequate financial resources. The Government have accepted the general principal underlying this recommendation. Under secondary education are also included the grants for Anglo-Indian and European education.

(iii) *University Education*: The Government gives a grant to the Bombay University, maintains arts, science and professional colleges and vocational institutions, and gives grants to private bodies conducting colleges.

§ 12. *Medical*: This subject was made "Provincial" (transferred) under the Reforms and it continues to be a Provincial subject under the Act of 1935.

"The medical organization of the presidency as distinct from its public health organization, is essentially a hospital organization designed to render medical relief to the general population, with ancillary specialist sections providing for medical relief, medical teaching, laboratory assistance, and research. The medical organisation, which is the framework of the scheme, is based on the district as the primary unit. There is at every district headquarters a hospital styled 'the civil hospital,' which is owned, staffed, financed, and controlled by Government. The Civil Hospital is the centre of the official system of medical relief and is a superior hospital for the whole district. Subsidiary to it are Government-aided dispensaries which are scattered throughout the districts."<sup>4</sup>

Besides hospitals and dispensaries in the districts and lower units, the Government has taken upon itself under the City of Bombay Municipal Act the duty of controlling and maintaining a number of hospitals in Bombay City, such as the J. J. Hospital, St. George's Hospital, the G. T. Hospital, the Cama and Alibless Hospitals, etc. Further, the Government maintains special institutions such as mental hospitals, leper asylums, the Haffkine Institute, the Chemical Analyses Department, etc. The expenditure connected with the medical college and medical schools is included under "Medical."

§ 13. *Public Health:* Certain functions in respect of urban and rural sanitation are "obligatory duties" of Municipalities and Local Boards, but there are other general or environmental functions in regard to public health which are performed by the Provincial Government. Among the functions of the Public Health Department are vaccination, advice and inspection in regard to urban and rural sanitation, sanitary and medical arrangements at fairs and pilgrimages, control of epidemic diseases, sanitary aspects of famine relief, distribution of quinine, provision of courses of instruction for sanitary inspectors and health officers, collection of vital statistics, etc.

§ 14. *Agriculture:* "The Agricultural Department has been in existence for nearly half a century and was formed as a result of the recommendations made by the Famine Commission which sat after the great famine of 1877. In the early years its primary functions were statistical but gradually its purposes have been widened and it is now intended to be an organization to ascertain

<sup>4</sup>"Reviews of Administration," Vol. XX, Medical and Public Health Departments, 1933, p. 2.

by experiment, investigation and research, the methods by which agricultural produce can economically be increased in quantity and improved in quality, and then to get these methods put into practice."<sup>5</sup>

The principal functions of the Agricultural Department include: (a) Research and investigation: Research is largely subsidised by outside agencies such as the Imperial Council of Agricultural Research, the Indian Central Cotton Committee, Sir David Sassoon Trust, etc. The Department maintains experimental farms for various types of farming research, such as plant-breeding, dry-farming, cattle-breeding, soil fertility, etc. (b) Agricultural propaganda through shows and demonstrations has been an important part of the work of the department. (c) The Department's activities also include work in connexion with "specialist" sections such as live-stock improvement, agricultural engineering and horticulture. (d) The Department also conducts studies in Agricultural Economics, particularly marketing and financing of crops. It maintains, as far as conditions permit, certain types of statistics relating to crops and their acreage and other aspects of the agricultural economy. (e) Lastly, the Department is in charge of Agricultural Education, which is imparted through the Poona College of Agriculture and agricultural schools.

§ 15. *Veterinary*: The functions of the veterinary department are: "(a) Precaution and cure of diseases of animals with special reference to epidemics. (b) Control of the importation of live-stock at ports, so as to prevent the importation of diseases. (c) Educational work at the Veterinary College, Bombay. (d) Veterinary dispensaries. (e) Inspection of animals for slaughter and meat after slaughter, where Municipalities so desire, and (f) Control of horse-breeding operations."<sup>6</sup>

§ 16. *Co-operation*: The co-operative movement in India was officially started in 1904, when the Indian Co-operative Societies' Act was passed. This Act was extended by that of 1912, which permitted the formation of non-credit co-operative societies. In 1919 co-operation was made a Provincial subject, and it remains so to this day.

In Bombay the post of Registrar of Co-operative Societies was created in 1904, the officer being made subordinate to the Director of Agriculture.

<sup>5</sup> "Reviews of Administration," Vol. XVI, Agriculture, p. 1.

<sup>6</sup> "Reviews of Administration," Vol. XVI, Agriculture, Veterinary and Co-operative Departments, p. 23.

Since the Reforms, a separate Co-operative Department has been instituted and placed under the Registrar. Under the Bombay Co-operative Societies Act (1925) the statutory functions of the Registrar are "to classify and register societies, to audit their accounts once a year, to hold inquiries into their working and financial condition, wind up societies, cancel registrations, appoint liquidators, and arbitrate in disputes."

It is to be noted that there are three separate agencies for supervising and controlling the activities of co-operative societies. In matters of finance, supervision and control are exercised by Central Banks, Supervising Unions and the Provincial Co-operative Bank. Propaganda and Education are handled by the Provincial Co-operative Institute, which is aided by the Government. Lastly, registration, audit, cancellation, liquidation, etc. come within the sphere of the Registrar of Co-operative Societies.

§ 17. *Industries*: In 1915 the Bombay Government appointed a Standing Committee of Advisers to advise them on industrial matters in general, and on the practicability of starting indigenous industries in particular. In 1917 the Government dissolved the committee and created the Department of Industries with a whole-time Director recruited from the Indian Civil Service. This system was continued till 1924, when, upon a vote of the Legislative Council reducing the grant for the department, many of its functions were distributed among other departments. In 1926 the Government appointed a Committee to report on the reorganization of the Department, and to advise on the formulation of its activities. The Industries Committee suggested the following functions: (1) The supply of industrial and commercial intelligence to private enterprise. (2) Technical advice and assistance to cottage industries and small organized industries. (3) Industrial Education and Demonstration. (4) Industrial Surveys. (5) Industrial Exhibitions. (6) Co-ordination of the work of the Industries Department with that of other departments in rural areas.

The Department was duly reorganized and the functions mentioned above were assigned to the Director. Besides these, the department has also been charged with other duties such as (a) work in connexion with mines and minerals; (b) advice in regard to financial assistance to industries by Government; (c) investigations in respect of new industries; (d) industrial research; (e) work in connexion with the Weights and Measures Act, 1932; (f) work in connexion with fisheries.

<sup>1</sup> *Ibid.*, p. 42.

In 1932 the Reorganization Committee recommended the abolition of this department on the ground that though the Province requires a strong and active industries department, it cannot afford one today, and that to keep in existence a department with so limited resources that it cannot do any considerable amount of work merely in the hope of better times, is to fritter away funds uselessly.<sup>8</sup> The Government, however, rejected this recommendation, and the department has been retained.

The average annual expenditure of the Department during 1921-32 was barely a lakh of rupees. During 1932-36 it ranged round the figure of 3.5 lakhs. Several new items of expenditure on industrial development were sanctioned by the Congress Ministry during 1937-39, as a result of which the total expenditure for the department increased from Rs. 6.82 lakhs (1937-38) to Rs. 13.14 lakhs in the Budget for 1939-40. But in that year the actual expenditure fell short of the budget grant, the accounts showing a figure of Rs. 7.65 lakhs. During the war period the expenditure has been nearly trebled, the budget figure for 1946-47 being Rs. 32.92 lakhs.

§ 18. *Miscellaneous Departments:* Under this head are included a number of miscellaneous charges, e.g., those in connexion with the inspection of factories, steam boilers, labour, statistics, examinations, preservation and translation of ancient manuscripts, the administration of the Indian Partnership Act, etc.

§ 19. *Civil Works:* In the Bombay Presidency the Public Works Department is in charge of Irrigation as well as Roads and Buildings. At one time a complete separation of these two branches was contemplated, but it was found to be expensive and unworkable. Their joint management has continued to this day, though certain allocations of expenditure between the two branches have been made at the instance of the Auditor-General.

The expenditure on Roads and Buildings is mainly included under "Civil Works" (expenditure head 41 under the Reforms and 50 under Provincial Autonomy). The common establishment charges are divided between the two branches in certain proportions laid down from time to time by the Accountant-General.

§ 20. *Famine Relief:*<sup>9</sup> A regular annual famine relief assignment was first provided in the year 1878-79, when a sum of Rs. 1,50 lakhs was set aside from ordinary revenue for the relief

<sup>8</sup> Report of the Reorganization Committee, 1932, pp. 163-170.

<sup>9</sup> The contents of this note are summarised from the Bombay Government's Memorandum to the Indian Statutory Commission (pp. 604-607).

of famine and for the construction of protective irrigation works. Till the year 1907-8 Famine Relief was a Provincial charge; in that year it was made a Central liability, the Central Government providing a sum of Rs. 37½ lakhs for distribution among Provinces for famine relief purposes. In 1917-18 a new arrangement was made under which the liability for famine relief was divided between the Central and Provincial Governments in the proportion of three to one.

Under the Reformed Constitution, Famine Relief was made a Provincial subject along with land revenue and irrigation. Devolution Rule 29 and the Schedule IV provided for the constitution of a "Famine Relief Fund" in each Province. The Provincial Governments were required to make annual assignments out of ordinary revenues for the purpose of famine relief and protective irrigation. Bombay was required to make an annual provision of Rs. 63.60 lakhs, this figure being based upon the average actual expenditure incurred by the Province on famine relief and protective irrigation during the past twenty-five years. The unspent balance of this assignment was to be credited to the Famine Insurance Fund which could be drawn upon for the purposes of famine relief, protective irrigation, and for granting loans to cultivators under the Agriculturists' Loans Act of 1884.

The annual assignment of 63 lakhs of rupees was soon found to be too high, and as a consequence, the balance in the Famine Relief Fund began to accumulate rapidly. Upon a representation made by the Bombay Government in 1926 the Government of India reduced the annual assignment to Rs. 33.6 lakhs, subject to reconsideration if the balance in the Famine Insurance Fund fell below Rs. 150 lakhs. In 1927-28 the whole position was reconsidered in consultation with the Provincial Governments, and it was decided that the famine relief assignment should be solely devoted to famine purposes, and for other objects separate provisions should be made in the budget. Under the new arrangement Bombay's annual assignment was fixed at Rs. 12 lakhs to be devoted solely to famine relief, the unspent balance being credited to the Famine Fund. The assignment could be suspended when the Famine Fund amounted to Rs. 75 lakhs. Any excess in the Fund could be used for protective irrigation, and for making advances to cultivators.

Upon the inauguration of Provincial Autonomy, the balance of the Famine Insurance Fund was handed over to the Province under the scheme of "decentralization of balances." In 1938 the

Bombay Famine Relief Fund Act was passed which provided that "the accounts of the Fund shall be made up at the end of every financial year, the securities belonging to the Fund being valued at their market value on the last day of such year." It is further provided that if the accounts so made show that the Fund falls short of Rs. 63 lakhs, then the deficiency is to be made up from the revenues of the Province.

In the Budget the amount to be spent out of the Famine Relief Fund is shown on the revenue side under "Transfers from Famine Relief Fund." On the expenditure side are shown (a) the expenditure on famine relief, and (b) the transfers from ordinary revenues to the Famine Relief Fund. The operations of the Famine Relief Fund are shown under the capital head "Famine Relief Fund."

§ 21. *Pensions*: The expenditure on pensions was about Rs. 55 lakhs a year at the beginning of the Reforms, but it increased to about Rs. 110 lakhs by the end of that period. This increase was due to (a) the transfer of pensions paid on account of officers employed in the Presidency to Provincial revenues and (b) increased charges resulting from the revision of salaries sanctioned at the commencement of the Reforms.

In 1936-37 Superannuation Allowances and Pensions amounted to Rs. 1,07.52 lakhs; in the budget for 1946-47 the provision under this head is Rs. 1,47.07 lakhs.

§ 22. *Stationery and Printing*: This head includes the expenditure in connexion with the Government Presses and the purchase of stationery stores for Government Departments.



**PART II**  
**FINANCIAL DEVELOPMENTS**

**CHAPTER VI**

**BUDGETING AND FINANCIAL PROBLEMS (1921-36)**

§ 1. *The Economic Background:* The period under review contains three fairly distinct phases of economic development. The first two years constitute a period of economic recession following the post-war inflation. The next six or seven years represent a period of economic re-adjustment and expansion in the field of production, trade, and money. During these years (1923-29), world production, the quantum of international trade and employment increased in an amazing degree, in spite of the legacy of obstructions and impediments left by World War I. During the same period a number of countries restored their monetary systems on the gold basis. The third phase begins from the middle of the year 1929 and extends upto 1933 or 1934—the years of the Great Depression. This period is characterized by a rapid fall of prices, production and employment in most countries, accompanied by “deficit budgets,” mainly as a result of decline in the important revenue heads such as the income taxes, customs and excises.

In India the cyclical fluctuations of economic activity correspond fairly generally to those in other countries. Here the post-war boom reached its peak in 1920, when the Calcutta Index Number (July 1914=100) stood at 202. In the same year the Government of India fixed the Rupee-Sterling exchange at the high level of 2s. (gold) upon the recommendation of the Babington-Smith Committee. At this time there arose an enormous demand for sterling, both out of genuine trade and speculation, and this forced the Government to sell “Reverse Councils” in large amounts. This process involved a serious contraction of internal monetary circulation, leading to a fall of prices. This brought in a depression in trade during the first two or three years of the Reform Period, which created financial difficulties at the Centre and in several Provinces. The price-level registered a continuous decline right upto the year 1930, mainly as a result of the deflationary policy adopted by the Government of India. In this respect the economic environment in India during the period 1923-30 was

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\* See Tables Nos. 33 and 34.

similar to that in England, where also monetary policy had a deflationary effect.

The depression period in India extends, broadly speaking, from 1930 to 1935. The sudden fall of the price-level was marked during the year 1930, when the Calcutta index number declined by about 30 points. It continued to fall till it reached the lowest level (87) in 1933, and then began to rise slowly. By 1935 the index number was four points higher than in 1933. The fall of prices was greater in the case of primary products entering into the export trade, than in the case of manufactured commodities constituting the imports, and this disparity adversely affected the terms of trade. The balance of trade in merchandise fell sharply in 1932, but at about this time there started an enormous outflow of gold which greatly eased the pressure on the exchange.

The fluctuations of prices and economic activity affected the budgetary and financial adjustments in the Province to a fairly large extent. The following study attempts to bring out this effort.

§ 2. *Bombay Budgets (1921-22 to 1935-36)*. The Province of Bombay started on its financial career under the Reformed Constitution with a comfortable opening balance of a little over 3 crores of rupees. Unfortunately, the general economic conditions had not recovered from the setback of 1920-21 when the budget for 1921-22 was presented by the Finance Member, Sir George Curtis. This very first budget revealed a deficit of a little less than Rs. 2 crores, a fact which was justly regarded with apprehension by Sir George. In the course of his budget speech he dwelt at some length on the necessity for drastic retrenchment in the interest of financial equilibrium. Later in the year, the Legislative Council passed Rao Bahadur R. R. Kale's resolution in favour of appointing a Retrenchment Committee. Such a committee was appointed in July 1921.

For the next five years the portfolio of finance was under the charge of Sir Henry Lawrence. His regime represents a phase of expansionist finance particularly in respect of capital expenditure. His first budget (1922-23) showed a deficit of Rs. 118 lakhs, which could not, obviously, be met by such minor additional taxation as he proposed. The Council rejected his proposals for raising the rates of stamp duty payable under the Indian Stamp Act and the Indian Court Fees Act, and insisted upon drastic retrenchment of expenditure, the avenues of which were, in the opinion of the Council, not fully explored. The taxation measures,

however, were later passed, upon an assurance given by the Finance Member that the expenditure estimates would be cut down by Rs. 60 lakhs. In the same session the Council passed Dr. Paranjpye's Education Act and consented to impose the Entertainments Duty to finance it.

For the next two years the financial operations showed good surpluses, mainly due to retrenchment effected in several departments. By 1925-26, however, most of the avenues of economy had been exhausted, and the Finance Member was compelled to seek the Council's support for additional taxation. In the course of his budget speech for 1925-26, Sir Henry Lawrence analysed the causes of Bombay's financial difficulties, and maintained that they were chiefly due to the inexpansive character of the principal revenue heads. He then tried to make out a case for additional taxation by pointing out that retrenchment had already reached the limits upto which it could be pushed without impairing the efficiency and serviceability of Government departments. In spite of all this, the Council rejected the Finance Member's proposals for enhancing the rates of stamp duty in Bombay, and for renewing the increased rates payable under the Indian Court Fees Act.

The year 1926-27 revealed the first serious deficit of no less than Rs. 166 lakhs. In the year the Indian Stamp (Bombay Amendment) Act was renewed, while another amending Act raising the stamp duty on documents relating to transfer of property in the city and island of Bombay was passed. The Budget for 1927-28 also showed a deficit of Rs. 50 lakhs. The Budget for 1928-29 would also have been a deficit one, but for the remission of Bombay's contribution to the Central Government. The Budget for 1929-30 was just balanced.

Then came the Great Depression. Its effect, however, was not noticeable at the time of presenting the budget for 1930-31, which was a balanced one. But in the course of the year the budget calculations, particularly in respect of revenue, were completely upset as a result of the depression. The actuals of the year showed a deficit of no less than Rs. 179 lakhs, chiefly due to the fall under the following revenue heads: Land Revenue (Rs. 38 lakhs); Excise (Rs. 85 lakhs); Forest (Rs. 26 lakhs); Stamps (Rs. 15 lakhs); and Irrigation (Rs. 35 lakhs).

The outlook for the year 1931-32 was far from bright. The economic depression was deepening and its disastrous consequences were being accentuated by the Civil Disobedience Movement. The

budget estimates for the year were: Revenue, Rs. 1,524 lakhs and Expenditure, Rs. 1,589 lakhs. The revenue was inclusive of Rs. 39 lakhs representing Bombay's share of the petrol tax and Rs. 33 lakhs on account of additional taxation for which the sanction of the legislature was sought. On the expenditure side, the Finance Member announced a cut of Rs. 39 lakhs, which was principally borne by Civil Works (12) and by Education (9), in the form of a 5 per cent reduction in the grants to local bodies for primary education. Of the new taxes, two were renewals of the old ones, viz., the Stamp and Court-Fee Acts. The Government made a proposal for imposing Succession Duties, but the bill was thrown out by the Council. In the course of the budget debate, the Finance Member promised to appoint a Retrenchment Committee in accordance with the wishes of the Council. The Committee was duly appointed with Sir Rustom Vakil as chairman.

The Budget and the Finance Act of 1932-33 are highly representative of depression finance. The current year, 1931-32, witnessed a continuous fall of prices and consequent worsening of the general economic situation. As a result, the revised estimates of the year showed an increment of about Rs. 73 lakhs in the deficit which was estimated for that year. The land revenue remissions and suspensions amounted to Rs. 19 lakhs, while reductions and suspensions in water rates caused a decline of about Rs. 35 lakhs under Irrigation. Stamps fell by Rs. 10 lakhs due to the economic depression while forest revenue declined by Rs. 12 lakhs for the same reason. The budget estimates for 1932-33 were: Revenue, Rs 14, 35 lakhs and Expenditure, Rs. 15,08 lakhs. The Finance Member pointed out that the expenditure estimate was arrived at after effecting large reductions upon the recommendations of the Retrenchment Committee. It was obvious from the figures supplied by him that a large part of the retrenchment was borne by Education and Civil Works, and that these cuts were not of such a character as to be maintained permanently. Establishment costs were reduced by levying a cut of 10 per cent in the pay of Government servants, and by retrenching posts wherever possible. In spite of all this retrenchment, however, the Government found it necessary to impose additional taxation. All the taxation proposals were, this year, included in a single Finance Bill—an improved procedure copied from the Central Assembly and the British Parliament. The Finance Bill contained the following proposals of additional taxation: a surcharge on electricity; enhancement of court fees; enhancement of duties under the Transfer of Property Act and a Stamp Duty on forward transac-

tions. Out of these, the first three were passed and the last was thrown out.<sup>1</sup>

In the course of the year 1932-33 a detailed inquiry into the entire administrative organization was conducted by the Reorganization Committee presided over by Mr. G. A. Thomas. The recommendations of the Committee and the subsequent economies effected are described at a later stage.

The budget for 1933-34 was presented by Sir Ghulam Hussain Hidayatulla. At the outset, he found it necessary to answer the charge made by the Reorganization Committee to the following effect: "The mere fact that an opening revenue balance of Rs. 3,08 lakhs on 1st April 1921 was converted into a deficit of Rs. 88 lakhs on 31st March 1931 creates a serious misgiving whether this (Finance) Department has fulfilled the main purpose of its existence. We have no wish to criticise the financial policy of the Government since the advent of the Reforms. We find it, however, very difficult to arrive at any other conclusion than that the source of much of the adversity that has overtaken this presidency can be traced to a lack of financial foresight."<sup>2</sup>

This was a serious charge and it could not be left unanswered. The Finance Member pointed out that the principal cause of financial difficulty was the decline in revenue under the four principal heads: Land Revenue, Excise, Stamps and Forests. He observed: "If the Honourable Members will compare the average of all our receipts from 1921-22 to 1929-30 under the four main heads I have just mentioned, with the figures of 1930-31, 1931-32 and 1932-33, they will see that our receipts decreased to a total extent of over four crores in these three years. . . . In the twelve years 1921-22 to 1932-33 and excluding capital expenditure, development schemes have cost our revenues the very large amount of eight crores and a half. . . . We may set against these the items of which our financial critics always remind us, namely, the three crores of opening balance, and the cessation of the Provincial contribution to the Central Government and the reduction in the Famine Fund assignment, from which two items our Provincial revenues have benefited to the extent of seven crores and a quarter. . . . It is thus clear that we have not frittered away all these savings but we had to make up the deficiency in our revenues. Now, Sir, the expenditure on the development schemes was voted, not merely upon the assurances of Government members but with very opti-

<sup>1</sup> For details see page 89.

<sup>2</sup> Report of the Reorganization Committee, 1932, p. 26.

mistic support from various other leaders of public opinion at the time. It was this House that demanded the restriction of our excise revenue. And it must not now blame those who constitute the present Government for not having in its coffers those savings which would now be such an invaluable asset."<sup>3</sup>

Turning to the estimates, the Finance Member pointed out that the revised figures for 1932-33 were better than the budgeted ones by about Rs. 32 lakhs, thus reducing the estimated deficit of Rs. 59 lakhs to Rs. 27 lakhs. The budget estimates for 1933-34 were: Revenue Rs. 12,91.4 lakhs; Expenditure, Rs. 13,40.9 lakhs. The deficit of about Rs. 50 lakhs was in spite of the retrenchment of Rs. 28 which had been effected in the expenditure estimates. Ultimately the deficit was reduced to Rs. 28 lakhs as a result of the taxation proposals sanctioned.

The Finance Act of 1932 was renewed; in addition a duty on the sale of tobacco in the Presidency, (other than in the city of Bombay) was imposed, of which the estimated yield was Rs. 4 lakhs. Again, following the recommendation of the Reorganization Committee, Toll-bars were imposed at certain places. They were expected to yield about Rs. 7 lakhs.

The actual working of the year 1933-34 showed a certain amount of financial improvement. This was reported by Sir Ghulam Hussain when he presented the budget for 1934-35. The budgeted deficit of Rs. 28 lakhs (1933-34) was converted into a small surplus, mainly as a result of retrenchments effected during the year. The budget for the year 1934-35 was just balanced. The budget for 1935-36, presented by the Honourable Sir D. B. Cooper, contained few novel features. The revenue estimates for the year fell short of the expenditure by about Rs. 29 lakhs. This deficit, however, was reduced to Rs. 2 lakhs as a result of the extraordinary receipts of Rs. 27 lakhs on account of the sale of certain securities formerly held in the High Court Funds, and now transferred to the Government. The Government had no proposals for fresh taxation; the Finance Act of 1932 and the Bombay (District) Tobacco Act, 1933, were however, to be renewed. In the course of the year the Bombay Motor Vehicles Tax was put upon the Statute Book.

§ 3. *The Nature of the Financial Problem:* After having reviewed the budgetary adjustments during the Reform period, we are in a position to visualize the nature of the financial problem

<sup>3</sup> Budget Speech, 1933-34, pp. 2, 3.

of the items. This problem gradually shaped itself during the first five or six years. The large deficit of the first year brought into exaggerated relief one aspect of the problem, viz., the necessity for retrenchment. But retrenchment cannot by itself constitute a major financial problem; the true problem of Government finance is one of spending and not of saving. In the course of the first few years, this essential problem emerged as the Government and the Legislature accepted schemes of beneficial expenditure. In 1922-23 they accepted a programme of compulsory primary education involving an additional outlay of nearly a crore of rupees. In 1924 they adopted the principle of Prohibition which in course of time would have caused a financial sacrifice of Rs. 5½ to 6 crores, according to the calculations of the Prohibition Finance Committee. Further, the Government had launched a costly capital programme of development in the city of Bombay, and of irrigation in the Deccan and Sind. The former was definitely known to be unremunerative by 1925 to 1926. Again, at the very commencement of the Reforms, the Government had sanctioned revised scales of pay for its servants involving an additional charge of nearly Rs. 3 crores annually. Lastly, by the year 1926, or possibly even earlier, the Government as well as the Council had realized that the Meston Settlement had given Bombay a set of revenue heads which had, on the whole, a declining tendency. The problem, therefore, was how to finance the extension of social services in several fields such as Education, Public Health, Agriculture, Industry, etc., in the face of these financial difficulties. The achievement of those in charge of finance and other departments must be judged by the success or otherwise with which they tackled this essential problem.

If those who wielded financial and administrative authority had a realistic appreciation of the problem they would have thought thus: here is a situation in which we have to accomplish certain improvements in social services in spite of the fact that the old revenue heads are showing a declining tendency, and that expenditure on ordinary administration has increased; under such conditions, we can either (1) increase revenue by additional taxation and/or (2) reduce the "cost of government" by effective retrenchment. If these two things are not properly managed, we shall be unable to provide increasing outlays on education and other social services, and also, we shall be unable to go on with projects of social reform such as prohibition which involve large financial sacrifices. But even if our financial provision for the

social services is steady, we shall have to find out ways and means for their expansion *within the available resources*.

In actual fact, we find that few members of the Government or the Council realized the financial situation in these terms. As a consequence the financial and administrative management of the period went on from year to year, without any plan or policy, and ultimately almost nothing was accomplished in the several fields of social reform. Thus, the problem of increasing revenue by additional taxation was handled most half-heartedly. Though something was achieved in the field of retrenchment, there were few economies which were of the nature of permanent reduction in the cost of government. In the fields of Education, Public Health, Agriculture, etc., expansion was hampered by lack of funds, while the policy of prohibition had to be given up half-way owing to financial and administrative difficulties.

The foregoing aspects of the financial problem and the attempts at solution will be discussed in detail in the following pages. Sections 4 and 5 of this chapter deal with the two factors which contributed to the financial problem, viz., declining revenue and increasing expenditure, under certain heads. The succeeding two chapters are devoted to the attempted solution—additional taxation and retrenchment. Chapter X is devoted to the achievements in the field of social services.

§ 4. *The Revenue Trends During 1921-35*: It is a commonplace that variations in governmental receipts are related to changes in policy on the one hand and to changes in prices and incomes on the other. It is not always possible to isolate the influence of these two factors on governmental finance when both operate side by side; but broad conclusions regarding the *predominance* of the one or the other factor may be established with reference to convenient periods of time. Thus, in the case of Bombay revenues, the factor of policy was, broadly speaking, predominant during the first nine years of the Reform period and during the next six years the revenues were largely influenced by price and income changes.

(A) Taking the first period, 1921-22 to 1929-30, we have to note the following facts: (i) The total revenue fluctuated between Rs. 13.50 lakhs and Rs. 12.50 lakhs. There was a general tendency towards a decline, but in the last year, 1929-30, the revenue recovered owing to the rise in the excise receipts. (ii) Land Revenue receipts showed fairly large fluctuations but the general



trend was towards a decline. Obviously, the fluctuations were due to variations in the seasons and to revision settlements involving increase or decrease of assessment. Thus, the decline of nearly Rs. 50 lakhs in 1923-24 was due to the bad agricultural season in several regions, necessitating large remissions and suspensions. The receipts recovered during 1924-26, but, in the year 1926-27, there was again a big drop. The 1927-28 season was disastrous in many districts in Gujarat owing to abnormal rainfall and consequent floods. The next two years were fairly normal.<sup>4</sup> (iii) The excise receipts reached their maximum in 1924-25, since which year they declined continuously. The fall in the excise revenue was almost entirely due to the adoption of the policy of gradual prohibition through rationing and other restrictive measures. Rationing was commenced in 1922. In 1927 the Government accepted the goal of Prohibition and vigorously adopted the restrictive measures calculated to reduce consumption. By 1928, however, the administrative difficulties of enforcing the restrictive policy became evident, and since that year the policy was somewhat relaxed. The difference between the maximum excise revenue (Rs. 443 lakhs in 1924-25) and the minimum revenue (Rs. 383.4 in 1928-29) was nearly Rs. 60 lakhs. (iv) The stamp revenue remained fairly steady at the level of about Rs. 175 lakhs in spite of increments in the rates of stamp duty and court fees. The forest revenue was also comparatively stationary at the average level of Rs. 75 lakhs. The Entertainment Tax and the Betting Tax yielded nearly Rs. 20 lakhs during the latter half of the period.

On the whole, the revenue position during these years was a cause of anxiety to the Government. Sir Henry Lawrence, who was responsible for finance during the first six years of the period, used to harp on this theme year by year in his budget speeches. He used to attribute the entire blame for the sorry situation to the inequity of the Meston Settlement under which Bombay had been made to depend mainly upon inexpansive and even declining revenues. It must, however, be pointed out that in some cases the decline was the result of the deliberate adoption of the policy of prohibition, which caused a fall of more than Rs. 50 lakhs during 1925-29.

(B) During the next six years, 1930-31 to 1935-36, the revenue was adversely affected by the world-wide economic de-

<sup>4</sup> The subject of Land Revenue Legislation which occupied the attention of the Government and the Legislative Council for a considerable period is treated in Appendix A.

pression. In 1930-31 there was a drop of nearly Rs. 2 crores from the 1929-30 level, and though the revenue recovered somewhat in the succeeding years, it continued to cause anxiety throughout the period. Bombay had thus to face the characteristic problem of "depression finance" during the years 1930-35. It is, of course, common knowledge that the provincial revenues are less sensitive to cyclical changes of prices and incomes than the central ones; but there is no reason to suppose that they are non-responsive to these changes. Land Revenue is, obviously, the only important revenue which shows inelasticity in spite of the severe fall of prices and agricultural incomes. The excise revenue declined by Rs. 1 crore in 1930-31, and though it recovered somewhat in subsequent years, it never reached the pre-depression level in spite of the adoption of a more liberal policy in excise administration. The stamp revenue during the period was lower by Rs. 20 to 25 lakhs a year; the forest receipts which reached Rs. 80 lakhs in 1929-30 fell to Rs. 52 lakhs in 1930-31 and remained below Rs. 60 lakhs throughout the depression. These facts show that at least three important Provincial revenues, Excise, Stamps and Forests, showed "cycle-sensitivity" to a fairly high degree.

§ 5. *Increasing Expenditure:* While, thus, the general revenues exhibited a declining trend during the period, increasing expenditure under certain heads constituted the second factor in the financial situation. In some instances (e.g., salaries and debt charges) the additional expenditure was sanctioned even before the commencement of the Reformed Constitution; in the case of others like the Famine Assignment and the Provincial Contribution, the burden was imposed by the financial settlement under the Act of 1919. The following account will serve to give an idea of the increase in public expenditure under the foregoing heads:

(a) *The Salary Bill:* The question of revising the salaries and allowances of Government servants arose as a consequence of the phenomenal rise of prices during and after the Great War of 1914-18. The Calcutta Index Number (1914-100) reached the highest level in 1920, when it stood at 202. In 1918 the Bombay Government sanctioned war allowances costing nearly Rs. 48 lakhs annually, while scales of pay of certain services were also revised upon the recommendation of the Islington Commission on Public Services. The Bombay Government felt, however, that the time had arrived for reconsidering the scales of all cadres of services, Imperial, Provincial as well as Subordinate, and for doing this it

appointed a Committee, upon whose recommendations enhanced scales were sanctioned for the two latter cadres.

As a consequence, the Salary Bill of the Bombay Government increased by about Rs. 3 crores over that of the year 1915-16. (Table No. 10)

TABLE NO. 10

INCREASED SALARY BILL UNDER DIFFERENT CADRES  
IN 1921-22

(Source: Bombay Budget, 1921-22)

(In Lakhs of Rupees)

All-India Services	Provincial Services	Clerk and Non-Gazetted Officers	Servants	Temporary	Establishment and Additional
1915-16	58.32	44.05	1,73.76	14.92	3.57
1921-22	82.49	73.73	3,17.32	16.80	19.83
Increase	24.17	29.68	1,43.56	1.88	16.26

The largest single increase was in the Police Department, in which it was more than Rs. 50 lakhs. The figures given above do not include two items of additional expenditure, viz., (i) an increase of Rs. 41 lakhs in the temporary and provisional allowances and (ii) Rs. 46 lakhs on account of the revised scales of pay for primary teachers.

As these increments came into effect in 1921-22, they constituted an enormous burden on the Provincial finances throughout the period under review. This burden was realized by none more acutely than by Sir Henry Lawrence who, in the course of his budget speech for 1922-23 observed: "We have had to increase the salaries of all Government servants. In the lowest ranks, we have doubled the pay and allowances, for instance, to policemen and school-masters. In the higher ranks we require the officers to bear a large part of the loss. We have adjusted compensation so that the subordinate services secure an improvement of pay of 50 to 70 per cent, the superior services of about 30 per cent, while the most senior officers on the highest salaries receive nothing whatever. The total of this additional allowance has amounted to something over 3 crores, of which 2½ crores

went to the subordinate services, 30 lakhs to the Provincial services, and 30 lakhs to the All-India Services,"<sup>5</sup>

The increased cost of government which resulted from this revision of scales of pay and allowances became less and less justified as, in the course of the Reform Period, the price-level went down continuously. The Calcutta Index Number fell sharply in 1921, and by 1929 it had reached the low level of 141. In 1930 there was again a sharp fall to 116.

During all these years the case for re-considering the scales was obviously strong, but the question was not taken up seriously till 1932, when it came under the searching review of the Thomas Committee on the Re-organization of Government. That Committee recommended lower scales for Provincial and subordinate services which were adopted in 1933. But the financial effect of these revised scales was not very significant during the Reform Period.

In the meanwhile there was a large increase in the pension charges on account of the enhanced scales adopted in 1920. Thus in the year 1921-22, the superannuation allowances and pensions amounted to Rs. 48.5 lakhs; in 1935-36, the figure was Rs. 1,27 lakhs, a net increase of Rs. 78.5 lakhs.

(b) *Interest Charges:* Increasing debt charges constituted the second important increment of expenditure during the Reform Period. Bombay started with the pre-Reform Irrigation debt of Rs. 8,91 lakhs plus Rs. 3,16 lakhs of "ordinary debt" due to the Government of India on account of the Provincial Loan Account. This latter was re-lent to agriculturists, local bodies, Indian States, etc., who paid interest to the Provincial Government. In 1920 the Bombay Government borrowed some Rs. 9 crores at the abnormally high rate of 6½ per cent for the Bombay Development Schemes (viz., Backbay Reclamation, Industrial Housing and Suburban Development). A part of this loan was re-lent to the three city Corporations, the Bombay Municipality, the Port Trust, and the Improvement Trust. Again, the Government undertook projects of irrigation in the Deccan and in Sind involving capital expenditure of the order of Rs. 30 crores. The following estimates of these capital schemes were supplied by Sir Henry Lawrence in his budget speech for the year 1922-23:

<sup>5</sup> Bombay Legislative Council Debates, Vol. V, p. 68.

(Rs. in Crores)

I. *Irrigation:*

Present Deccan	7.5
Present Sind	3.5
Future Deccan	2.5
Future Sind	16.5
	<hr/>
	30.0

II. *Bombay Development:*

Back Bay	8.5
Industrial Housing	9.0
Suburbs	12.0
	<hr/>

These latter estimates were later revised as follows:

Back Bay	Rs. 6.33 crores.
Housing	Rs. 3.50 "
Suburbs	Rs. 3.00 "

By 1925 it was realised that all these schemes would be unremunerative; in the case of the first-named scheme, it was estimated that if all work were closed down the loss would be nearly Rs. 4.88 crores, while if it were proceeded with, the ultimate loss would be nearly Rs. 3 crores. Owing to the extremely complicated nature of accounting adopted in these years in connexion with interest and debt charges, it is almost impossible to estimate the total financial burden on the province entailed by these schemes of development. According to an official calculation, in the ten years from 1st April 1921 to 31st March 1931, the various schemes undertaken by the Development Department cost Provincial revenues a net amount of Rs. 7,18 lakhs.\* During the subsequent years, 1931-32 to 1935-36, the annual net debit on the revenue account was a little more than Rs. 60 lakhs.

Besides the increased debit charges on account of the Bombay Development Schemes, the Government's investments on capital projects in Irrigation, Forests, Civil Works, Agriculture, etc., also involved a considerable drain on the current revenues. The net increase in "unavoidable charges" in respect of debt is shown in Table No. 11.

\* Cf. Financial Position of the Government of Bombay.

TABLE NO. 11  
INCREASE IN DEBT CHARGES  
(In Lakhs of Rupees)

Debt charges (net amount debited to revenue excluding Lloyd Barrage)	1921-23	1935-36	Increase
	72	152	80

(C) Other items which involved large additional expenditure, especially during the early part of the period, were Famine Relief and the Provincial Contribution. Under the Devolution Rules Bombay had to provide an annual assignment of Rs. 63.60 lakhs for famine relief. In 1926 this sum was reduced to Rs. 33.6 lakhs under certain conditions, and in 1927-28 it was fixed at Rs. 12 lakhs a year. The Provincial Contribution during the first four years was Rs. 56 lakhs per year, and in the next two years it was Rs. 34 lakhs and Rs. 28 lakhs respectively.

## CHAPTER VII

### ADDITIONAL TAXATION

§ 1. *Introductory*: The need for fresh sources of taxation was felt throughout the period which, for the purpose of the present study may be divided into two parts, viz., (i) 1921-22 to 1929-30 and (ii) 1930-31 to 1935-36. During the first period, the need arose out of the adoption by the Government and by the Council of two policies, one involving increasing expenditure, viz., compulsory primary education and the other, a substantial sacrifice of revenue (prohibition). The necessity was recognised by the Government and by the Council from the very beginning of the Reformed Constitution. In the first budget speech (1921-22), the Finance Member, Sir George Curtis, stressed the necessity for additional taxation in the interest of budget equilibrium. In the Council Rao Bahadur R. R. Kale's Resolution on Retrenchment recommended to the Government to formulate "proposals for new sources of remunerative taxation." Such proposals were also made by the Compulsory Education Committee (1922) and by the Prohibition (Finance) Committee (1926) to enable the financing of their respective programmes. During the second part of the period (1930-35), the need for additional taxation arose out of the necessity for budgetary equilibrium which had been upset by the enormous decline of revenue due largely to the world economic depression. The actual measure of additional taxation during these two periods are described below.

§ 2. *Additional Taxation During 1921-30*: (a) The rates of duty payable under the Indian Stamp Act were raised in 1922-23 for four years, and they were renewed year by year. The revenue realised from the enhanced rates is obviously difficult to calculate; the official figure is Rs. 12 lakhs a year.<sup>1</sup> In 1926 another amendment of the Stamp Act was passed which raised the duty on transfer of property in the city of Bombay. This was calculated to bring nearly Rs. 3 lakhs. On a rough estimate, therefore, we may take Rs. 15 lakhs as the additional revenue from the enhanced rates of duty under the Stamp Act.

(b) In 1922, the Court Fees Amendment Act was passed and it continued in force for two years. This Act raised the rates of court fees in respect of suits above the value of Rs. 500. In

<sup>1</sup> "The Financial Position of Bombay," p. 11.

1926 the amendment was re-introduced with the difference that the enhanced rates were made applicable to suits of the value of Rs. 5,000 and over. The revenue under this latter was about Rs. 6 lakhs.

(c) As regards new sources of taxation, the Government exploited only two—the Entertainments Tax and the Betting Tax, both being included in the Scheduled Taxes List. The Entertainment Tax was expressly imposed for financing Compulsory Primary Education, but its yield fell much short of the liabilities under the latter. The Betting Tax, though in itself a good measure, could not be a very productive source. The yield under the head "Scheduled Taxes" is given in Table No. 12.

TABLE NO. 12

## SCHEDULED TAXES DURING 1922-30

(Source: Bombay Budget, 1935-36)

(In Lakhs of Rupees)

1922-23	1923-24	1924-25	1925-26	1926-27	1927-28	1928-29	1929-30
2.7	9.4	9.0	15.3	19.6	21.2	21.5	20.1

The three measures described above yielded an additional sum of about Rs. 4 lakhs in 1929-30. It requires no expert knowledge to realise the hopeless inadequacy of these measures to bring in sufficient revenue demanded by the situation. As one looks back upon the record of these years one is amazed at the lack of a sense of realism displayed by the Government and the Legislative Council in this respect. It should have been clear to any one at that time that the policies in only two fields—Education and Excise—would necessitate substantial additional taxation. This should have been realized at least during the years 1926-29, which saw a series of deficits in the budget. If the Government had had a clear view of the financial situation, they would have ordered an expert inquiry in the field of provincial taxation to supplement the labours of the Indian Taxation Inquiry Committee. The least that could have been done was to have investigated the possibilities of some of the taxation measures suggested by the Compulsory Education Committee (1921-22), the Bombay Excise Committee (1922-23) and the Prohibition Finance Committee (1926). For instance, the first-named Committee had suggested, among other measures, succession duties, taxation of



stock exchange transactions and taxation of agricultural incomes. The two latter Committees had also favoured the first and second proposals and had suggested, in addition, an increase of local fund cess, an irrigation cess, etc. The other possible forms of taxation were sales taxes on particular commodities (e.g., on tobacco), a profession tax, a motor vehicles tax, etc. The last-named tax had been referred to by Sir Henry Lawrence in his budget speech for 1926-27 but it was not worked out till 1935-36. The Government, however, considered only one of the foregoing measures, viz., the succession duties, and prepared a bill for imposing these duties in 1927. This hastily-prepared measure was thrown out by the Council.

§ 3. *Additional Taxation During the Depression:* The problem of taxation presented itself once again during the depression years, 1930-36. This time additional revenue had to be raised urgently in order to restore budgetary equilibrium. As already pointed out, the actuals of the year 1930-31 showed an enormous deficit, and the Government was faced with the problem of balancing the budget by additional taxation on the one hand and retrenchment on the other. The following measures of additional taxation were passed during the period 1930-31:

(i) (a) Government raised the motor registration and licence fees<sup>2</sup> which they were collecting under the rule-making powers conferred by the Indian Motor Vehicles Act. The enhanced fees brought in an additional revenue of nearly Rs. 10 lakhs a year. Some years later, the Provincial Government's powers in regard to the levy of such fees were questioned, and they had to be legalised by means of an amendment (1935) to the Indian Motor Vehicles Act. (b) The Government amplified the Bombay Betting Tax of 1925 and introduced the so-called "Bookies' Tax."

(ii) 1932-33: The Finance Act of the year contained the following: (a) The Electricity Duty:<sup>3</sup> Under this, provision was made for the levy of a surcharge on the consumption of electrical energy for lights and fans to be collected from the supplier. Exemption was granted to Government, industries, tramway companies, railways and local authorities hospitals, and to consumers

<sup>2</sup> These receipts were shown under "XIX, Police" in the Budget for 1930-31; in subsequent years up to 1936-37 they were shown under "XXVI, Miscellaneous Departments."

<sup>3</sup> Receipts from the Electricity duty were shown under "XXXV, Miscellaneous" from 1933-34 to 1936-37.

of less than 12 units a month. The revenue estimate was Rs. 12 lakhs a year; the actual yield, however, averaged Rs. 8.8 lakhs during 1932-36. During the Council discussions, complaints were made that the duty would adversely affect "progress," and that it would fall heavily upon the poorer sections of the urban population; it was even suggested that it would induce the users of electricity to go back to oil! (b) The second part of the Finance Act related to court fees. Under it provision was made for the enhancement of court fees in respect of suits above Rs. 1,000. It was pointed out by some members that the enhanced rates would adversely affect the poor agricultural litigant; hence, the Select Committee proposed to keep the rates on suits from Rs. 1,000 to Rs. 10,000 as before. The Government, however, kept the rates as proposed. The additional yield was expected to be Rs. 3 lakhs. (c) A proposal was made in the original bill to levy a stamp duty on forward transactions in the commodity markets and in the Stock-Exchange. The Select Committee, however, opined that the practical difficulties of administration were very great and the proposal was abandoned. (d) Provision was made to enhance the stamp duties on the transfer of property in the cities of Poona, Ahmedabad and Karachi. It was estimated that the additional revenue would amount to a lakh of rupees.

(iii) 1933-34: (a) The Finance Act of 1932 was renewed and the following additional measures were passed: The Bombay (District) Tobacco Act. Under this a licence fee on the sale of tobacco in the Presidency (other than the city of Bombay) was imposed. This yielded Rs. 5 lakhs during the first two years, and nearly half the amount subsequently. Tobacco imported into the town of Bombay was subjected to an enhanced duty (from Rs. 7/8 to Rs. 30 per maund) under an amendment (1932) to the Bombay Tobacco (Town of Bombay) Act. The receipts from this measure were, however, handed over to the Bombay Corporation in order to enable it to bear the increased liabilities on account of the amalgamation of the Bombay Improvement Trust with it.<sup>4</sup> (b) Secondly, additional revenue was obtained from Tolls.<sup>5</sup> This form of impost has an interesting history. As the Honourable Khan Bahadur D. B. Cooper<sup>6</sup> pointed out in 1935, the toll system was applied to Bombay in 1864 under the Government of India Act of 1851. Since that time tolls have been a source of provin-

<sup>4</sup> Receipts under these duties were shown under "XXXV, Miscellaneous" till 1936-37.

<sup>5</sup> Receipts from tolls were shown under "XXX, Civil Works" till 1936-37.

<sup>6</sup> Speech on the Motor Vehicles Taxation Bill (1935). Bombay Legislative Council Debates, Vol. 44 (pp. 1481-82).

cial and local revenue. In 1908, however, due to the numerous complaints raised against the system, the Government announced the policy of gradually abolishing the tolls, a policy which was pursued up to 1914 with such thoroughness that tolls on all Provincial roads were abolished. In 1922, however, some of the tolls on Provincial roads were reimposed for the maintenance of roads. In the year 1933 the Government proposed to increase the revenue from this source. In this they were guided by the following observations of the Thomas Committee:

"In reviewing the revenue of the department (Public Works) we notice that a sum of Rs. 9½ lakhs is realized from the receipts from tolls on Provincial roads. We are aware that it has been the general policy of Government gradually to reduce the number of places at which tolls are levied, but we are very doubtful whether the pursuance of this policy is justifiable in existing financial conditions. Toll may be, and doubtless are, annoying to the travelling public, but they are undoubtedly one of the fairest forms of taxation, since they fall exclusively upon those who are making use of the facilities in respect of which they are charged. It has been argued that taxation of motor transport is already so high that it would be unjustifiable to increase it; if this argument is correct it can be met by the reduction of such taxation in other directions, but should not be met by a method which involves the exemption of all other classes of traffic also. We consider that Government should regard tolls as a regular and legitimate source of revenue and that arrangements should at once be brought into force to increase the tolls levied on Provincial roads by at least one lakh of rupees."

Upon this recommendation the Government re-imposed certain tolls and set up new ones on certain Provincial roads in 1938. In the next year the Government modified the system in the direction of uniformity and simplicity. The net additional revenue derived from tolls ranged from Rs. 7 to 8 lakhs a year during 1933-36.

The new toll system was unpopular from the very start. As a source of revenue it was not so free from objections as the Thomas Committee believed. In a country like India where transport facilities from the rural to the urban centres are ill-developed, anything that hinders free traffic is bound to have adverse economic effects. Again, there was some reason to believe that the incidence of the tolls was greater on the rural peasantry

<sup>1</sup> Report of the Committee on the Reorganization of Government, 1932, p. 264.

already hard hit by the agricultural depression than upon the city dwellers travelling in private cars. Such a statement, however, must be made guardedly, as there are no statistics available regarding the incidence of tolls on different types of vehicles. This fact was complained against by Mr. J. B. Greaves, the representative of the Bombay Chamber of Commerce in the Legislative Council.

Another objectionable feature of the tolls was the farming system adopted for their collection. The system of farming out revenue to the highest bidder has been generally regarded as vicious; in a country of illiterate masses, it tends to become all the more pernicious. In the case of tolls the contractors were known to charge much higher rates than they were entitled to; numerous complaints regarding their excessive exactions had been made from time to time.

It would appear that the Government had early realised the objectionable character of the tolls. In October 1933, Sir Rustom Vakil, Member for Local Self-Government, convened a conference in which the question of their abolition and the substitution of a compound tax on motor vehicles was discussed. The immediate abolition of tolls, however, would have involved a financial loss which the Government could ill-afford to bear under the circumstances. In course of time, however, the Government prepared a scheme for the abolition of tolls and the imposition of a Provincial tax on motor vehicles.

(iv) 1935-36: The Motor Vehicles Tax Bill introduced by Khan Bahadur Cooper in March 1935 was based upon the accepted principles that the multifarious forms of Provincial and local levies on motor vehicles should be substituted by a consolidated tax. This principle was recognised by the Indian Road Development Committee of 1928. Its applicability to the province of Bombay was obvious and urgent; for, here, the motor vehicles were subject to numerous imposts like registration and licence fees, tolls, municipal wheel taxes, etc. The present bill proposed to abolish all these levies; the local bodies were to be compensated for their loss of wheel taxes and tolls; and a consolidated tax on motor vehicles was to be imposed. The bill, however, met with considerable opposition from the representatives of Local Boards and Municipalities, who complained that the Government were taking one of the most fruitful sources of revenue from them.<sup>3</sup> As a result of this opposition this bill was dropped.

<sup>3</sup> Cf. Speech of Mr. Hosenally M. Rahimtoola, the then Mayor of Bombay, in the Bombay Legislative Council. *Bombay Legislative Council Debates*, Vol. 43, Part II.

In September 1935 a less comprehensive measure was proposed and put upon the statute book. This was the Bombay Motor Vehicles Act (1935), which, while abolishing the tolls, retained the municipal wheel tax. It also lowered the registration and licence fees leviable under the Indian Motor Vehicles Act. The rates of tax under the Bombay Act were different for motor cycles, motor cars used for transport of goods, motor cars plying for hire and used for the transport of passengers, etc. In each case the tax rate varied according to weight of goods and the number of passengers.

Out of the proceeds, of the revenue, the local bodies were paid compensation for the loss of the revenue from tolls. It was also provided that if the proceeds exceeded Rs. 26.57 lakhs, the excess should be entered into a separate fund which should be utilized for the construction, improvement and maintenance of roads. The Act came into force on the 1st of April, 1936.

From the account given above, a rough calculation of the amount of additional revenue obtained during 1930-36 may be made. It is estimated that in the year 1935-36, the additional tax burden over that in 1929-30, was as follows:

	Lakhs of Rupees
1. Motor Registration and Licence Fees	10
2. Tolls	7
3. Electricity Duty	9
4. Bookies' Tax	1½
5. Enhanced Court Fees	3
6. " Stamp Duties	1½
7. Tobacco Duties	20

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The contribution of these measures towards the restoration of budget equilibrium was obviously very insignificant. The Tobacco Duty was fairly productive, but its proceeds went to the Bombay Municipality. The objectionable character of the tolls was realised early and they were abolished in 1936-37. The Motor Vehicle Tax proved a fruitful source of revenue but it was imposed in the last year of the period. The Electricity Duty and Motor Registration and Licence Fees together brought in nearly Rs. 20 lakhs, but this sum was quite insignificant compared to the magnitude of the budget deficit.

§ 4. *Conclusions on Tax Policy (1921-35)*: From the foregoing account one is forced to conclude that the Reform Period was characterised by a surprising lack of inventiveness in the field of taxation. This was partly explained by the fact that the Meston Settlement had considerably narrowed the field of Provincial taxation by diverting a large portion of taxable income to the Central Exchequer. Bombay was making a large "indirect" contribution to the Central revenue in the form of the income-tax, customs duties, and excise duties, and this undoubtedly made it difficult to impose additional taxation, as Sir Henry Lawrence used to point out frequently in the course of his budget speeches. But even under the Meston Settlement there was some scope for fresh taxation on those productive classes which, as the Taxation Inquiry Committee had shown, escaped their share of the fiscal burden. For instance, the small traders and substantial landlords could have been made to contribute to the Provincial revenues through selective sales taxes, the agricultural income tax, etc.

There was another reason for the absence of important new taxes. It was widely held that Bombay was the most highly taxed Province, and that any further taxation would be detrimental to the productive capacity and the standard of life of its people. In his Budget Speech for 1927-28, Sir Chunilal Mehta gave the following figures of per capita revenue in the major provinces calculated upon the basis of the actual of 1924-25: Bombay: Rs. 7.4, Madras: Rs. 3.8, Bengal: Rs. 2.2, United Provinces: Rs. 2.7, Punjab: Rs. 5.6.

Such a comparison is, of course, quite meaningless. If at all any significance attaches to inter-Provincial comparisons, it is to the proportion between total income of the Province and the total amount of taxation. Even such comparisons have a limited significance. In truth, the part of the total income which the government of a political unit may slice off for general public purposes depends upon a variety of factors, none of which are statistically measureable. In technical language, the "optimum" of finance of each political unit differs according to the economic and social environment, the standard of living, the distribution of income, and so on. Each political unit, therefore, ought to attempt to adjust its financial operations to such an "optimum" as best it can. In this adjustment, the levels of finance obtaining elsewhere have a very limited relevance.

We are, forced to the following conclusions: that during the period 1921-1936, there was an undoubted need for fresh produc-

tive taxes; but that both the Government and the Legislature shirked their duty of finding out fresh taxes to make good the loss on account of the decline of the old ones; that fresh taxation was not altogether precluded by the financial settlement of the Reforms; but that it undoubtedly rendered the problem difficult by diverting a large portion of taxable revenue to the Central Exchequer.

## CHAPTER VIII

### RETRENCHMENT

§ 1. *Introductory:* Retrenchment in governmental expenditure is of two types: firstly, it consists of temporary cuts in expenditure with a view to attaining a balanced budget and secondly, it is of the nature of permanent reduction in "the cost of government" by means of reorganisation of the governmental machinery with a view to avoiding waste and superfluity in every branch of administration. The former type involves certain comparatively simple budgetary adjustments; the latter necessitates a continuous scrutiny of governmental expenditure and administrative machinery. As a rule the latter aspect of economy tends to be obscured by the former, and this was what happened during the period under review.

During these years the problem of retrenchment presented itself on several occasions. During the initial years of the Reform period, this problem arose in almost all Provinces as well as at the Centre, and several Retrenchment Committees were appointed to suggest measures of economy. This initial economy drive was the product of temporary budgetary difficulties arising out of the trade depression and out of the financial settlement under the Act of 1919. In subsequent years, upto 1930, the problem of retrenchment was not one of making budgetary adjustments, but one of releasing money for the purpose of expanding social services in certain important directions. In the depression period (1930-35) the problem again presented itself in an acute form; this time it was largely a question of temporarily cutting down expenditure for the sake of balancing the budget.

§ 2. *Retrenchment (1921-30):* In Bombay the retrenchment drive was initiated in the very first budget session (February-March, 1921) of the Legislative Council when Sir George Curtis, Finance Member, asked for a grant for the appointment of a Retrenchment Officer to examine office establishments and to suggest economies. In the same session Rao Bahadur R. R. Kale moved a resolution for the appointment of a Retrenchment Committee to examine the whole question of economy in governmental expenditure. In accordance with this resolution a Retrenchment Committee was appointed with Rao Bahadur Sathe (later Mr. C. M. Gandhi) as chairman, and its report was published in 1923. The



Committee suggested direct retrenchment of the order of Rs. 87½ lakhs, exclusive of certain indirect and ultimate economies to which their recommendations were calculated to lead.

In the budget session of February-March, 1922, when the Government put forward proposals for raising the duties levied under the Stamp Act and the Court Fees Act, the Council expressed itself very strongly on the Government's inability to cut down expenditure sufficiently, and threw out the taxation measures. Ultimately the Council agreed to pass them upon an assurance given by the Government that the expenditure estimates would be cut down by Rs. 60 lakhs.

In the budget speech of February 1923 the Finance Member, Sir Henry Lawrence, declared that the retrenchment of Rs. 60 lakhs promised in the previous year was fully effected, and that further economies to the extent of nearly Rs. 38 lakhs had been brought into force by reducing establishments in various departments.

Later, in 1927, a certain amount of saving was effected as a result of an inquiry into departmental expenditures undertaken by Mr. Shillidy. A similar inquiry was made with reference to expenditure of the Public Works Department by Mr. P. G. Shah.

It is not possible for a non-official investigator to estimate the total amount of retrenchment effected during these years, or to calculate what part of it was of the nature of postponement of expenditure and what part represented permanent economy in administration. Nor is it easy to say how the total saving was distributed over the several departments. The official publication entitled *The Financial Position of the Government of Bombay* (page 15) states that total retrenchment was Rs. 63 lakhs. It appears from the *Review of Administration* compiled in 1932 that the retrenchment affected almost all departments, and particularly, Land Revenue, General Administration, and Public Works Departments.

As one looks back upon the financial events of these years, one feels that the Government postponed from year to year the essential problem of effective retrenchment so as to reduce the cost of government. Here again, it should have been clear to the members of the executive government and of the Council that the financial situation demanded something much more drastic in the way of retrenchment than was attempted in these years. The problem was not one of cutting down expenditure here and there

so as to present a balanced budget. The problem, rather, was to release a vast amount of money for financing policies which the Government and the Council had accepted. This would have necessitated certain fundamental and drastic steps in the direction of re-organizing the Governmental machinery. In other words, the problem should have been approached from the point of view of reducing the "cost of government," particularly in respect of the "primary functions" such as General Administration, Police, etc. That the cost of administration was comparatively high in Bombay as compared with other provinces was generally recognised; but from the figures supplied by the Government itself it does not appear that any significant reduction was made in this regard during these years. Figures in Table No. 13 may be of interest in this connexion.

TABLE No. 13

EXPENDITURE ON PRIMARY FUNCTIONS DURING  
1921-1930

(Source: Bombay Budget, 1935-36)

(In Lakhs of Rupees)

Department	1921-22	1929-30	Decrease (-) or Increase (+)
1. Land Revenue and General Administration	193.4	192.2	-1.2
2. Cost of Collection (Excise, Stamps, Registration, Forest, Scheduled Taxes)	89.3	90.7	+1.4
3. Police	186.7	172.9	-13.8
4. Jails and Convict Settlements	31.3	24.4	-6.9
5. Justice	70.-	75.3	+5.3
6. Stationery and Printing	22.5	12.7	-9.8
7. Civil Works	114.3	110.8	-3.5
	707.6	679.0	-28.6

These figures show a small decrease in expenditure, but if account is taken of the increased cost of educational administration due to revised scales of pay for primary teachers, the saving would appear to be quite normal.

The reason why during the period under review there was no effective economy is quite obvious. It is that our public expenditure is largely dominated by one factor, viz., the salaries of public servants, and this factor remained untouched during all these years.

The high scales of pay and allowance sanctioned in 1920 when the price index was at 202 were maintained throughout the period, although in later years the price-level declined significantly. *The fundamental fact that there can be no permanent and effective economy in governmental expenditure without affecting the salaries of public servants* was not fully realized during these years. This fact was appreciated by the Thomas Committee on the Reorganization of Government (1932); but it should have been clear to any one, even without expert knowledge of finance, who watched the events during all these years. By 1926 the price-level had fallen sufficiently to justify a thorough-going revision of the scales of pay in all Provincial and Subordinate services. If this had been effected, the Government would have released large resources for its ameliorative activities and earned the gratitude of future generations.

§ 3. *Retrenchment During the Depression (1930-36)*: The problem of retrenchment arose once again in an acute form during the depression. This time it was largely a temporary problem, necessitating re-adjustments in expenditure and revenue in order to attain budget equilibrium. In magnitude, however, the problem was immense; the decline of revenue in the first depression year, 1930-31, was nearly Rs. 2 crores, and the deficit as revealed by actuals was Rs. 179 lakhs! Retrenchment necessitated by a budgetary disequilibrium of this magnitude was necessarily drastic. The following is a record of the Government's action in this field:

In the budget for 1931-32 the Finance Member announced a cut of Rs. 39 lakhs which mainly affected Civil Works (12.7), Education (9) and Public Health and Medical Departments (5.3). The Education cut was in the form of a 5 per cent reduction in the grants to local bodies for primary education.

Very soon a Retrenchment Committee under the chairmanship of Sir Rustom Vakil was appointed. In the *ad interim* report (July 1932) of the Committee, certain immediately realizable economies were suggested for the purpose of meeting the budget deficit of Rs. 60 lakhs. These suggestions related to the abandonment or postponement of certain schemes of the Public Works Department, reduction in the number of Executive Councillors and Ministers, cut in the primary education grants to local bodies, and scaling down of the salaries of public servants. On the last point all members of the Committee were agreed, though there were differences of opinion regarding the degree of reduction which should be made applicable to the different cadres of service.

In their final report a number of permanent reductions in establishment were suggested. The Committee, however, confessed to an inability to recommend any thorough reorganization of the Governmental machinery with a view to economy. Still, upon its recommendations the Government was able to effect large economies in expenditure. According to *The Financial Position of the Government of Bombay*, the following retrenchments were effected:

	Rs. lakhs
1. Recommendations made in the <i>ad interim</i> Report of the Retrenchment Committee	61
2. Recommendations of the final Report of the Retrenchment Committee	57
3. Action taken independently by Government	40
	1,58

The total figure given by the Finance Member in his budget speech for 1932-33 was, however, only Rs. 137 lakhs, distributed among: Irrigation (16); Civil Works (31); General Administration (19); and Education (27). This includes the cut of 10 per cent in the salaries of public servants, for effecting which an Act of Parliament had been passed.

The foregoing measures of economy were largely of a temporary character. According to the Reorganization Committee: "The major portion of this reduction... has been effected to meet the emergency by means which obviously cannot be continued indefinitely, such as the temporary cut in pay, the reduction in the repair grants for Irrigation and Civil Works, the reduction of grants to local bodies for primary education, etc. The reductions of this nature amount to about 78 lakhs."

In spite of these reductions the budget continued to exhibit a deficit. It was, therefore, felt by the Government that something more drastic must be attempted if budget equilibrium was to be achieved. For that purpose the Reorganization Committee, with Mr. G. A. Thomas as chairman, was appointed in July 1932. The Committee was asked "to make recommendations for the more efficient organization of the whole machinery of Government, and for effecting all possible reductions in the expenditure controlled by the Government of Bombay, having regard to the present or prospective financial position, and the prospect of the development of Provincial autonomy in the near future.... The Government desire to make it clear that the mere pruning of expenditure

is not their sole purpose in appointing this Committee. Something on broader lines is now required. They desire that in addition to securing the maximum reduction of cost consistent with efficiency, the Committee should examine how far adjustments are desirable in the machinery of Government, in the inter-relations of its component parts, and in the relations with local bodies and other organizations, in order to ensure that each branch of the organization shall be so designed as best to fulfil its purpose and to permit steady development in the future.”<sup>2</sup>

The report of the Thomas Committee is the most representative document of “depression finance.” Though the Committee’s principal task was the overhauling of the entire governmental machinery, it paid a good deal of attention to the temporary problem of budget balancing. Though it is not possible to discuss all the problems raised by the report, certain significant financial recommendations may be mentioned.

Among these, perhaps the most important was that which related to the pay, allowances, pensions and other matters connected with the public services. On this question the Committee’s attitude was characterised by unusual sanity. It felt that the rates of pay for public servants in this country were higher than what were necessary to obtain men of the right stamp. The Committee quoted the following observation of the Islington Commission with approval: “To set in India for the public services a standard of remuneration which is in excess of what is required to obtain suitable Indian officers is to impose for all times on the country a burden which she ought not to bear.” Though the Committee could not bring under their purview the question of the pay and allowances of the All-India Services, it found that without reference to that question, the problem of Provincial services could not be handled. For, “it is a fact that cannot be gainsaid that the scales of pay for the Provincial Services have always borne a definite relation to those of the All-India Services. . . . We believe that an undue inflation of the basic pay of the All-India Services is reflected right through every branch of the administration from the superior Provincial Services down to the subordinate establishments, with the result that an artificially high standard of living has been created.”<sup>2</sup>

The Committee then proceeded to recommend lower scales for Provincial Services and the constitution of a Subordinate

<sup>2</sup> Report of the Committee on the Reorganization of Government, 1932, pp. 1, 2.

<sup>3</sup> *Ibid.*

Service. It also suggested reductions in special pay, allowances and pensions.

The Committee made a large number of other recommendations, the total financial effect of which was a betterment of about Rs. 2 crores. This sum was classified by the Government as follows:<sup>2</sup>

	Rs. Lakhs
(a) Savings on pay and pensions	82
(b) Savings dependent upon the sanction of the Secretary of State or the Government of India	20
(c) Savings dependent upon the efforts of local bodies	38
(d) Betterment which is within the power of the local Government and Legislature to secure in the near future	60

Group (a) consisted of an estimated saving of Rs. 57 lakhs in pay, owing to the introduction of revised scales, of Rs. 8½ lakhs in pension charges, and Rs. 15 lakhs due to reduced grants to local bodies in view of the reduction in the pay of primary school teachers. As regards (b) the Government could not definitely estimate the actual realizable saving, since it depended upon the sanction of higher authorities. The category (c) related to the savings which could be effected by reducing the Government's contributions to Local Authorities, which, the report suggested, should increase their resources by raising the Local Fund Cess, and by imposing a professional tax and tolls. Group (d) was divisible into Rs. 20 lakhs of additional revenue and Rs. 40 lakhs of reduction of expenditure. The former consisted of such proposals as the increase in registration fees, the removal of the exemptions in the entertainment duty, the re-introduction of the stamp duty on cheques, tolls, and the increase of fees in the Government colleges. The saving of Rs. 40 lakhs consisted of reduction in various types of allowances, reduction in the number of peons, transfer of the Government secondary schools to non-official agencies, the closure of the Agricultural and Veterinary Colleges, and the Schools of Art.

In 1934 the Government issued a statement regarding the action taken on the recommendations of the Thomas Committee. The most important point in this connexion was the adoption of

<sup>2</sup> This is summarised from "The Financial Position of the Government of Bombay," pp. 16-20.

revised scales of pay for Provincial and Subordinate Services (excepting the Judicial Services), and for clerical establishments in the city of Bombay. As a result of this action an ultimate saving of nearly Rs. 34 lakhs a year was anticipated. The Government also gave effect to certain recommendations regarding the reduction of allowances involving an immediate saving of nearly Rs. 4½ lakhs, and an ultimate saving of nearly Rs. 5¾ lakhs. In the Department of Education, while the Government could not accept the general policy of closing down the Government Arts Colleges, they closed the Deccan College at the end of the academic year 1933-34; in the arts and professional colleges, fees paid by students coming from Indian States and other Provinces were raised. The Government also gave effect to several minor retrenchments suggested by the Thomas Committee. They also adopted two important revenue measures recommended by the Committee, viz., raising the tolls on provincial roads (Rs. 7 lakhs), and enhancing the charges for the registration and copying of documents (Rs. 4.8 lakhs). According to the calculations of the Financial Secretary, the total financial betterment as a result of the effect given to the Thomas Committee's recommendations was Rs. 23.84 lakhs for the year 1933-34, while an ultimate saving of nearly Rs. 75.86 lakhs was expected in the years to come.

The foregoing measures of retrenchment undoubtedly served the immediate purpose of restoring budget equilibrium. The 1934-35 budget was a balanced one, and, though the Budget Estimate of 1935-36 showed a small deficit, the actuals revealed a revenue surplus of Rs. 43 lakhs. It must, however, be pointed out that a good part of the retrenchment effected during these years was of the nature of temporary cuts (e. g., 10 per cent reduction in salaries, and 5 per cent to 19½ per cent cuts in education grants to Local Bodies) which could not be maintained indefinitely. Perhaps the only important permanent saving was that due to revised scales of pay and allowances adopted in 1933-34.

The retrenchment policy of the period raises a large issue in what may be called "depression finance." While the success attained by the policy in restoring budget equilibrium may be recognised, one may well ask whether in a depression period, year-to-year budget balancing is a desirable ideal. Theorists have almost unanimously condemned the policy of ruthless retrenchment since it inevitably tends to deepen the economic depression by discouraging current consumption and investment. It is believed that during a depression the ideal of annual budget

balancing should be given up, and that governmental finance should be based on "deficit budgetting." Such a policy would lead to long-range planning of the budget, with a view to accumulating surpluses in the period of prosperity, which could be used for meeting budget deficits during years of depression. This question is of great importance and it has been discussed at the end in connexion with the future financial policy.<sup>4</sup>

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\*The present writer has discussed this question in the following articles:

- (i) "The Optimum of Finance" (Indian Journal of Economics, July 1939).
- (ii) "Depression Finance of the Bombay Government" (Indian Journal of Economics, April 1941).
- (iii) "The Nature and Characteristics of a Budget" (Bombay University Journal, July 1940).



## CHAPTER IX

### DEVELOPMENTAL EXPENDITURE UNDER THE REFORMS

§ 1. *The Progress of Social Services Under the Reforms:* Under the Government of India Act of 1919 most of what are called "nation-building departments" were handed over to popular ministers in charge of "transferred departments." Most of these departments constituted the so-called "Social Services" like Education, Medical and Public Health, Agriculture and Co-operation, etc., whose extension was accepted as an ideal of financial policy by the Government as well as by the Legislative Council. But the net results achieved during the Reform period were not such as to redound to the credit of those who were in charge of administration and finance in this Province. The total expenditure on the "developmental" departments increased somewhat during the first nine years, but during the depression it was cut down to the original level.

TABLE NO. 14

(Source: Bombay Budget)  
(Lakhs of Rupees)

	1922-23	1929-30	1935-36
1. Education	1,71.1	2,06.2	1,79.8
2. Medical	44.4	46.3	39.9
3. Public Health	17.4	23.6	18.8
4. Agriculture	23.4	29.2	26.1
5. Industries	2.7	1.1	4.1
Total	2,59.0	3,06.4	2,68.7

In this respect the record of provinces like Madras and the Punjab was more noteworthy.

(i) In the Medical and Public Health Departments we find that the expenditure increased by about Rs. 8 lakhs in the period 1921-30, but that it decreased by about Rs. 4 lakhs in the depression period. During the whole period, one scarcely finds any bold programme of expansion, though, obviously, there was much scope for beneficial activity in these fields. In this connection the "Review of Administration" relating to the Public Health and Medical Departments makes interesting reading. It gives a summary of reforms, developments and economics wherein paltry administrative improvements are enumerated. Among others, this

list includes "the reconstitution of the Bombay Medical Service into two classes, the appointment of a Lay Secretary for Hospital Administration, the unification of the supply arrangements for the hospitals included in the J. J. Group in Bombay, the revision of the rules for the levy of fees in Government and state-aided hospitals and dispensaries so as to ensure that non-indigent people who take advantage of the facilities provided by these institutions pay a moderate charge for them, the taking over by the Government of the management of the nursing arrangements at the Cama and Alless Hospitals and of the training school for nurses of the hospital"<sup>1</sup> . . . and so on. But at the same time it is admitted that "from the broad view-point, the medical organization of the presidency is defective," since, "being a hospital organization it is incapable of serving the needs of the rural population."<sup>2</sup> Similarly, it said that "the public health administration in this Presidency is still in an undeveloped stage. In most of the Provinces of India and in countries outside India the tendency is to develop a Government public health service. In this Province the policy is to induce local bodies everywhere to provide themselves with medical officers of health recruited from among general practitioners. But scarcely any progress has been made in rural areas."<sup>3</sup>

An important item, viz., the starting of a school for Tropical Medicine was abandoned early in the Reform period due to financial stringency. (ii) The Department of Agriculture undertook a number of research schemes during the period under review, but many of them were carried out at the instance and expense of other bodies such as the Sir David Sassoon Trust Fund, the Imperial Council of Agricultural Research and the Indian Central Cotton Committee. (iii) The expenditure of the Department of Industries remained at a low level throughout the period. The functions of this department, as suggested by the Bombay Industries Committee (1920-27) included such important services as the supply of industrial and commercial intelligence, technical advice to cottage industries and small organized industries, industrial education and industrial surveys. As, however, the Reorganization Committees pointed out, the provision for the department was so small that it could do little service in these fields. The Committee, therefore, advocated its abolition! (iv) Education: (a) Primary Education: At the very commencement of the Reforms the Government and the Council accepted the ideal of

<sup>1</sup> "Review of Administration in the Bombay Presidency," No. XX (Medical and Public Health), 1933, p. 37.

<sup>2</sup> *Ibid.*, p. 29.

<sup>3</sup> *Ibid.*, p. 65.

free and compulsory primary education. At the instance of the first Education Minister, the Hon. Dr. (now Sir) R. P. Paranjpye, the Government appointed the Compulsory Education Committee under the chairmanship of the Hon. Sir N. G. Chandavarkar to "consider and report on the desirability and practicability of introducing free and compulsory education in municipal and rural areas of the Presidency (including Sind, but excluding Bombay City." The Committee was asked to work out a definite programme of extension of compulsory education, to assess its cost and to suggest financial measures for meeting it. In their Report (1922) the Committee surveyed the existing organization of primary education in the Province and pointed out how it was more costly as well as more efficient than that in other Provinces. The Committee was agreed as regards the general desirability of introducing compulsory primary education for boys and girls within the age-group of five to ten years. They pointed out, however, that conditions of practicability were different in different regions. In Maharashtra and Karnatak, the people were generally in favour of compulsion; but in Gujarat and in Sind, conditions were not so propitious, so that a good deal of caution was necessary while introducing the principle of compulsion in these latter areas. Again, difficulties would have to be faced in applying compulsion to girls, especially in rural areas.

The Committee chalked out a programme of extension of compulsory education spread over ten years. In the case of municipal areas, their proposal was to bring all boys within the sphere of compulsion in five years; in the case of non-city municipalities and villages, the programme would be spread over seven years. At the end of ten years it was expected that the total attendance of boys would increase by 5 lakhs, and that 80 per cent of the boys of school-going age would be brought within the sphere of compulsion. In the case of girls the experiment should be tried first in municipal areas, and then gradually in rural areas as conditions permit. As regards the cost of the programme of compulsory education, the Committee estimated that it would reach a maximum level in the seventh year, after which it would fall slightly, as shown in Table No. 15.

The Committee thus envisaged that at the end of the ten-year period, the municipalities would be spending nearly as much again as they spent in 1921-22, that the District Local Board expenditure would be more than trebled, and that the Government would be called upon to spend nearly Rs. 2 crores out of provincial revenues on primary education.

As regards the actual measures, we may note that provision for compulsory primary education had been made by the Bombay Primary Education Act of 1920. The former applied to Municipalities, but as it was a permissive Act, only four municipalities had taken advantage of it. The latter was applicable to the City of Bombay in which it was adopted in certain wards. The Primary Education Act of 1923 was a more comprehensive measure, covering the whole Presidency except the City of Bombay. The preamble to the Act declared the policy of the Government to be "universal, free and compulsory elementary education for boys and girls to be reached by a definite programme of progressive expansion." The Act had two principal features: one relating to the introduction of schemes of primary education in municipal and rural areas, and the second, relating to the control and inspection of primary schools. These two features should be studied separately.

TABLE NO. 15

## ESTIMATED EXPENDITURE ON COMPULSORY EDUCATION

(Source: Report of the Compulsory Education Committee, pp. 28, 29)

	Municipalities	District Local Boards	Government
1922-23	14	9	123
7th Year	14+15	9+14	123+86
10th Year	14+13	9+20	123+77

(i) As regards the introduction of compulsion, the Act of 1923 permitted the local authorities to prepare schemes and to submit them to the Government for scrutiny. The Act also empowered the Government to call upon local authorities to prepare such schemes, if they failed to do so on their own initiative. In the case of schemes accepted by Government, it was to provide half the recurring and non-recurring expenditure incurred by municipalities, and two-thirds of the expenditure incurred by District Local Boards, in addition to the "datum-line grant," i. e., the grant paid by the Government to the local authority in the year before the transfer of primary education. The Act laid

down the age limit of six to eleven years for the purposes of compulsion.

Let us now examine the actual results and achievements of this measure. These would be indicated by (a) number of Local Authorities which introduced compulsory education; (b) the increase in the number of pupils of school-going age; (c) increase in the number of schools; and (d) the efficiency of the system from the point of view of the growth of "literacy."

Though the Primary Education Act was passed early in 1923, there was considerable delay in giving practical effect to it. Schemes for the introduction of compulsory primary education began to be received by the Government in 1925-26, and their actual adoption commenced from 1927.

(a) Let us first note the number of local authorities that introduced compulsion up to 1935-36. In this connexion it is to be noted that four municipalities and Bombay City had already introduced compulsion under the Act of 1918 and 1920 respectively. Under the Act of 1923, according to the Quinquennial Report on Public Instruction in the Bombay Presidency, 1932-37, (pp. 119, 120) "5 Local Authority Municipalities have introduced compulsion for boys and girls, but two of these, viz., Bombay City and Poona City, have only introduced compulsion in certain parts of the municipal area. Four Local Authority Municipalities have introduced compulsion for boys only and in one of these municipalities, viz., Sholapur, compulsion has only been introduced into three wards. The District Local Board, West Khandesh, is the only Local Board which has introduced compulsion in any form. . . . Very few local authorities are taking serious steps to enforce compulsion when it has been introduced." Several schemes for compulsory as well as voluntary introduction of primary education had to be turned down owing to financial stringency.

(b) As regards the number of pupils attending primary schools, we find that in the decade 1912-1922, the number increased from 5.20 lakhs to 8.60 lakhs. During the subsequent thirteen years, i.e. up to 1935-36, the increase was only 3.88 lakhs, i.e., the number in 1935-36 was 12.48 lakhs. It was calculated by the Compulsory Education Committee that if primary education were to be made universal, provision would have to be made for nearly 17.6 lakhs of pupils. (7.7 lakhs boys and 9.9 lakhs girls); in actual result, only 3.88 lakhs of pupils had been added to the rolls of primary

schools. It should be noted further that most of this increase was due to voluntary expansion of primary education.

(c) Taking the number of primary schools, we find that it was 12,622 in 1921-22, and 14,952 in 1935-36. The Compulsory Education Committee calculated that in 1921-22 there were 10,167 towns and villages having one or more primary schools, and 16,563 villages without a school. In 1935-36 the situation had improved but slightly, there being 10,767 towns and villages with schools, and 16,102 without a school. Out of these latter, 259 villages had a population exceeding 1,000.

(d) As far as the quality of education is concerned, no hard and fast conclusion could be laid down.

From the foregoing evidence it is safe to conclude that the experiment in compulsory education was a failure. The Government admitted that the failure was due to the fact that finances could not be found for the furtherance of compulsory primary education as laid down in the Act of 1923. In this connexion the figures embodied in Table No. 16 are worthy of note:

TABLE NO. 16

## ANNUAL EXPENDITURE ON PRIMARY EDUCATION

(Source: Reports on Public Instruction, Bombay)

(In Lakhs of Rupees)

Year	Municipalities	District Local Boards	Government
1921-22	27.65	5.82	98.22
1926-27	41.87	14.67	1,21.60
1931-32	42.35	14.82	1,00.35

It will be seen from this table that while the Municipalities and District Local Boards had increased their expenditure almost to the extent of the Compulsory Education Committee's expectations, the Government failed almost year by year to provide sufficient funds for the expansion of primary education. We have already referred to the fact that during these years the Government had to refuse sanction to several schemes presented by Local

Authorities for the expansion of primary education on a compulsory or voluntary basis for lack of funds. As a fact, during the depression years, from 1931-32 onwards, the Government had to apply a series of cuts to primary education grants:

1931-32	5 per cent
1932-33	19 $\frac{1}{4}$ " "
1933-34	12 " "
1934-35	12 " "
1935-36	11 " "

It will thus be seen that financial stringency was almost the sole cause which prevented the growth of compulsory as well as voluntary primary education according to the expectations of the Compulsory Education Committee, and of the Minister and Legislature that passed the Act of 1923.

But to say that the Education Department was starved of funds is not to excuse those who were in charge of it during the whole of the Reform period. As a matter of fact all departments of Government had to face financial stringency during these years. We have dealt elsewhere with the cause of these financial difficulties, and pointed out how they arose out of the declining character of the principal revenues, the increased cost of Government on account of increments in salaries and debt charges, and on account of the experiment in gradual prohibition adopted in the commencement of the Reforms. The main point, however, is that those who were placed in charge of education should have realised early, (at least by 1925-26 in which year the Finance Member took stock of the financial situation and pointed out that most of the avenues of retrenchment had been exhausted, that the revenue position was causing anxiety, and that, therefore, new taxation had to be resorted to) that it was chimerical to expect the Government to set aside increasing amounts for primary education so as to meet the requirements of the Act of 1923. It would have been grossly unrealistic for anyone associated with the Government and the Legislature during all these years to expect a provision, let us say, of Rs. 2 crores for primary education! *If the financial position had been realised early, then the entire problem of expansion of primary education would have appeared in a different light.* For a realistic approach to the problem, the education Ministers should have taken for granted that any large increase in financial resources was out of the question; their task, therefore, should have been to work out the possibilities of expanding educational facil-

ities through certain organizational readjustments such as would enable better results to be obtained out of the available resources. Such readjustments should have been directed towards reducing the cost of primary education in a variety of ways.

In this connexion it was realised early that Bombay had the costliest system of primary education in the whole of India. Here the average cost of educating a pupil, as well as the proportion of the cost borne by the Government, was higher than elsewhere.

TABLE NO. 17

## COST OF EDUCATION PER PUPIL

(Source: Annual Reports on Public Instruction, Bombay)

	Average Annual Cost of Educating a Pupil (Boy)	Cost to Government
1921-22	Rs. 17-3-0	Rs. 15-8-0
1925-27	20-0-0	12-14-0
1831-32	17-15-0	10-13-0
1935-36	16-1-0	9-3-0

As against this, we find that in other Provinces the average cost of educating a pupil and the proportion of the cost borne by Government were much lower. Thus, for 1935-36, we have the following figures:

Province	Total Cost Per Pupil	Cost to Government
Madras	Rs. 8-4-0	Rs. 4-13-0
Bengal (1934-35)	3-7-0	1-2-0
Punjab	13-5-0	8-8-0
Bihar & Orissa	6-3-0	0-2-0
Burma	9-13-0	0-2-0
C. P. & Berar	10-15-0	4-1-0
Assam	5-1-0	2-15-0
North-West Frontier	14-4-0	12-0-0

This high cost was due primarily to the scales of salaries for primary teachers prevalent in this Presidency. The starting salaries had been raised in 1921-22 and the grades were fixed some years later in accordance with the Sathye-Paranjapye Scheme, except in respect of the maxima. But while it would have been



difficult (as well as unjust) to lower the scales, it would not have been impossible to reorganize the educational system so as to reduce the average cost per pupil. Some important directions in which this reorganization could have been effected may be indicated:<sup>4</sup>

- (1) Reduction in the number of Government primary schools, and encouragement of private agencies through grants-in-aid.
- (2) Effective prevention of "wastage" through "stagnation."
- (3) Reduction of the primary course from five years to four years.
- (4) Simplification of the curriculum and text-books prescribed for the primary school standards.
- (5) Increasing the number of pupils per teacher.
- (6) Adoption of the shift system on a wider scale.

These reforms would have involved the exercise of a good deal of educational talent and organizing ability. But they would have reduced the demands on finance, and would have enabled a much wider extension of educational facilities, on a compulsory as well as on a voluntary basis, than was possible under the rigid system which was maintained throughout the period.

(a) We must now examine the administrative aspect of the Primary Education Act of 1923. It vested the control of primary education in the elective "School Boards" of Local Authorities. By 1935-36 twenty District Local Boards and forty-eight Local Authority Municipalities had taken over the responsibility of managing primary education. It was claimed in favour of this drastic step in the direction of transfer of control that it brought the public into more intimate touch with education, but on the whole this transfer of control did not prove a success. It was repeatedly admitted that the elective School Boards lacked educational and administrative talent, that they provided a fruitful field for party politics, while the day-to-day administration (particularly appointments and transfers of teachers) had been largely governed by communal or personal considerations. Though the Government retained some powers of supervision and inspection, they were insufficient to provide an effective check on the School Board administration. The situation, thus, was that the Government handed over large funds to Local Authorities without being able to exercise sufficient control over the administration of these funds so as to prevent inefficiency and waste. The whole state of

<sup>4</sup>For what follows the author is indebted to the writings of Mr. R. V. Paralkar, the ex-Secretary of the Schools Committee of the Bombay Municipality. In particular, reference should be made to his "Mass Education in India," and "Literacy in India."

affairs was obviously unsatisfactory, and the Congress Government's amending Act (1938), which ensured a greater measure of control over local authorities, has been a step in the right direction.

(b) Up to now, we have been discussing the state of Primary Education during the Reform period. Something may now be said about progress in other branches of education, such as secondary, collegiate, university, etc.

(i) During the period under review the number of secondary schools increased from 463 (1921-22) to 783 (1935-36), while the number of pupils increased from 77,607 to 1,38,722. The expenditure out of Provincial funds, however, decreased slightly, and so did the number of schools maintained by the Department (34 in 1921-22 to 31 in 1935-36). As is well known, the Government originally laid down the policy of maintaining one "model" high school at every District headquarters; this policy was not, however, pursued rigidly, and latterly some Government schools were closed down. The Thomas Committee rightly recommended the extension of this practice on financial grounds. It is common knowledge that the cost of educating a pupil in Government schools is higher than that in an aided-school; whether, however, the quality of education is better in the former than in the latter (as is often claimed by the Government) is doubtful; or at any rate, unproved.

One aspect of expenditure on secondary education deserves to be commented upon at this stage. It is the comparatively high level of expenditure incurred by the Government on the education of Europeans and Anglo-Indians. Thus, in 1935-36 the Government spent Rs. 3.44 lakhs on secondary schools for Europeans and Anglo-Indians, in which the number of pupils was 5,593. The Government contribution works out at 38.2 per cent of the total expenditure on secondary education for these communities, and at Rs. 61 per pupil. As against this the Government provided Rs. 14.66 lakhs for boys' Anglo-Vernacular Schools, where, in 1935-36, 1,13,247 pupils were receiving education. This comes to 22.5 per cent of the expenditure on these schools, and Rs. 13 per pupil.

(ii) In the field of University education, the Act of 1928 was an important event. The purpose of the Act was to provide greater facilities for higher education, particularly post-graduate teaching and research, in all fields of learning including technology. The Act also extended the elective principle in respect of the composition of

the several University authorities including the Senate. The statutory grant to the University was fixed at Rs. 1,17,000 representing the following:

	Rs.
(i) For development of University work	45,000
(ii) For the School of Economics and Sociology	12,000
(iii) For travelling allowances of Fellows, for charges in connexion with inspection of Colleges	10,000
(iv) For carrying out some of the recommendations of the University Reforms Committee	50,000

In 1921-22, there were 20 Arts and Professional Colleges affiliated to the University; in 1935-36, that number increased to 37. During the same period the number of pupils increased from 8,465 to 17,914. It is common knowledge that the growth of Collegiate education in this Province has been mainly due to the efforts of private educational bodies. The Government closed down the Deccan College at the end of the year 1933-34.

§ 2. *The Prohibition Movement Under the Reforms:* We now turn to the policy regarding excise administration, which involved a large financial sacrifice towards a social ideal. In Appendix B, we have given a connected account of the history of excise policy and administration, wherein we have treated the Reform period in some detail. Here it is sufficient to note that the ideal of prohibition was accepted both by the Government and by the Legislative Council early in the Reform period. The measure adopted for the purpose, particularly "rationing," did bring about a curtailment of illicit consumption of alcoholic liquors and other intoxicating drugs, but it was soon realised that owing to administrative difficulties of enforcing the policy, illicit production and consumption had also increased to a large extent. The Government, therefore, felt by the year 1927-28 that while the policy of prohibition was causing a large decline in excise revenue, no real progress was being achieved towards the goal of prohibition, even of temperance. The policy was, therefore, relaxed in 1928-29 and considerably modified in 1931-32 and in subsequent years.

The entire handling of the excise policy during these years was marked by a lack of realistic appreciation of its financial implications. When the Government accepted the resolution in favour of Prohibition in 1924, they should have realised what the

experiment would mean in terms of finance. This was brought to the notice of the Government in 1926 by the Prohibition Finance Committee which estimated the total cost of prohibition at Rs. 5½ to 6 crores. Now, by 1925 or 1926, no one with any sense of realism would have honestly thought that the Government would be in a position to make a financial outlay on such a scale during the next few years. The Government had already accepted the principle of compulsory primary education and passed an important Act giving effect to it, which involved increasing financial liabilities in the years to come; it had undertaken a costly capital programme in connexion with Bombay Development and Irrigation in the Deccan and Sind; it had raised the salaries of Government servants involving an increase of nearly Rs. 3 crores in the cost of administration; at the same time it had realised that the revenue position, thanks to the Meston Settlement, was far from satisfactory. Under such circumstances, to accept a policy involving an ultimate liability of at least Rs. 5 crores betrayed a lack of sense of financial realities which has no parallel in modern times.

§ 3. *Conclusion:* From the foregoing account it should be clear that from the point of view of the extension of social services and social reforms, the period under review is one of the most sterile in the history of this Province. No bold schemes of reforms were even conceived in respect of nation-building departments except in the field of education and excise. The reform projects undertaken in these two latter fields failed to achieve the desired results owing to financial stringency. In the view of the present writer, much could have been done in these fields if the financial and administrative problems had been realistically approached by those who were in authority during the period. In the field of finance, it should have been realised, at least by 1925 or 1926, that if budget equilibrium was to be maintained, the Government would not be in a position to make increasing outlays on education and other social services, nor could it afford to sacrifice revenue on a scale demanded by the Prohibition policy. Education Ministers should have realised that their problem was to extend educational facilities within the available resources. If they had approached the problem in this way, they would have explored the possibilities of expansion through the internal re-organization of the educational system, particularly in respect of primary education. We have already indicated some of the adjustments which would have resulted in the reduced cost of primary education. In the field of excise policy also, the Government should have frankly

placed before the Council the position that prohibition would involve a financial loss of a magnitude that would totally disorganize the financial structure of the Province and that even then the administrative success of the measure would be problematical. Under such conditions the cause of prohibition and temperance would have been better served if the policy had been applied to a few selected areas, particularly those urban centres wherein the drink evil was largely concentrated. Such measures would have involved less loss of revenue than a general policy of prohibition applied to the whole province, and it would have been more successful in attaining concrete results in the form of a real reduction in the consumption of liquor, as it would have been easier to administer and enforce.

## CHAPTER X

### THE BUDGET FOR 1936-37 AND THE SEPARATION OF SIND

§ 1. *The Budget for 1936-37:* Under the Government of India Act of 1935, Sind was separated from Bombay into an independent Province. The Budget for 1936-37 embodied this important feature of the new constitution. Since it does not come within the perview of Provincial Autonomy, I have seen fit to treat it as a separate entity. I have, however, appended a note on the Separation of Sind, explaining its historical, economic and financial implications.

For the year 1936-37 the financial betterment from the separation of Sind was estimated at Rs. 76 lakhs. The budget gained a further sum of Rs. 22 lakhs, due to the conversion of the Development Loan. As against these gains, there had to be deducted Rs. 53 lakhs—the deficit for 1935-36. The remaining sum was utilised for the abolition of tolls (Rs. 9 lakhs), additional provision for primary and secondary education (Rs. 6½ lakhs), expenditure in connexion with the new constitution (5½ lakhs), etc. In this way the Finance Member handed on “a solvent administration to the control of the New Government.”

§ 2. *Separation of Sind:* The lower valley of the Indus composed of the seven districts of Sind differs much from the Bombay Presidency in point of physical features, climate, language and culture. Its separation from the Bombay Presidency and its constitution into a separate province was long urged by the Muslim League and other associations of Muslims. From the point of view of administration and financial efficiency however, it was thought that Sind would be too small<sup>1</sup> in area and population to form an independent political unit. On this ground the Government of Bombay had considered “the proposal for the separation of Sind... both impracticable and undesirable at present.” The Simon Commission, while expressing sympathy for the claims of the separationists, observed: “There are grave administrative objections to isolating Sind and depriving it of the powerful backing of Bombay before the future of the Sukkur Barrage is assured, and the major readjustments which it will entail have been effected.”<sup>2</sup>

<sup>1</sup> The area of Sind is approximately 47,000 sq. miles, of which about 10,000 sq. miles are desert. Its population according to the Census of 1931 was 3,279,377.

<sup>2</sup> Report, Vol. II, p. 25.

In spite of these pronouncements, the Sub-Committee No. IX of the Round Table Conference (1931) accepted the principle of separation, and observed: "They consider that the social and linguistic differences between the inhabitants of Sind and those of the Presidency of Bombay proper, the geographical isolation of Sind from Bombay, the difficulties of communication between the two, and the insistency with which separation has been advocated, provide an impressive case for the division of Sind from the Bombay Presidency and the creation of a separate Provincial Government there. . . . They observe that the Government of Bombay have pointed out certain administrative difficulties in the way of separation of Sind, but they do not believe them to be insuperable."

§ 3. *The Financial Aspect:* The Committee, however, could not give any definite opinion regarding the financial aspect of the question. This had long been a matter of bitter controversy between the Muslims and the Hindu sections in Sind. The Muslims, who were generally separationists, minimised the financial difficulties of separation. Their spokesman, Khan Bahadur M. A. Khuhro, wrote a book, *The Story of the Sufferings of Sind*, in which he attempted to make out a case for the separation of Sind on historical, linguistic and cultural grounds, brushing aside its administrative and financial difficulties. The Hindus, on the other hand, who were mostly anti-separationists, enlarged upon the financial consequences of separation. Their views were set forth by Professor H. L. Chhablani in his pamphlet, *The Financial Aspects of the Separation of Sind*. He dwelt at length upon the disadvantages of a small province like Sind from the point of view of public finance, and pointed out how the huge deficit that would inevitably attend separation must necessarily involve higher taxation which the people of Sind could hardly bear. That Sind would be a deficit Province was, of course, a well accepted fact; that fact was based upon the figures supplied by financial experts like Sir Henry Lawrence and Sir Chunilal Mehta. In order, however, to obtain the latest data on the question, the Sind Sub-Committee of the R. T. C. recommended that a thorough inquiry be made regarding the financial aspects of separation. Accordingly, the Government of India appointed a Committee of two experts, Messrs. Miles Irving and D. G. Harris, "to examine carefully the probable revenue and expenditure of a separated Sind, the security of the debt on the Sukkur Barrage, and also to recommend an equitable adjustment of the financial commitments for which Sind may properly be considered liable."<sup>3</sup>

<sup>3</sup> Sind Financial Inquiry Report, 1931, p. 1.

The report of the Committee revealed that the separated Sind Province would have to start with a huge deficit. The Committee first calculated the "normal" revenue and expenditure of Sind, and then the additional cost on account of separation. The Committee adopted the data of the three previous years (1927-28 to 1930-31) for calculating the "basic" figures for 1933-34, at which year the Committee expected the separation of Sind to take place. The results were as follows:

	Revenue	Rs. Lakhs
V	Land Revenue	102.05
VI	Excise	33.00
VII	Stamps	20.30
VIII	Forest	6.60
IX	Registration	1.52
IXA	Scheduled Taxes	0.55

Adding to these the administrative receipts and miscellaneous income, the total revenue estimate was Rs. 182.42 lakhs. The total expenditure was estimated at Rs. 279.82 lakhs made up as follows:

	Rs. Lakhs	
5.	Land Revenue	14.39
6.	Excise	3.30
7.	Stamps	0.45
8.	Forests	4.01
9.	Registration	0.82
13.	Irrigation Working Expenses	33.22
22.	General Administration	23.50
26.	Police	41.21
27.	Education	27.24

The deficit of Rs. 97.40 lakhs, excluding any allowance for overhead or direction charges, represented the extent to which Sind was financed by the rest of the Presidency.

Besides this basic deficit, Sind would be burdened with other charges on account of separation. For instance, Sind would have to maintain a gubernatorial headquarters and a cabinet, to build up an additional administrative establishment, and provide other amenities previously obtained from Bombay. The cost of these was estimated at about Rs. 11.045 lakhs, taking the total deficit to Rs. 108.45 lakhs.



The question of the adjustment of assets and liabilities between Sind and the rest of the Presidency was a thorny one. It is well-known that Bombay had raised a huge debt for the Sukker Barrage in Sind, while it had also incurred a large amount of expenditure from ordinary revenue on Sind irrigation. It was at one time suggested that since Sind contributed about 15 per cent of the revenues, the assets and debts should be divided in that proportion. This, however, would have involved constant revenue adjustments which would have proved highly unworkable in practice. The Committee, therefore, suggested (i) "that no question of debt arises at all in respect of past expenditure from revenue. Throughout the years prior to separation the revenues of the joint Province were devoted to those objects, which, at the time, appeared to be the most deserving in the interests of the Province as a whole; it is quite immaterial in which particular division of the Province the expenditure occurred; and all such revenue transactions must, in our opinion, be considered as finally closed; (ii) that the only debt which requires to be distributed is that which entails continuing liabilities in the shape of payment of interest and repayment of capital... (on this question) we have reached the conclusion that the only equitable distribution both of assets and debt is for Bombay to take over all assets situated in the Presidency proper and for Sind to take over all those situated in Sind, each party taking with its assets, any liabilities attaching to them... The adoption of this principle leads to a purely geographical distribution of practically the whole of the debt, the only exception being the debt incurred to finance, the commutation of pensions and the deficits which have occurred since 1930. In the former case the debt has been divided between the Presidency proper and Sind in proportion to the cost of the Pensionable establishment employed in each; in the latter in proportion to their respective contribution to the joint revenues."

§ 4. *The Sind Conference:* The financial difficulties of separation disclosed by the Irving-Harris Report were placed before the Sind Conference convened in April 1932. At this Conference the divergence of opinion and viewpoint—between the Muslim separationists and Hindu anti-separationists came to a head. The former regarded the Irving-Harris estimates of revenue to be too conservative, and of expenditure to be too sanguine; the latter group, led by Professor Chhablani stressed the opposite opinion. In a note presented by the Hindu members, it was argued that the

<sup>4</sup> *Ibid.*, pp. 9, 10.

possibilities of retrenchment and additional taxation to overcome the deficit were not so large as supposed by the Muslim members; while "the anticipated revenue from the Sukker Barrage would hardly be sufficient for the inevitable growth of expenditure in the barrage zone." Their conclusion was that "Sind cannot stand on its own legs for a generation to come, and that any attempt to add to the height of taxation in this period of acute depression will create serious discontent among the non-Muslim communities who are generally opposed to the separation of Sind from the Bombay Presidency but on whose shoulders a very large part of the burden of the proposed taxation is likely to fall."<sup>5</sup>

The President, Mr. Brayne, steered a middle course between the two types of opinion and gave the following estimates:

	Rs. Lakhs
Expenditure (Ordinary)	232.50
Famine Relief	2.05
Pensions	9.00
Interest and Reduction of Debt	27.00
	270.55
Revenue	177.00
Deficit	93.55

He further pointed out that recently Bombay had imposed additional taxation and had effected a good deal of retrenchment. The former would bring Rs. 2 lakhs for Sind, while the latter would mean a saving of Rs. 12 lakhs, so that the financial figure for the deficit would be Rs. 79.55 lakhs. As regards the additional cost of separation, the Irving-Harris figure of Rs. 11.05 lakhs appeared to the President to be reasonable; he, however, pointed out that in view of the financial position of Sind, the figure should be reduced to a certain extent by rigid economy in the expenditure on the Cabinet and the Secretariat.

§ 6. *Sind Under the Government of India Act 1935*: The Government of India Act, 1935, provided for the separation of Sind from the Bombay Presidency and its constitution into a Governor's Province. It was obvious that as a separate Province, Sind would need a subvention from the Government of India to meet the recurring deficits and the initial cost of administrative and legislative establishment. For the year 1936-37 the Government of

<sup>5</sup> Sind Conference Report, 1932, p. 50.

India granted to Sind a subvention of Rs. 1,02 lakhs plus a non-recurring sum of Rs. 6 lakhs. Over and above this, the Government undertook to provide Rs. 17½ lakhs for buildings, etc., in Karachi. As regards the future, Sir Otto Niemeyer recommended a sum of Rs. 1,05 lakhs as a recurrent subvention, and a non-recurrent grant of Rs. 5 lakhs towards the cost of the Shikarpur Jail. The Government of India (Distribution of Revenues) Order, 1936, provided that Sind shall get "in the first year after the commencement of Part III of this Act, 110 lakhs of rupees; in each of the next nine years, 105 lakhs of rupees; in each of the next twenty years, 80 lakhs of rupees; in each of the next five years, 65 lakhs of rupees; in each of the next five years 60 lakhs of rupees; and in each of the next five years, 56 lakhs of rupees."

§ 7. *Financial Arrangements Between Bombay and Sind:* With the separation of Sind from the Bombay Presidency, arrangements were made for the division of assets and liabilities in respect of loans. These arrangements have been thus summarised by the Financial Secretary in his Introductory Note to the Budget for 1936-37.

"All permanent assets will be the property of the Province in which they are situated and outstanding debt linked with the assets will pass with them. Bombay Development loan will remain with Bombay. Barrage debt will pass to Sind, save that the debt of the Nasirabad Section will be taken over by the Government of India, and debt borrowed for the pensionary charges will be divided between the areas on the same basis as other pensionary liabilities, which is that the liability of pensions earned before the date of separation and for loan money applied to meet pensionary charges, including pensions and commutations, and will be divided in the proportions in which the revenues of the Bombay Presidency including Sind have been collected in the two areas. This adjustment throws an additional burden on next year's Bombay Budget, as 34 lakhs of barrage borrowings for pensionary charges will remain with Bombay. Outstanding debt which is not connected with permanent assets, will be similarly allocated. The reason for allocation on this basis is that pensionary charges and unallocated debt are at present the joint responsibility of the Presidency including Sind, their annual costs are a burden upon the two areas in proportion to the revenues which are collected in those areas. Accordingly these responsibilities have been divided in the revenue ratio, which, from an analysis of revenues of the ten years 1922-23 to 1931-32 has been ascertained to be

15 per cent collected in Sind and 85 per cent collected in the Bombay Presidency excluding Sind. The balance in the Famine Relief Fund will be divided on the same basis. The outstanding credits of the Provincial Loans and Advance Accounts will pass to the areas in which the borrowers reside, together with equal amounts of debt to the Government of India outstanding against that account. Loan savings will be allowed according to the purpose for which they were borrowed. Substantial quantities of unissued stores of any class will be divided in proportion to the indents of the two areas over the past three years. The balance at credit of the Road Development Fund will be divided in such a way that, after taking account of expenditure in the two areas, Sind will receive one quarter of the total credits received by the Presidency up to the time of separation."

## CHAPTER XI

### FINANCIAL DEVELOPMENTS UNDER PROVINCIAL AUTONOMY

(1937-1939)

§ 1. *The Economic Background:* The inauguration of the new constitutional arrangements under the Government of India Act of 1935 coincided with a general economic revival in India and in the world outside. In the world economy signs of recovery could be discovered as early as 1933-34, since which year there was a fair progress in point of production, trade and employment in most countries.<sup>1</sup> The motive forces towards economic expansion were different in different countries. In the group of countries led by England, economic revival was the result of cheap money policy, protectionism, industrial rationalization, subsidization of agriculture and building and rearmament programmes. In the U. S. A. it was largely due to the price policy and industrial and agricultural assistance programmes under the New Deal. In totalitarian countries like Germany and Italy, economic revival and expansion were brought about by state control of prices, foreign trade and production, and the attainment of economic self-sufficiency for the sake of war preparation. The forces of economic recovery received a setback in 1937-38, which year saw a "recession" in prices and production, first in America and then elsewhere. Business conditions, however, improved in 1938 and subsequent years, due, in a large measure, to the programmes of rearmament in several countries.

In India the year 1934-35 recorded the first clear indications of revival from the depression of the early thirties. "The Review of the Trade of India" for that year testified to the improved conditions in several industries, particularly cotton textile, jute, iron and steel, cement, paper, etc. There was also some recovery in the prices of certain agricultural products, chiefly oilseeds and cotton. The improvement in the economic condition was kept up during the succeeding two years. Most industries recorded large increases in production, the sugar industry in particular showing phenomenal progress. The agricultural condition also exhibited fair signs of revival, the trend of prices being in the upward di-

<sup>1</sup> See the League of Nations World Economic Survey for 1933-34 and subsequent years.

rection. India's position, in respect of raw cotton, ground-nuts, oilseeds, wheat, etc., improved in a marked manner during these years.

During the course of the year 1937-38, however, India experienced, along with many other countries, a serious "recession" of economic activity. As a result of the economic set-back in America and elsewhere, Indian industry and agriculture showed a sharp decline during the year. After the early months of 1937, agricultural prices went down precipitously, the fall being more than 25 per cent in some cases. There was a similar set-back in industrial conditions. Industrial profits and the prices of industrial shares went down considerably in the course of the year. Prices and production, however, exhibited considerable variation from industry to industry. While the cotton mill industry reached a record figure in production, conditions in the jute industry were highly unsatisfactory, owing largely to internal dissensions. Coal, iron and steel and tea enjoyed a prosperous year,<sup>3</sup> while the sugar industry experienced a decline in production and profits.

During the course of the year, 1938, prices and agricultural and industrial activity remained at a low level. Things, however, began to improve in 1939, while a decisive turn for the better was given by the war which started in September, 1939.

§ 2. *Provincial Autonomy and the Interim Ministry:* Provincial Autonomy under the Government of India Act was inaugurated on April 1, 1937. In the Bombay Legislature the Congress Party had a majority, but as it was not prepared to accept office before certain assurances were given by the Governor, an Interim Ministry headed by the Hon. Khan Bahadur D. B. Cooper was formed. The Hon. Mr. Jinnadas Mehta was in charge of Finance.

The general programme of the Interim Ministry was outlined in a White Paper issued in July 1937. Its principle features were: a progressive policy in regard to free and compulsory education; remission of land revenue in proportion to the fall in agricultural prices; an excise policy directed towards prohibition; improvement of rural sanitation; encouragement of village industries, arts and crafts; and lastly, labour welfare by means of such measures as machinery for industrial peace, minimum wage, etc. This programme was estimated to cost nearly a crore and a quarter of

rupees. Education alone involved an expenditure of Rs. 41 lakhs, while Land Revenue reduction and Prohibition meant a loss of Rs. 24 lakhs and Rs. 30 lakhs respectively. The problem of financing the programme was discussed by the Ministry at the Conference of Ministers held in June 1937. At that Conference the Finance Member, the Hon. Mr. Jamnadas Mehta, pointed out that the finance requisite for the programme could be found in four ways, viz., (1) by retrenchment (2) by the assignment of income tax under Section 138 of the Government of India Act, 1935, (3) by borrowing and (4) by new taxation. As regards retrenchment, its possibilities, said Mr. Mehta, were limited. The second source was governed by the Central Government's Order in Council. In the matter of borrowing, the Provincial Government's powers were restricted under the Act. There remained the fourth source, viz., new taxation, which, said the Finance Member, should be used in such a way that "the poor should be left out and the new burden should be imposed on the shoulders that are capable of bearing it." Bearing this in mind, the Council of Ministers suggested the following measures of additional taxation:

	Rs.
1. Tax on money-lenders	5 lakhs
2. Tax on betting (the rates under the existing tax were to be raised)	6 lakhs
3. Entertainment tax	2 lakhs
4. Electricity duty	15 lakhs
5. Sales tax	1 crore
6. Tax on newspaper competitions	5 lakhs

In the scheme of additional taxation Mr. Mehta laid the greatest stress on the sales tax, a fiscal device extensively used in France, Germany, the Netherlands and some of the States in America. Before, however, the Finance Member had time to work out in detail the legal and administrative aspects of his scheme, the Interim Ministry resigned and the Congress Ministry took office.

§ 3. *Congress Finance:* The Congress Ministry assumed the reins of Government in July 1937, and remained in office till October 1939. During this regime the Finance Minister, the Hon. Mr. A. B. Latthe, presented three budgets, the first in August 1937, the second in February 1938, and the third in February 1939. During all these years, the general financial position of Bombay was better than in any previous period. In the first place, the depression had lifted and the process of recovery had gone well

ahead. Again, as a result of the separation of Sind, Bombay had gained about Rs. 75 lakhs. Further, the Province could reasonably expect increasing receipts from the income tax under the Niemeyer Award. Lastly, as a result of the scheme of debt consolidation, there was a saving of about Rs. 22 lakhs in debt-charges. Under such circumstances, it should have been possible for a Ministry to pursue a moderately progressive policy without disturbing the general financial structure. The Congress Government, however, was bent upon ambitious schemes of development, which could not be accomplished, even partially, during the subsequent years. These schemes were incorporated in the three budgets to which reference has already been made.

i. **The First Budget:** The first budget introduced by the Hon. Mr. Latthe in August 1937 was a hastily prepared document, the Ministry having had less than a month's time to formulate its financial proposals. The Budget speech contained an outline of the Congress programme of a most ambitious character. The speech, however, was marred by graceless attacks upon the financial proposals of the Interim Ministry, one of which was characterised as "not worth the paper on which it was written." The Finance Member's positive proposals related principally to rural relief, which included reduction of the land revenue demand, the provision of water-supply, measures against indebtedness and the encouragement of cottage industries. Other basic features of the programme were Prohibition and Mass Education. The programme was to be financed both by retrenchment and by additional taxation. The former would involve reorganization of the whole administrative system on a more economical basis. In regard to additional taxation, the Finance Member observed: "Our study of the situation has confirmed our view that ours was the most heavily taxed Province in India, and in the opinion of everybody who knew anything of realities, the utmost limits of taxation had been reached." Though this observation was made at the outset, the Finance Member later realised that his programme was bound to involve large financial liabilities and that, in view of the declining trend of the old sources, new taxation would be necessary. In imposing this, care would have to be taken to see that it effected the much-needed shift of incidence from the poorer classes to those whom the Finance Member described as the "taxable-untaxed." The only concrete proposals of this nature were the abolition of the land tax in the case of uneconomic holdings, and the imposition of a levy on the higher agricultural incomes and on the "alienated" lands.



The Budget estimates for 1937-1938 were as follows:

	Lakhs of Rupees
1. Revenue Receipts	11,99.55
2. Revenue Expenditure	12,17.22
Revenue Deficit	<u>17.67</u>

The deficit was to be met out of the surplus of 40 lakhs in the past year's accounts.

ii. The Second Budget: The second budget of the Congress Ministry (1938-39) contained many bold proposals of expenditure and taxation. The revenue receipts were estimated at Rs. 12,09 lakhs, while the revenue expenditure was Rs. 12,50 lakhs, leaving a deficit of Rs. 41 lakhs. The expenditure programme outlined in the budget principally related to the needs of "the large class of poor agriculturists in the Province." For their sake, remissions of land revenue were offered; in some areas substantial forest concessions were to be given; waste lands were to be offered to poor peasants rent free, and in some cases they were to be placed at the disposal of Village Panchayats; village water-supply was to be improved and a scheme for subsidizing medical practitioners to settle down in villages was to be worked out. It was also announced that the construction of minor irrigation works was to be speeded up, and that a programme of rural road construction was to be taken in hand. There was also a fairly large provision for education, mainly in the form of grants to local bodies. Another interesting feature of the educational programme was the starting of the Deccan College Research Institution, for which a recurring grant of Rs. 75,000 and an initial grant of Rs. 50,000 was provided. Lastly, money was sanctioned for an Economic and Industrial Survey Committee which was appointed to enquire into the possibilities of developing the economic resources of the Province. Provision was made for improving the housing accommodation of the Bombay labourers. Lastly, the policy of prohibition was to be initiated in right earnest and this was estimated to involve an expenditure of Rs. 31.5 lakhs. On the whole the expenditure on new schemes amounted to Rs. 1,16.6 lakhs of which Rs. 68.5 were recurrent and the rest non-recurrent.

The mode of financing this programme was thus outlined by the Finance Minister. The non-recurring items were to be largely met out of the revenue surplus of the previous years. In regard to the recurring expenditure, it was to be defrayed

partly by retrenchment and partly by new taxation. The retrenchment principally consisted of a cut of Rs. 10 lakhs in the Government's grant to the Bombay Corporation out of the tobacco revenue in the City of Bombay. New taxation proposals consisted of a surcharge on the Electricity Duty, amendments of the Stamp Act and the Court Fees Act and amendments to the Tobacco Acts. The Finance Member examined the possibility of taxation of sales and of agricultural incomes, and concluded that both these measures were bristling with difficulties.

iii. **The Third Budget:** The Finance Member's speech on the occasion of the third budget (1939-40) contained one significant admission. It was that many of the appropriations for new schemes of expenditure had been unspent for lack of properly-worked-out machinery. In the 1937-38 accounts, the sum of Rs. 5 lakhs, provided for reduction of land revenue, remained unspent. In the accounts of 1938-39 Rs. 5½ lakhs under Irrigation, Rs. 9 lakhs under Education, and Rs. 4 lakhs for Village Panchayats were unspent. Such unspent appropriations were obviously objectionable from the point of budgeting and they were justly criticised in the Assembly. Another significant feature of the budget was the creation of a "Special Development Fund" out of the revenue surplus and unspent appropriations of the previous years. The Fund was to be utilised for what was broadly described as development purposes of a non-recurring character. The estimates for 1939-40 were:

Revenue Receipts	Rs. 12.55 crores
Revenue Expenditure	Rs. 12.83 crores

The deficit, which was due to non-recurring expenditure, was to be met out of the opening balance.

The financial programme of the year was of a most progressive character. A separate Rural Development Department was to be instituted for taking over the various rural welfare activities of the Government. The total new expenditure on rural development was estimated at Rs. 45 lakhs. A loss of Rs. 40 lakhs was to be incurred as a result of land revenue reductions in accordance with the new legislation. The biggest item was, however, the loss of Excise Revenue (Rs. 150 lakhs) in addition to the expenditure on preventive measures (Rs. 15 lakhs) on account of Prohibition. The total cost of the programme was put at Rs. 250 lakhs.

This huge programme was to be financed by additional taxation. The enhanced Electricity Duty was expected to yield Rs. 17

lakhs; the new Urban Immovable Property Tax was estimated to produce nearly a crore and a quarter of rupees; sales taxes on petrol, and on mill-made cotton and silk cloth were to realise Rs. 35 lakhs; a tax on prize competitions was expected to yield Rs. 5 lakhs. Further it was stated that the Government were exploring the possibility of an Agricultural Income Tax and of reducing the losses on the "alienated lands."

Such in outline was the "Prohibition Budget" of 1939-40. In the course of the next few months a large part of this programme was put on the statute book. Thus the prohibition programme, begun in the previous year in Ahmedabad, was extended to Bombay City. The taxation measures were duly passed with certain modifications. Before the year was out, however, the Ministry resigned.

§ 4. *General Review of Congress Finance:* After having given an account of the three Congress Budgets, we proceed to review the general financial developments during the Congress regime. The following are some of the noteworthy features about the Revenue position:

(a) *The Income Tax:* Increasing receipts under the income tax have been a very favourable factor in Provincial finance under the new constitution. We have already noted that under Section 138(1) of the Government of India Act, 1935, a prescribed percentage of the income tax receipts was to be handed over to the Provinces. Upon the recommendations of Sir Otto Niemeyer, the Government of India (Distribution of Revenues) Order of 1936 was issued, which fixed the percentage at 50, and the share of the Bombay Government at 20 per cent of the Provincial share. The Order also laid down that the Central Government may retain for five years, either the whole of the Provincial share or as much of it as together with the Railway contribution to general revenues, shall bring the Central Government's share up to Rs. 13 crores. The Provinces, as we have seen, complained against this latter provision and the Order was modified with effect from 1st April, 1939. The revised Order provided that the sum which the Central Government may retain out of the Provincial share shall be Rs. 4½ crores a year during 1939-42. This provision is obviously favourable to the Provinces, and under it Bombay received Rs. 55.80 lakhs in 1939-40.

(b) *Land Revenue:* When the Congress Ministry assumed office, high hopes were entertained in regard to the reform in the

land revenue administration, particularly in view of the following pronouncement contained in the Congress Election Manifesto: "Pending the formation of a fuller programme, the Congress reiterates its declaration made at Karachi that it stands for a reform of the system of land tenure and revenue and rent and an equitable adjustment of the burden on agricultural land, giving immediate relief to the smaller peasantry by a substantial reduction of agricultural rent and revenue now paid by them, and exempting uneconomic holdings from payment of rent and revenue."<sup>2</sup>

In his first budget speech Mr. Latthe admitted "the anomalies which had crept into the system of classification of lands and the rate of assessment dependent upon that classification," and recognised that "our first duty, therefore, was to give relief by way of reduction of the State demand." At that time the Finance Member could write off all arrears except those in respect of the previous year, and reduce the demand in the case of over-assessed lands to the extent of Rs. 5 lakhs. The latter, however, could not be effected, since, in the absence of definite principles, the sum could not be allocated for the intended purpose. It became clear, therefore, that the question of relief in assessment must be considered as a part of a larger scheme of reform of the land revenue system as a whole. The Ministry, thereupon, set about the task of preparing a comprehensive measure dealing with the subject. In April 1939 they presented the Land Revenue Code (Amendment) Bill, which subsequently became an Act. This measure has been discussed in Appendix A.

(c) Excise: A detailed account of the Congress Prohibition programme is given in Appendix B. It is sufficient here to observe that the programme involved an immense sacrifice of revenue. In the budget for 1938-39 the loss was estimated at about Rs. 31 lakhs, in the 1939-40 budget, an additional loss of Rs. 1,50 lakhs was visualised, while an additional expenditure of Rs. 10 to 15 lakhs was also provided for. Obviously the loss of revenue of this magnitude could not be met out of old sources; recourse, therefore, had to be taken to additional taxation.

(d) Additional Taxation: (1) The Finance (Amendment) Act of 1939 contained the following provisions:

The rates of Electricity Duty were raised, except in the case of cinemas and theatres. The exemption granted to consumers of less than 12 units under the old Act was deleted and such con-

<sup>2</sup> Quoted by Mr. Jammadas Mehta in his speech on the Finance Act (Amendment) Bill, 1939, (B. L. A. D., Vol. 5, p. 1110.)

sumers were subjected to a duty of one anna per unit. Those consuming more than 12 units were subjected to a duty of half an anna more than what they paid before. In order that the consumers might not be subjected to a higher burden, the Government prevailed upon the Bombay Electric Supply Company to reduce its own rates correspondingly. The higher rates which were made applicable to Bombay City, were to be extended by notification to other urban areas. It was also provided that electrical energy consumed by a person who was not a licensee and who generated energy for his own use, might be subjected to similar duties. Under these enhanced rates, the receipts from the Electricity Duty increased from Rs. 17.95 lakhs (1938-39) to Rs. 31.31 lakhs (1939-40).

(2) The Finance (Amendment) Act of 1939 also imposed the Urban Immovable Property Tax. It applied to buildings and lands in Bombay and Ahmedabad at the rate of 5 per cent of the annual letting-value when it did not exceed Rs. 2,000, and 10 per cent when it exceeded Rs. 2,000.<sup>3</sup>

(3) By the same Act, Court fees payable in respect of plaints, probates, letters of administration and certificates of succession were raised, and so were the fees payable for the institution of suits.

(4) By an amendment of the Stamp Act, the duties payable on Stock Exchange agreements were doubled. The Government intended to extend the duties to transactions in other forward markets.

(5) In 1939-40 the Sales Tax Act was passed under which all Trades carrying on business in the sale or purchase of certain goods (specified in the schedule) were to take a licence for such a trade, which would be liable to be cancelled in case of contravention of provisions of the Act in respect of maintenance of accounts. The sale of articles mentioned in the Schedule, (viz., motor spirit and manufactured cloth) was subjected to a tax at a maximum rate of 1 anna in the rupee. In the course of the year, however, the sales tax on cloth was abandoned owing to administrative difficulties.

Let us now turn to the expenditure side. Table No. 18 sets forth the trends of expenditure since the inauguration of Provincial Autonomy. The figures for 1936-37 are given for facili-

<sup>3</sup> The rates were reduced in subsequent years.

TABLE NO. 18

## EXPENDITURE CHARGED TO REVENUE OF THE BOMBAY GOVERNMENT

(Source: Bombay Budgets, 1942-43, 1945-46)

(In Lakhs of Rupees)

Heads of Expenditure	1936-37	1937-38	1938-39	1939-40	1940-41	1941-42
1. Direct Demands on Revenue	160.19	157.72	176.54	167.81	176.04	186.91
2. Irrigation Revenue Account	48.20	54.09	50.97	53.39	52.25	52.09
3. Debt Services	162.43	123.16	125.82	125.30	121.26	118.38
4. General Administration	104.97	102.88	80.91	78.77	75.20	87.06
5. Administration of Justice	62.19	62.69	66.53	66.43	65.63	67.23
6. Jails and Convict Settlements	18.04	17.32	16.33	16.82	18.62	21.18
7. Police	142.76	142.34	143.70	150.31	157.54	172.81
8. Ports and Pilotage	0.05	0.05	0.02	0.05	0.06	0.01
9. Scientific Department	0.96	1.06	1.03	1.14	1.09	1.07
10. Education	159.98	168.05	190.64	200.17	193.90	206.73
11. Medical	41.79	43.54	45.33	46.39	54.43	53.19
12. Public Health	22.60	24.06	24.54	28.10	28.13	34.62
13. Agriculture	13.76	13.63	14.80	11.99	11.74	19.74
14. Veterinary	3.90	3.98	4.10	4.41	4.39	4.57
15. Co-operation	6.08	6.09	6.14	15.76	18.25	15.05
16. Industries	6.57	7.58	8.92	7.65	6.96	8.80
17. Miscellaneous Departments	7.11	7.68	8.34	11.74	9.67	10.92
18. Civil Works	110.88	151.32	123.05	126.31	110.28	153.24
19. Famine Relief	2.05	7.12	3.06	0.66	1.00	1.50
20. Transfers to Famine Relief Fund	—	6.51	1.70	—	—	2.42
21. Superannuation Allowances and Pensions	107.52	110.87	115.16	120.38	124.87	128.84
22. Commutation of Pensions	0.06	0.06	0.04	0.03	—	—
23. Stationery and Printing	12.40	13.18	12.58	12.67	17.05	18.57
24. Miscellaneous	6.39	6.94	55.97	35.61	110.21	157.22
25. Extraordinary Charges	0.17	0.34	0.36	1.38	2.84	1.21
Total Expenditure on Revenue Account	1,201.07	1,214.31	1,279.58	1,283.27	1,360.61	1,325.38

# FROM 1936-37 TO 1946-47.

1942-45	1937-41	1941-45	1937-46
217.82	276.41	375.40	275.45
50.65	48.73	65.04	72.77
122.35	152.00	336.00	349.43
88.80	100.82	122.11	122.91
70.02	75.50	81.54	82.06
34.58	55.62	43.91	38.27
212.29	248.56	265.94	275.10
-0.01	-0.02	0.01	0.02
1.21	1.11	1.32	1.52
209.31	219.30	243.50	263.24
56.29	76.88	91.14	84.63
42.37	36.01	50.37	62.26
30.38	54.59	119.48	176.95
5.08	5.86	8.42	8.31
12.24	9.92	11.98	16.04
9.40	13.94	16.82	22.70
20.68	35.44	72.14	127.40
172.90	149.98	191.95	227.91
12.72	81.13	82.00	1.50
—	—	—	—
130.57	134.79	146.13	153.29
—	—	—	—
19.68	26.41	25.60	28.09
41.82	181.94	316.12	66.52
4.55	—	—	—
778.78	2,150.00	3,122.59	2,908.95

tating comparison. The following were some of the noteworthy features in regard to the expenditure under the Congress regime:

(a) Debt Charges: It will be noticed that there was a large saving in debt charges subsequent to the year 1936-37. It was due to the repayment and conversion of the Bombay Development loan of 1920, and to the adoption of the scheme of "Debt Consolidation" upon the recommendation of Sir Otto Niemeyer as already described.

(b) Extraordinary Charges: The increase in these charges for the year 1939-40 was due to the provision for purchasing the lands forfeited and sold during the Civil Disobedience Movement.

(c) Pensions: Another important increase in expenditure is in respect of the head, "Superannuation Allowances and Pensions." These charges had been increasing since the Reforms as a consequence of the higher scales of salaries adopted after World War I.

(d) The Special Development Fund: In 1939-40 a provision of Rs. 50 lakhs was made for the formation of a "Special Development Fund." It does not appear that the Fund was constituted for any comprehensive plan of economic development. Rather, it was a solution for a technical accounting difficulty that the Ministry had faced for the previous two years. In 1936-37 and in 1937-38, the Government had contemplated the spending of the surpluses on non-recurrent schemes, such as village water-supply, minor irrigation, etc. Both owing to the absence of well-prepared plans of expenditure, large amounts remained unspent and, therefore, lapsed. "Government have, therefore, reconsidered what the best means is of spending the free balance that is expected to be available at the beginning of the next year. After careful consideration they have come to the conclusion that it will be best to set apart this money in a separate fund to be called 'Special Development Fund.' One of the results of this scheme will be that the sanctioned expenditure will run continuously and smoothly without fear of grants lapsing on a particular date. . . . This fund will be operated upon in the same manner as certain funds granted by the Central Government such as, for instance, the Central Road Development Fund. To the extent that money is required for financing schemes debitable to this fund, it will be taken as a receipt in the Revenue Section and the corresponding expenditure will be shown under the service head. The result will be that the expenditure from the Development Fund will not af-



fect the revenue surplus or deficit. Secondly, whatever money is not utilised will remain in the Fund and will only be available for the purposes for which the Fund may be used. We propose to utilize the Fund for what may be broadly described as development purposes of a non-recurring character."<sup>4</sup>

(e) Education: In the field of education the Congress Ministry attempted a good deal during its regime of about two years. The total expenditure on education increased by about Rs. 40 lakhs, of which a large part was spent on primary education. The progress in the several educational fields is briefly indicated below:

(i) Under their scheme of "Mass Liquidation of Illiteracy," the Congress Ministry launched a programme of expansion of primary education. The following table brings out the progress in respect of the number of schools, pupils and expenditure.

TABLE NO. 19  
PROGRESS IN LIQUIDATION OF ILLITERACY

(Source: Annual Reports on Public Instruction)

	1936-37	1937-38	1938-39	1939-40
Number of Schools	12,901	13,244	16,435	19,115
Number of Pupils	11,40,299	11,91,509	13,22,668	15,00,456
Expenditure out of Provincial Funds	97,66,831	1,00,31,231	1,16,16,611	1,22,124
Percentage of Prov. Expenditure	—	55.0	60.5	61.1

A marked feature of the expansion of primary education was the opening of a large number of "voluntary schools" in villages with a population of less than 700. The Government set aside a sum of Rs. 4 lakhs in 1938-39 for financing the scheme, out of which grants were given to local agencies for starting voluntary schools. It would appear that the scheme received a very satisfactory response, as seen from the fact that in 1938-39 a little less than 2,400 voluntary schools were opened. In 1939-40, the sum allotted for the purpose was Rs. 9½ lakhs and the number of new schools opened was 2,492. There was a fair increase in the number of Local Board Schools also. The number of pupils attending primary institutions increased from 114 thousand to 150 thousand, while the expenditure on primary education out of Provincial Funds rose from Rs. 97.6 lakhs to Rs. 122.2 lakhs.

<sup>4</sup> Brochure on Bombay Development Plans, 1939, p. 1.

The latter increase enabled not only the starting of new schools under the scheme described above, but also the restoration of cuts applied to grants to local bodies, and the payment of arrears of the grant to the Ahmedabad Municipality. During the period under review an attempt was made to introduce "basic" schools based on the "Wardha Scheme." In the earlier period, agricultural bias classes were started with a view to adapt primary education to rural needs. Under the Congress plan, the syllabus was given a "craft" bias, the craft chosen being spinning and weaving. The experiment was inaugurated in 1939, but subsequently, many schools of this type had to be closed on account of several difficulties which cropped up. It appears that this whole subject needs much more inquiry and investigation at the hands of educational experts than it has received till now.

The question of training of primary teachers also engaged the attention of the Government. In 1936-37 less than 50 per cent of the teachers were "trained." Early in 1938 a Committee was appointed to consider the question of expanding the facilities for the training of primary teachers, and its report contained many valuable suggestions. The details of the scheme suggested by the Committee were worked out by the Educational Inspector, and it was brought into effect in 1939-40. During that year the number of training institutions increased by ten, while the number of pupils admitted for training rose from 1,900 to 3,500. The expenditure on primary training institutions increased by more than a lakh and a half of rupees.

A bold step was taken in the matter of the control of primary education. Under the Primary Education Act of 1923, the control of primary education was vested in School Boards elected by the local authorities. The School Boards were made responsible for opening new schools, appointment and transfer of teachers, and the framing of rules for their employment. The Government's duties were of a purely advisory character, though it retained some check through the process of audit. The control of primary education by the Elective School Boards was recognised to have given rise to serious evils.

As a result, the progress of primary education, especially compulsory education, was not satisfactory, and it was high time some bold steps were taken to remedy the state of affairs. In March 1938 the Prime Minister and Minister of Education, Mr. B. G. Kher, introduced the Bombay Primary Education Amend-

ment Bill which sought to radically alter the organisation of primary education. The Bill which subsequently became an Act contained, among others, the following provisions: The administrative officers became Government Servants with definite powers; the inspecting staff was placed under Government control; minimum educational qualifications were prescribed for members of School Boards over which the Government had certain powers of control; powers of appointing administrative officers were delegated to certain municipalities; and a Provincial Board of Primary Education was established for advising Government on matters relating to primary education. It is reported that the new arrangement has been working smoothly, though in the beginning there was some friction between School Boards and Administrative Officers.<sup>5</sup>

Some progress was recorded in the field of adult education. Till 1937 adult education received little financial assistance from the Government. From 1937-38 the Congress Government launched a policy of assisting private agencies like the Bombay Literacy Association, the Bombay Presidency Adult Education Association, etc., to expand facilities for adult education. The financial provision was only Rs. 10,000 in 1937-38, but it was increased to Rs. 40,000 in 1938-39, while in 1939-40, more than a lakh and a half of rupees were utilised for the purpose of giving grants-in-aid. For advising Government on these matters, a Provincial Board of Adult Education was appointed on the recommendation of the Adult Education Committee (1938).

(iii) In the field of professional education, special efforts were made to increase facilities for technical training. A few new institutions were started, such as the Leather Working School and Tanning School at Khar. Another important development in this field was the provision of physical education. In September 1937, the Government appointed the Physical Education Committee to consider the question of physical education in primary and secondary schools, and upon its recommendation the Physical Training Institute was opened at Kandiwali in November 1938.

(iv) In the field of higher education, the establishment of the Deccan College Research Institute deserves to be specially mentioned. In the budget for 1938-39 the Finance Member asked for a non-recurring grant of Rs. 50,000 and a recurring grant of Rs. 75,000 for this institution. The actual amount of recurring

<sup>5</sup> Vide Report on Public Instruction, 1939-40 and 1940-41, and also the Quinquennial Report on Public Instruction, 1937-42, p. 35.

expenditure has been less than this sum. The Institute specialises in post-graduate research in such subjects as Linguistics, Vedic Literature, Ancient and Medieval History, Maratha History and Sociology.

(v) Rural Development: In the budget for 1939-40 the Finance Minister asked for a provision of nearly Rs. 45 lakhs for rural development. This was to be utilised for building up a rural development organization, to which would be entrusted a large number of rural welfare activities. Early in March 1939, the Government resolved that these activities would best be performed by the co-operative Department and that, therefore, the latter be designated "the Co-operative and Rural Development Department." It was decided that this Department should take over the propaganda work carried on by the Department of Agriculture, and that "work in the College of Agriculture, research, experiment and livestock improvement and the propaganda staff of the Department which consists of 45 District agricultural overseers, 30 agricultural suboverseers, 29 permanent kamgars and 50 temporary kamgars (in charge of Taluka Demonstration Centres) should be transferred to the Co-operative Department. . . . In due course the propaganda work of the Industries and Veterinary Departments, so far as it affects rural development, should also be taken over by the Rural Development Department."<sup>6</sup> The newly constituted Department was to be reorganised on the following lines:

(a) "There should be a Board of Rural Development consisting of the Registrar of Co-operative Societies and Director of Rural Development, the Director of Agriculture, the Director of Veterinary Services, and the Director of Industries and a few non-officials nominated by Government with the Hon'ble Minister in charge of Rural Development and Agriculture as Chairman. The function of the Board should be to advise on general principles and policy regarding rural development activities."

(b) The Registrar of Co-operative Societies and Director of Rural Development was to be given assistance by a Deputy Director in connexion with Rural Development, and by an expert in connexion with co-operative finance. Further, the Assistant Registrars of Co-operative Societies should be entrusted with duties of Rural Development Officers in the Districts. In each district there should be a Rural Development Association consisting of Departmental Officials and some non-officials. It was decided to appoint

<sup>6</sup> Government Resolution, Revenue Department, No. 15/33, dated 8th March, 1939.

about 1,000 workers for propaganda work in connexion with agricultural improvement, co-operation, cottage industries, village panchayats, and rural welfare in general.

In June 1939 the personnel of the Provincial Rural Development Board was announced. In order to facilitate the work of the Board, the following Committees were constituted: (i) Agriculture and Live Stock Committee, (ii) Cottage Industries Committee, (iii) Training and Propaganda Committee, (iv) Backward Areas Committee.

The Board and the Committee met in July 1939 and considered a large variety of subjects such as legislative and administrative measures for improving the economic condition of the villager, measures for land improvement and water-supply; measures for introducing better cultivation methods including the preparation of manures, removal of crop pests, etc; horticulture; marketing with special reference to the proposed Bombay Agricultural Produce Markets Act; the improvement of live-stock; cottage industries and subsidiary occupations to agriculture; training of rural workers; and development of backward areas.

The activities of the Rural Development Department for 1938-39 and 1939-40 have been set forth in the Administration Reports of the Department for the respective years. It appears that the department has been doing valuable work in connexion with (i) prevention of soil erosion, (ii) extension of "dry farming" methods, (iii) improvement of measures, (iv) introduction of better methods of agriculture including improved implements, seeds, etc., (v) control of insect pests, (vi) improvement in horticulture, and (viii) the popularization of these methods through shows, demonstration centres and classes. It appears, however, that many of the large grants voted for rural welfare work in 1938-39 and 1939-40 remained unutilized. We have already noted that the "Special Development Fund" was created in 1939-40 mainly in order to prevent the lapse of such grants on account of non-utilisation in the budget year. It is to be noted that in the year 1939-40 also, there were many instances of this character.

In one respect, however, the work of the Co-operative and Rural Development Department deserves special mention and that is in regard to the encouragement of "multi-purpose" co-operative societies as agencies for rural welfare work including debt adjustment. The idea that co-operative societies, instead of confining

themselves to a single purpose, should embrace all aspects of rural life, including farming, marketing, public health, education, debt conciliation, etc., has been gaining ground in recent years, and has been particularly fostered by the Reserve Bank of India.<sup>7</sup> The Congress Government accepted the principle underlying the multi-purpose co-operative societies and made an attempt to encourage their formation so that they could serve as an agency for the rural welfare programme. In 1938-39 seven experimental societies were started, and as a result of active propaganda, their number increased to 65 in 1939-40. In subsequent years, however, the pace slowed down, partly due to the realization of certain practical difficulties in their working.

§ 5. *Critique of Congress Finance:* The appraisal of a scheme of public finance must ultimately depend upon our conception of social welfare which in its turn is based upon our final values in life. Yet, there are certain purely economic and technical considerations which can be applied in judging any attempt at financial reform. The following observations are offered in the light of the latter type of considerations.

We have noted that the Congress Ministry was fortunate in having started with a comfortable financial position. By the time Provincial Autonomy was inaugurated, Indian economic life had started well in the direction of recovery. Again, Bombay had gained something like Rs. 75 lakhs out of the separation of Sind. A small relief had been obtained as a result of debt consolidation. And, lastly, arrangements in regard to the sharing of the income-tax promised an increasing revenue, which, in actual fact, exceeded the most optimistic expectations.

As a result of these favourable factors, the Congress Ministry enjoyed an additional revenue of something like Rs. 1.5 crores without any additional taxation and retrenchment. This sum could have been increased to about Rs. 3 crores through tax measures which would not have burdened the poorer classes, and by retrenchment which would not have affected administrative efficiency. This amount could have been utilised for financial reforms of a type both practicable and desirable; but instead of this, the Congress Ministry attempted a wholesale reconstruction of the financial structure with one objective, viz., Prohibition. The result was that many reforms that were urgently needed were not

<sup>7</sup> Reference may be made to the general bulletins and reports published by the Reserve Bank, and particularly to (i) Co-operative Bank of Kodinar (ii) "Review of the Co-operative Movement in India," (1941).

attempted, and those that were attempted were not effectively carried out. In what follows, I have enumerated some of the sins of commission and omission in the field of taxation and expenditure.

**Tax Reform:** A programme of tax reform does not raise merely legal and administrative issues; it necessarily assumes certain fundamental economic and social values. The principle economic question always is, Do we want our tax-system to reduce distributional inequalities? If we do, then we have to know how the present tax system affects the different income groups and productive classes, and proceed to shift the tax burden from one class to another. Such a study of the "incidence" of taxation has not yet been carried out adequately and, therefore, Provincial ministries had to proceed upon certain assumptions in their scheme of tax-reform. One of these assumptions is summed up in the vague statement that the present structure of taxation is regressive, and that the fiscal burden is relatively greater on the poor than on the rich. This doctrine has been a favourite argument in the armoury of almost every political party in India, and none has advocated it more strongly than the intellectuals of the Congress. When, therefore, the Congress Ministers took office, much was expected of them in the direction of reducing the burden on the poorer classes, and, perhaps, also increasing it on the richer ones. But what was the actual achievement of the Ministry in Bombay? It could be summed up briefly thus: What was attempted did not in all cases lead to this result and what could have led to it was not attempted. Coming to details:

(i) **Land Revenue:** The Congress Ministry was aware of the fact that the tax which was responsible for high incidence on the poor was the Land Tax. In his first budget speech the Hon'ble Mr. Latthe observed that "our first duty was to give relief by way of reduction of the state demand." He, however, admitted on the occasion of presenting the second budget in February 1938 that *ad hoc* reductions would lead to anomalies and that, therefore, the burden on the agriculturists could not be reduced except by means of some permanent reform in the system of land revenue assessment. The Government passed such a measure in 1939; we have reviewed it in detail in Appendix A. Here it contents us to observe that in spite of many desirable features, the Land Revenue Code (Amendment) Act (1939) is not calculated to reduce in any substantial measure the burden of the land tax. For, ac-

ording to that Act, the maximum pitch of assessment has been fixed at 35 per cent of the "rental value," a level which is rarely exceeded under the present assessment rates. This, however, does not mean that the incidence of land revenue is light. Rather, it means that in most tracts rental values are unduly inflated, a fact which was admitted by the Congress Revenue Minister, in the course of the discussions on the Tenancy Bill. In fact, one of the principal objects of the bill was to fix "fair rents" such as would be within the paying capacity of the tenant. The fixation, therefore, of 35 per cent of rental value, as the maximum height of assessment cannot afford any appreciable relief unless rack-renting is systematically prevented.

(ii) **Urban Property Taxation:** Another important revenue measure of the Congress Ministry was the Urban Immovable Property Tax introduced in the last budget of the Ministry. This tax represents an important attempt to "tax the untaxed" or, in other words, to increase the fiscal contribution on the part of the richer sections of the community. At the time of the passing of this measure, and even later, much opposition was encountered from the vested interests in the cities to which it applied. It was criticised as an encroachment on the municipal sphere of taxation. The real defect of the tax, however, is that its incidence is "sectional"; it falls on a particular class of property owners, viz., those who have real property in the cities of Bombay and Ahmedabad. The type of investment which the tax affects is one which least bears discouragement; for, the scarcity of housing accommodation in large towns is a matter which he who looks may read. Again, the difficulty of preventing the shifting and transfer of the tax to the poorer class of tenants has not been small.

(iii) Among other tax measures mention may be made of the sales tax on cloth and petrol. The sales tax was one of the proposals sponsored by Mr. Jamnadas Mehta when he was Finance Member in the Interim Ministry. The Congress Finance Member had at first scoffed at the proposal, but in 1939-40 he had to resort to this measure in order to make good the loss on account of prohibition. The Bombay Sales Tax Act of 1939 applied only to petrol and manufactured cloth (cotton and silk), but later the tax on cloth was abandoned due to administrative difficulties. The sales tax on petrol has been retained to this day and has been a fairly productive source of revenue. Yet, it is obvious that the Congress Ministry failed to make the best use of this form of taxation. The sales tax, indeed, is not an ideal fiscal device but



it is one which has large possibilities under Indian conditions. As is well-known, the tax of two main types, viz., general turnover tax levied on all sales, and a selective sales tax levied on sales of particular commodities. If care is taken in selecting commodities, such a tax could be applied extensively in our country for levying an indirect contribution from the richer sections of the community. A number of articles entering into the consumption of the comparatively well-to-do sections could be subjected to the sales tax. If the Ministry had been serious about "taxing the untaxed" this fiscal device could have been extended to a large variety of goods.

(iv) Other measures such as the enhancement of Electricity Duties, Stamp Duties and Court Fees, and the taxation of Prize Competitions cannot be regarded as important achievements in the fiscal field.

So much for the measures of tax reform undertaken by the Congress Ministry. What about those measures which were expected of the popular ministry, but which were either indefinitely postponed or never attempted?

(v) **Agricultural Income Tax:** In his first budget speech the Finance Minister had announced the intention of the Government to work out a plan of taxing the higher agricultural incomes so as to relieve the burden on the poorer agriculturists. In his second budget speech, however, he admitted that the proposed measure raised a number of difficulties, particularly in respect of the evil of fragmentation of holdings, due to which the plan had to be postponed. In the course of the next year and a half, little was heard of this salutary measure, except a brief reference in the budget speech in February 1939 to the effect that the question of introducing an agricultural income tax was being pursued steadily and that it was hoped that the Government would be in a position to place their conclusions before the House in the next session. It is not possible to know how far the planning of the measure had progressed by the time the Ministry resigned (October 1939), but one thing is clear, and that is that a measure which would have meant "taxing the untaxed" was not put on the statute book.

(vi) The proposal of taxing the alienated lands met with a similar fate. This occupied an important part in the financial policy outlined in September 1937. But here again legal and technical difficulties began to crop up as soon as concrete proposals were shaped. In the budget speech of 1939, it was announced that

“the Government have also been carefully investigating the question of reducing land revenue losses on alienated lands and villages and the expenditure on the cash grants which are being paid for various reasons. The total *nukshan* on these accounts amounts to nearly Rs. 72 lakhs a year and Government are at present engaged in considering the question from every point of view.... The potentialities of the two sources will depend upon the character of the Land Revenue legislation which we pass.” The subsequent Land Revenue Code (Amendment) Act, however, had little bearing on this question.

(vii) Another significant omission was the subject of inheritance taxation. In this connexion it appears that after the investigation by Sir Allan Lloyd, the Central Government made inquiries of the Provincial Governments in regard to the feasibility of inheritance taxes, but that most of the latter were lukewarm about it. It will be recalled that attempts at the taxation of inheritance were made twice during the Reform period, but that both failed as a result of the opposition in the Council. The Congress Ministry in Bombay should have explored this avenue of additional taxation but it was strangely silent on this subject.

All these omissions point to one conclusion, viz., that in no scheme of tax reform can one avoid increasing the burden on the richer classes. If one wants to avoid displeasing these classes, one had better not talk of “taxing the untaxed.”

§ 3. *Public Expenditure Under the Congress Ministry:* We have described in a previous section some of the schemes of the Con-

TABLE NO. 20

## EXPENDITURE ON SOCIAL SERVICES

(Source: Bombay Budget)

(In Lakhs of Rupees)

Expenditure Heads	1936-37	1939-40
Education	1,59.92	2,00.17
Medical	41.79	46.39
Public Health	22.50	28.10
Agriculture	13.76	11.99
Veterinary	3.90	4.41
Co-operation	6.08	15.76
Industry	6.57	7.65
<b>Total</b>	<b>25,46.08</b>	<b>3,14.47</b>

gress Ministry in the field of education and rural welfare. There is not a doubt that during the regime of the Congress Ministry expenditure on "Social Services" recorded a laudable increase. Thus, as compared with 1935-36, the expenditure on Education, Medical and Public Health, Agriculture, Co-operation and Industry, increased by nearly 25 per cent.

It appears, however, that while large sums were appropriated for diverse schemes of rural welfare such as improvement of village water-supply, improvement of rural medical facilities by subsidizing medical practitioners to settle in villages, road construction, prevention of soil erosion, dry farming experiments, etc., the administrative equipment for these schemes was imperfect. As a result, large portions of budgeted grants remained unspent. The following figures are available in the Appropriation Accounts for 1938-39 (p. 3):

TABLE NO. 21  
UNSPENT BUDGETED GRANTS ON SOCIAL SERVICES

	Charged on the Revenue of the Province	Voted by the Legislative Assembly	Total
<b>I. Authorised Expenditure</b>			
(a) Original Schedule	3,68,69,000	10,02,62,000	13,71,31,600
(b) First Supplementary Schedule	—	7,85,786	7,85,786
(c) Second Supplementary Schedule	15,83,514	60,32,295	76,15,809
	<u>3,84,52,514</u>	<u>10,70,80,681</u>	<u>14,55,33,195</u>
<b>II. Actual Expenditure</b>	3,76,05,684	10,00,45,982	13,76,51,666
<b>III. Less (-) Than Granted</b>	8,46,830	70,34,699	78,71,529
<b>IV. Percentage of III to I</b>	2.2	6.6	5.4

The principal "savings" on voted grants and charged appropriations were: (i) Rs. 14 lakhs under "Irrigation," due to "less expenditure on new minor irrigation works due to insufficiency of works ready for execution, absence of fixed programme for repairs and lack of adequately trained staff." (ii) Rs. 4 lakhs under "Public Health," due to "less expenditure on village water-supply and postponement of the scheme of health unit organization." (iii) Rs. 1.65 lakhs under "agriculture" due to "late starting of various schemes." (iv) Rs. 2.28 lakhs "Industries" due to "less expenditure on several industrial schemes and postponement of the scheme for the improvement of fishing methods." (v) The

Accountant General drew special attention to such cases where budget provisions had been made which could not be spent, or only partially spent, because the schemes were not complete in detail. We have already noted how in 1939-40 the Government created the "Development Fund" to meet the technical accounting difficulty presented by such unused appropriations. But such accounting devices were no solution of the real problem, which arose out of the lack of proper administrative machinery.

It would, however, be somewhat unfair to labour this point, since the Congress Ministry had a very short tenure of office, during which it was not possible to give effect to its expenditure programme in its completeness.

## CHAPTER XII

### WAR FINANCE

§ 1. *India's War Finance:* It is needless to say that India's economic and financial policy during war-time was controlled and directed by the Central Government. It is, however, worth noting that the Central Government's policy and its results have had important repercussions on Provincial finance. Indeed, it may be said that the basic financial problems which the Provinces had to face were largely the results of the Central Government's financial policy.

It is now a well-accepted fact that during the war-period the Central Government's expenditure on account of defence, as well as on account of the Allied purchases, greatly exceeded the receipts by way of taxes and loans; and that there thus developed an "inflationary gap," which induced an enormous expansion of currency by the Reserve Bank upon the backing of Sterling Securities.<sup>1</sup> This inflationary issue set in a spiral of rising prices, as indicated in Table No. 22.

TABLE NO. 22

#### INDEX NUMBERS OF WHOLESALE PRICES

(Economic Adviser's Index)

Month and Year	Index Number
August 1939	100.3
January 1940	133.2
July 1940	112.1
January 1941	114.8
July 1941	140.9
January 1942	145.0
July 1942	161.2
January 1943	195.6
July 1943	240.9
January 1944	236.9
July 1944	244.2
January 1945	250.3
July 1945	244.4
January 1946	250.2
March 1946	253.3

This inflationary finance has had important effects on the financial structure of Provincial governments. The rising price-

<sup>1</sup> For a detailed and critical account of India's War Finance, see "The War and Indian Economic Policy," by Gadgil and Sovani, 1944, Publication No. 10, Gokhale Institute of Politics and Economics.

level and increasing money incomes, as well as the additional taxes and enhanced tax-rates imposed by the Central Government, brought about an enormous increase in the Provincial revenues, such as the income-tax share, excise, stamps and forests. The Provinces, however, have not had to bear any significant part of the war expenditure, and therefore, the revenue increments resulted in large recurring surpluses, the disposal of which constituted the principal financial problem. The manner in which this problem arose in Bombay, and the policy which the Government pursued, are set forth in what follows.

§ 2. *Bombay's War Budgets:* In November 1939 the Congress Ministry resigned, and the Governor of Bombay assumed charge of the whole administration under Section 93 of the Government of India Act. The budgets during the subsequent years were authorized by the Governor.

(i) The first War budget of the Bombay Government (1940-41) authorized by the Governor showed a small revenue surplus, the estimates being as follows:

Revenue Receipts	Rs. 12,82.88 lakhs
Revenue Expenditure	Rs. 12,82.40 lakhs
Revenue Surplus	Rs. 0.48 lakh

These estimates provided for the continuance of the various schemes inaugurated by the Congress Ministry, including prohibition. For this purpose the Urban Immovable Property Tax, the Electricity Duty and the enhanced Stamp and Court-Fee Duties were extended for a year. The excise revenue was expected to be Rs. 1,57.33 lakhs, but the income-tax receipts were estimated at Rs. 60 lakhs.

(ii) When the second War budget (1941-42) was published in March 1942, several changes had taken place in the general economic and financial situation. The revised estimates for the year 1940-41 showed a very large increase in the revenue surplus (Rs. 1.03 lakhs), while the accounts showed a further increment (Rs. 1,87.48 lakhs). This was mainly due to improved receipts under Excise (Rs. 63.79), Other Taxes and Duties (Rs. 31.01 lakhs), Income-Tax (Rs. 23.20 lakhs), Stamps (Rs. 12.69 lakhs) and Land Revenue (Rs. 7.85 lakhs). Out of this surplus Rs. 1.00 lakhs were transferred to the Special Development Fund.

The Budget estimates for the year 1941-42 were:

Revenue Receipts	Rs. 13,56.65 lakhs
Revenue Expenditure	Rs. 13,56.00 lakhs
Revenue Surplus	Rs. 0.65 lakh

These estimates took into account the changes in the prohibition policy as a result of the High Court decision (July 1940), at which time the Government issued the following *Communique*: "The Government intends to devote any additional revenue from these changes to the relief of taxation under the Urban Property Tax, but it should not be assumed that any large relief will be possible, since the Government anticipates that these arrangements will mean the continued sacrifice of most of the revenue from the sale of country liquor and toddy." In accordance with this commitment, the rates of the Urban Property Tax were reduced by 20 per cent, involving a relief of Rs. 24 lakhs.

On the expenditure side there was an increased provision of Rs. 50 lakhs on social services including Education, Medical Relief, Public Health, Rural Development, etc. A beginning was made in the grant of dearness allowances to low-paid government servants. A three-year programme, involving a total cost of Rs. 1,38 lakhs, was chalked out, to be financed out of the Special Development Fund which had accumulated to Rs. 1,66 lakhs. The opening free balance of Rs. 1,11 lakhs was kept in reserve for contingencies arising out of war conditions.

(iii) The budget for 1942-43 revealed a considerably improved financial position with reference to the year 1941-42. The revised estimate for the latter year showed the revenue surplus to be Rs. 1,64.99 lakhs, while the accounts revealed it to be Rs. 2,61.01 lakhs, which included the additional amount of Rs. 1,00 lakhs transferred to the Special Development Fund. The increased receipts were chiefly under Provincial Excise (Rs. 64.86 lakhs), Land Revenue (Rs. 61.37 lakhs), Income-Tax (Rs. 58.60 lakhs), Stamps (Rs. 32.64 lakhs), Forest (Rs. 28.51 lakhs), and Other Taxes and Duties (Rs. 25.30 lakhs).

The revenue receipts for 1942-43 were estimated at Rs. 15,18.16 lakhs, and revenue expenditure at Rs. 15,17.18 lakhs. The additional revenue due to relaxation of prohibition measures was estimated at Rs. 28 lakhs, i.e., Rs. 4 lakhs more than that of the previous year. In view of this increase a slight reduction was effected in the rates of the Urban Property Tax. Financial provi-

sion of Rs. 70 lakhs was made for Air Raid Precautions and other war measures, while a Post-War Reconstruction Fund was started with a sum of Rs. 22.4 lakhs. The beneficent activities in several departments were continued, and the sum of Rs. 20 lakhs was transferred to the Special Development Fund.

(iv) The 1943-44 estimates were as follows:

Revenue Receipts	Rs. 17,69.20 lakhs
Revenue Expenditure	<u>Rs. 17,68.74 lakhs</u>
Revenue Surplus	Rs. - 0.46 lakh

This year's budget provided for the transfer of Rs. 60.53 lakhs to the Post-War Reconstruction Fund. It also provided Rs. 97 lakhs under different expenditure heads for meeting the extra cost due to enhanced dearness allowance rates. The "3 per cent Bombay Government Loan, 1955" floated in the year 1942-43 enabled the repayment of Rs. 3.50 lakhs consolidated debt bearing interest at  $4\frac{1}{2}$  per cent. This conversion operation meant a reduction of the equated instalments payable to the Central Government by Rs. 19.02 lakhs for the next 39 years; but for the next 13 years it necessitated a provision of Rs. 15.94 lakhs on account of interest and depreciation fund charges.

(v) The budget for 1944-45, like that of earlier years, revealed a great improvement in the financial position for the year 1943-45. While that year's budget had estimated a revenue surplus of Rs. 0.46 lakh, the revised estimate framed upon the actuals of the first eight months showed it to be Rs. 1,63.43 lakhs, exclusive of the transfer of Rs. 1.50 lakhs to the Special Development Fund, and of Rs. 1,10.53 lakhs to the Post-War Reconstruction Fund. The actuals for the year revealed a further improvement, the revenue surplus being Rs. 3,70.55 lakhs. The principal increases took place under the following revenue heads: Income-Tax (Rs. 1,48.00 lakhs), Excise (Rs. 2,47.71 lakhs), Stamps (Rs. 99.79 lakhs), Forest (Rs. 92.53 lakhs), Entertainment Tax (Rs. 86.33 lakhs), and Sales Tax on Petrol (Rs. 50.48 lakhs). Expenditure also increased under Forest (Rs. 36.04 lakhs), Jails and Convict Settlements (Rs. 30.45 lakhs), Police (Rs. 28.45 lakhs), Agriculture (Rs. 27.75 lakhs), Famine (Rs. 71.13 lakhs) and Civil Defence (Rs. 20.48 lakhs).

The estimates for 1944-45 provided for a revenue surplus of Rs. 0.86 lakhs. The revenue estimate (Rs. 24,89.56 lakhs) was based upon the continuance of all taxes at the 1943-44 rates, ex-



cepting the Urban Property Tax of which the rates were further reduced. This policy was justified as an anti-inflationary measure, while it was also based upon the consideration of making provision for post-war reconstruction schemes. With this latter end in view a sum of Rs. 4.5 crores was proposed to be transferred to the Post-War Reconstruction Fund. Financial provision was also made for a programme of agricultural development, including bunding schemes, irrigation works, "Grow More Food" campaign, etc.

While a nominal surplus (Rs. 0.86 lakhs) was assumed in the budget, the accounts revealed a surplus of Rs. 305.54 lakhs, the principle revenue betterments being Income-Tax (Rs. 57.40 lakhs), Land Revenue (Rs. 60.74 lakhs), Excise (Rs. 331.41 lakhs), Forest (Rs. 143.84 lakhs), Other Taxes and Duties (Rs. 170.40 lakhs) and Stamps (Rs. 32.01 lakhs). On the expenditure side two important items were Rs. 2,00 lakhs transferred to the Debt Redemption and Avoidance Fund, and an additional provision of Rs. 150 lakhs for the Special Development Fund. The real surplus, therefore, was of the order of Rs. 6,50 lakhs.

(vi) In March 1945 Bombay's sixth War budget was authorized by the Governor.

The budget estimates for the year 1945-46 were:

Revenue Receipts	Rs. 29,09.19 lakhs
Revenue Expenditure	Rs. 29,08.95 lakhs
Revenue Surplus	Rs. 0.24 lakh

The tax rates as they existed at the end of 1944-45 were continued, and this meant a departure in the case of the Urban Property Tax, since the circumstances under which it had been imposed no longer existed. The excise revenue had recovered and had increased beyond the pre-prohibition level, but now the Government decided to dissociate the levy of the Urban Property Tax from the original circumstances that had occasioned its imposition. In view of the vastly increased expenditure on social services and on war-time schemes, and in view of the necessity for providing for post-war programmes, this decision of the Government might be said to be wise. The Post-War Reconstruction Fund was this year increased by Rs. 4 crores, bringing it to Rs. 11 crores. Large sums were appropriated for the Bombay Milk Scheme (Rs. 60 lakhs), the Bunding and Dry Farming Scheme in Bijapur (Rs. 75 lakhs), Irrigation Works (Rs. 29 lakhs), and for the purchase of ground-

nut cake and bone-meal manure for distribution among cultivators (Rs. 58 lakhs). Dearness Allowances required a provision of Rs. 1.25 lakhs, and a sum of Rs. 2 crores was transferred to the newly created Debt Redemption and Avoidance Fund.

The revised estimate for 1945-46 (as revealed in the budget for 1946-47) showed a surplus of Rs. 30.97 lakhs.

(vii) The estimates for the year 1946-47 are:

Revenue Receipts	Rs. 30,19.87 lakhs
Revenue Expenditure	Rs. 30,14.73 lakhs
Revenue Surplus	Rs. 5.14 lakhs

The revenue estimate assumes the continuance of all the taxes and fees, and it includes (i) the Sales Tax (Rs. 82.50 lakhs), and the extension of the Urban Immovable Property Tax to Poona (Rs. 4 lakhs). The income-tax receipts are estimated to be less than those of 1945-46 by Rs. 61 lakhs, while excise and forest are also expected to be diminished by a crore and 78 lakhs of rupees respectively. Rs. 2.25 crores have been transferred to the Post-War Reconstruction Fund, which will be Rs. 13.25 crores at the end of the year. Out of this Fund Rs. 1.33 lakhs have been provided for reconstruction schemes in 1946-47, but it is pointed out that larger provisions may have to be made in the course of the year on schemes of re-employment and food procurement. A sum of Rs. 1.30 lakhs has been provided for the Milk Supply Schemes in Bombay and Poona, while Rs. 78 lakhs have been allotted for the Dry Farming Scheme in Bijapur, and Rs. 62 lakhs for the distribution of ground-nut cake and bone-meal manure. The Debt Redemption Fund has been assigned a further sum of Rs. 2 crores, bringing it to Rs. 6 crores. The Dearness and War Allowances are estimated at Rs. 2.62 lakhs for the year. Additional provisions have also been made in respect of Education, Medical, Public Health, Agriculture, and other nation-building departments.

§ 3. *Review of Bombay's War Finance:* Bombay's war finance was dominated by one central fact, viz., large recurring surpluses arising out of expanding revenue. The surpluses were not generated by deliberate policy in the sphere of taxation; they were, rather, the outcome of certain fortuitous circumstances created by the war. In fact, it could even be said that the Provincial surpluses were due, in a large measure, to the Central Government's financial policy.

We have already indicated the nature of India's financial problem during war-time, and the way in which it was handled by the Central Government. We have seen how there developed in Central finance an "inflationary gap" which led to the expansion of note issue and a spiral of rising prices. This inflationary finance at the Centre was responsible for an enormous increase in Bombay's revenue receipts under the following important heads:

(i) **Income-Tax:** As a result of the enhanced Income-Tax rates, and the imposition of the Excess Profit Tax, the total receipts by way of income-tax share increased by leaps and bounds, as shown in Table No. 23.

TABLE NO. 23

## BOMBAY GOVERNMENT'S SHARE OF TAXES ON INCOME

(In Lakhs of Rupees)

1939-40	1940-41	1941-42	1942-43	1943-44	1944-45	1945-46 (Revised)	1946-47 (Budget)
55.80	83.20	147.80	218.00	390.00	531.20	454.00	392.80

It will thus be seen the Province has been getting unexpectedly large sums under this head, which, today, has become one of the most important sources of revenue, next only to excise. It is obvious that these windfalls have been the outcome of Central tax policy in the sphere of direct taxation; but it must be noted that the Central Government's income-tax receipts have increased largely as a result of rise of prices and the consequent expansion of money incomes in most spheres of economic life.

(ii) During the war period excise revenue also registered a marked increase. When the Congress prohibition programme was in full swing, the excise revenue was expected to fall by nearly Rs. 1.5 crores. The budget for 1939-40 estimated the excise revenue at Rs. 2,87.10 lakhs, but this figure did not include the expected loss of Rs. 1,50 lakhs on account of prohibition measures which were to be introduced in that year. The Finance Member expected the receipts from excise to be about Rs. 1,40 lakhs for the year 1939-40; the actuals, however, revealed them to be Rs. 2,02.13 lakhs. In the Governor's first budget (1940-41) allowance was made for the decline of the excise revenue due to prohibition. But in the course of the year, the prohibition measures had to be modified as a result of the High Court decision,

leading to a relaxation of restrictions on the purchase and possession of foreign liquor. Excise revenue, since then, has been on the increase, although the prohibition policy was continued. The excise receipts exceeded the pre-prohibition level in 1942-43 (Rs. 3,75.25 lakhs), and they reached the record figure of Rs. 7,55.90 lakhs in 1944-45. The budget estimate for 1946-47 is Rs. 6,52.67 lakhs. The increase has been due to a variety of causes, mainly, increased purchasing power, reduced imports of foreign liquors, high army demand, etc.

(iii) Revenue from stamps increased by a little more than a crore of rupees during the war period. In the accounts of 1939-40 the receipts were Rs. 1,44.36 lakhs; in the revised estimate for 1945-46 they have been shown at Rs. 2,57.00 lakhs; and in the budget estimates for 1946-47 the figure is Rs. 2,49.28 lakhs. This has been largely due to the "increased volume of business and more numerous transactions in regard to purchase and sale of properties, transfer of shares and execution of contractual obligations."<sup>1</sup> This, again, has been the outcome of inflation, which gathered strength during the year 1942-43. The increase in receipts after 1943 has been also due to the enhanced rates made applicable under the Bombay Act No. XIV of 1943.

(iv) Due to war conditions the forest revenue also increased enormously, especially after 1942-43. In the pre-war years forests yielded Rs. 38.61 lakhs; the receipts went up to Rs. 69.76 lakhs in 1941-42; but in subsequent years there took place a phenomenal increase in revenue mainly as a result of war demand and high prices of forest produce, particularly timber. The actuals for the year 1944-45 were Rs. 3,13.81 lakhs; while the revised estimate for 1945-46 is Rs. 2,29.43 lakhs. In the budget for 1946-47 the estimated revenue is Rs. 1,51.07 lakhs, the fall being obviously due to the diminution of war demand.

It must, however, be noted that the expenditure on the forest department also registered a large increase, chiefly under "conservancy and works."

(v) Another revenue source of which the yield has increased in a marked degree has been "Other Taxes and Duties," including taxes on luxuries, entertainments, amusements, betting and gambling. As a result of increased purchasing power especially in urban areas, the receipts under this head increased from Rs. 26.40 lakhs (1939-40) to Rs. 48.53 lakhs (1942-43); then there took

<sup>1</sup> Budget Memorandum, 1944-45, p. 22.

place a marked rise, the figure for 1944-45 (accounts) being Rs. 4,90.55 lakhs. The budget estimate for 1946-47 is placed at Rs. 4,88.78 lakhs. The increased revenue has also been due to enhancements of rates in regard to these taxes.

From the foregoing account it is clear that a very large part of the above revenue heads has been the result of war conditions, and particularly of the inflationary price trends and increasing money incomes. The general effect on the total revenue position is indicated by the figures in Table No. 24.

-TABLE NO. 24

SHOWING TOTAL REVENUE RECEIPTS IN 1939-40, 1942-43,  
1945-46 AND 1946-47

(Source: Bombay Budgets, 1945-46 and 1946-47)

(In Lakhs of Rupees)

1939-40	1942-43	1944-45 Accounts	1945-46 Revised	1946-47 Budget
12,49.59	19,70.31	33,66.80	32,49.69	30,19.87

Let us now examine the policy which the Government pursued in connexion with this fortuitous revenue increment, and the consequent recurring surpluses. For this purpose it will be convenient to divide the period into two parts, viz., (i) from November 1939 to March 1942; (ii) from April 1942 up to March 1946.

The first period did not give rise to any large problems of financial and economic policy. During these two-and-a-half years, the Government's budgetary position had improved to a certain extent owing to the increased receipts under income-tax and excise. The Government's policy was to maintain steady progress in all the nation-building departments and to prepare themselves for financial contingencies arising out of the war. In pursuance of this policy, the Government steadily increased the provisions under education, medical, public health, agriculture, veterinary, co-operation, and industries. It is not necessary to describe the various measures undertaken in these branches.\*

At the same time the Bombay Government made provision for further development expenditure by transferring to the Special

\* The official publication "Bombay's Progress—1939-42" gives a detailed account of all these measures.

Development Fund Rs. 25 lakhs in 1939-40, Rs. 1,00 lakhs in 1940-41, and Rs. 1,27 lakhs in 1941-42. Besides, the opening balance of Rs. 1,11 lakhs (1941-42) was kept in reserve "to meet any unknown contingencies arising out of war conditions."<sup>2</sup>

Difficult problems of financial and economic policy arose during the second period beginning from April 1942. This period is characterized by a rapidly rising price-level. There accrued, as detailed previously, embarrassing surpluses in the Provincial budgets. At the same time the Government was faced with difficult administrative problems in the field of civil defence, food-supply and price control.

The general financial policy during these years was based upon four main considerations laid down in the budgets for 1942-43 and 1943-44. These were: (i) "It is essential that there should be no lack of financial provision for 'war measures' falling within the Provincial sphere, in particular for measures connected with Civil Defence, and the maintenance of internal security, and law and order. (ii) Subject to the foregoing consideration, and within the limitations imposed by the need to give priority to war demands on personnel and material, there should be no curtailment of expenditure on the 'nation-building' activities of the Government; in particular, schemes of rural development. (iii) A beginning should be made in the building up of sufficient provision for meeting post-war needs and problems. (iv) Substantial additions to the recurring liabilities of the Province should not be made merely on account of increase of revenue due to temporary and fortuitous causes."<sup>3</sup> (v) Inflation must be countered.<sup>4</sup>

None can take exception to the above considerations which underlay the Government's financial policy during the war period. The actual achievement also came very close to the general principles laid down here, except in a few cases. The following points may be noted in this connexion:

(i) A consistent policy was pursued in respect of making provision for post-war needs. In 1942-43 the Government created the "Post-War Reconstruction Fund" and set aside in the budget for that year a sum of Rs. 22.4 lakhs for the purpose. The purposes of the Fund were thus explained in the Budget for 1942-43: "It is certain that many matters will arise after the war requiring

<sup>2</sup> H. E. the Governor's Statement on the Provincial Budget for 1941-42.

<sup>3</sup> Introductory Note to the Budget Memorandum, 1942-43, p. vi.

<sup>4</sup> Introductory Note to the Budget Memorandum, 1944-45, p. vi.

the urgent provision of money which the Province may be unable to provide from its annual revenue. It would be premature to attempt to define these problems at this stage. Resumption of building schemes of Government held up during the war for lack of steel, replantation of forests the exploitation of which has been accelerated by war demands, and, possibly, an economic programme to meet the situation caused by the release of skilled labour and the demobilization of Indian soldiers, are a few illustrations of the objects for which the Post-War Reconstruction Fund may be eventually used."° In subsequent years fairly large transfers were made to the Fund which, by the end of 1946-47, is expected to be Rs. 13.25 crores. Besides, Rs. 6 crores have been transferred to the Debt Redemption and Avoidance Fund created in 1943-44. The building up of such reserves out of fortuitous recurrent surplus has been a policy of financial prudence. It might also be regarded as a counter-inflationary measure on a small scale.

(ii) At this stage it may be pertinent to discuss whether it would not have been better to have given tax relief out of the recurrent surpluses. It should be clear, however, that such a policy would not have been appropriate during the period under review. Reduction in general tax levels would have had an inflationary effect, and hence such a policy would have been inconsistent with the general aims of war finance. The Government afforded some measure of relief in the case of the Urban Property Tax in accordance with their commitment already referred to above. The rates of this tax were gradually reduced as the excise revenue recovered, but in 1945-46 this policy was abandoned and the tax was retained although the circumstances under which it was imposed no longer existed. On the whole this was a wise decision, considering the general aims of war finance on an inflationary background.

Now, the only tax in the case of which relief has been needed in the past is the land revenue. Here also, it is obvious that a fair measure of relief has already been obtained automatically as a result of rising prices and increasing farm incomes, though it must be admitted that this relief has not been uniformly distributed over the different agricultural classes. Even granting that relief was called for, it would appear that it would have been impossible to grant it systematically and scientifically so as to reach those classes which really deserved it. We have already referred to the difficulty experienced by the Congress Ministry in this re-

° Budget Memorandum, 1942-43, p. IX.

gard. The fact is that reduction of land revenue assessment cannot be accomplished by *ad hoc* measures; it raises larger issues connected with the permanent modification of the whole system of Land Revenue Settlement and Revision. We, therefore, conclude that tax relief as an alternative to building up financial reserves would not have been proper from the point of view of general policy, and would not have been easy from the point of view of administration.

(iii) It is worthy of note that increasing provision has been made during the war-period for "nation-building" departments, as the figures in Table No. 25 show.

TABLE NO. 25

## SHOWING EXPENDITURE ON "NATION-BUILDING" DEPARTMENTS DURING 1940-41 TO 1946-47 (BUDGET)

(Source: Bombay Budgets)

	1940-41	1941-42	1942-43	1943-44	1944-45	1945-46 Revised	1946-47 Budget
1. Education	193.30	206.75	209.31	219.30	237.72	276.42	293.67
2. Medical and Public Health	82.56	87.81	98.66	112.89	136.53	162.60	173.50
3. Minor Irrigation Works	8.39	9.42	8.00	6.00	6.16	32.29	38.64
4. Agriculture, Veterinary, Co-operation, and Rural Development	34.38	45.51	52.09	75.45	139.19	224.15	231.64
5. Industries	6.96	8.80	9.40	13.94	14.64	20.64	32.92
6. Miscellaneous (Milk Supply Schemes)	—	—	—	—	—	—	—

A part of the increased expenditure is attributable to dearness and war-allowances and to additional establishments, but even taking account of these, there has been a net progressive increase in the expenditure on the social services. Thus, in education, the grants to Local authorities for primary education were increased from Rs. 130.81 lakhs in 1939-40 to Rs. 223 lakhs in 1946-47. The question of pay and allowances of primary teachers was examined in 1939 by a Committee consisting of Mr. S. N. Moos, Director of Public Instruction and Mr. M. R. Paranjpe, upon whose recommendation the Government sanctioned the basic scale of Rs. 25-1/2-30-1-40 for trained teachers appointed and trained after 1935. A further rise has also been sanctioned with effect from April 1946. It is clear, however, that this whole question will have to be thoroughly examined afresh in view of the



increased cost of living during the war period. The question is linked up with the larger problem of financing primary education within the means available for the purpose.

In the Medical and Public Health Departments, a number of small schemes have been provided for. Fairly large increments have also been made in provisions for the departments covering Agriculture, Veterinary, Co-operation and Rural Development. Agricultural research and propaganda, "Grow More Food" campaign, provision of better seeds, bunding and dry farming schemes, anti-erosion measures, and a variety of other projects have been financed out of departmental grants, Special Development Fund, and grants from outside bodies, such as the Imperial Council of Agricultural Research, Sir Sassoon David Trust Fund, the Indian Central Cotton Committee, Sir Cusrow Wadia Trust Fund, etc. Mention must also be made of the Milk Supply Schemes in Bombay and Poona on which fairly large sums have been spent since 1944-45.

(a) Provisions directly and indirectly necessitated by war conditions include those connected with Civil Defence (particularly A. R. P. measures), recruiting, police, dearness allowances, food-administration and price control. Two of these need a somewhat detailed examination.

(b) Dearness Allowances: Provision for the payment of dearness allowances was first made in the budget for 1941-42, when the rates sanctioned were Rs. 2 for all employees getting less than Rs. 40 a month in Bombay and less than Rs. 30 in the mofussil. The extra burden was estimated at Rs. 11 lakhs a year. In 1943-44 these rates were increased to Rs. 9 and Rs. 7 respectively; dearness allowances at the rates of Rs. 11 and Rs. 9 were sanctioned for servants getting Rs. 120 in Bombay and Rs. 90 in the mofussil, respectively. As a result of these increments, the estimated extra cost was nearly Rs. 87 lakhs. This included also the additional grants to Local authorities adopting similar schemes of dearness allowance for their own employees. Subsequently, the rates of dearness and war allowances have been raised, and it has been estimated in the budget for 1946-47 that the total charge on this account is about Rs. 2,62 lakhs including grants-in-aid to local bodies.

(c) The problems of food supply, price control and rationing within the Province led to certain significant developments in the field of economic administration and finance during the war

period. Bombay being a deficit area in respect of food grains, the policy of price control necessitated strict measures against hoarding and profiteering, and required an early introduction of rationing and Government supply of grains at controlled prices. "Cheap grain shops" were started early in 1940, and for this Government purchase of certain food grains became necessary. In course of time, however, it was realized that policy should be directed towards the production of larger quantities of food grains within the Province, by diverting acreage from commercial to food crops, and by increasing the general productivity of land devoted to food production. Again, in order to ensure the proper distribution of foodstuffs among the people, food rationing became necessary. This naturally involved government procurement of foodstuffs through compulsory purchase or levy. All these developments in food policy ultimately meant a large extension of Government activity in the field of production and distribution of food grains, and consequently, large encroachment of the Government in the sphere of private trading. Such measures have resulted in a significant expansion in public expenditure, which, there is some reason to believe, could be continued with profit during the period of post-war reconstruction. The foregoing developments are indicated in some detail in what follows:

It is a matter of common knowledge that Bombay is a deficit Province in respect of food grains, and that it has to depend upon imports from other Provinces to balance its food-budget. With the loss of Burma, and the imposition of export bans by other Provinces, Bombay's food position became precarious and it called for a well-thought-out policy directed towards securing imports as well as increasing Provincial production of food grains. When the Central Government initiated the "Grow More Food" campaign in 1940-41, the Government of Bombay readily adopted it and offered facilities to cultivators in order to induce them to increase food production. Interest-free loans for the purchase of seed, loans on easy terms for the construction and repairs of wells and other land improvements, transport priorities in respect of food grains, distribution of improved varieties of seeds, reduction of irrigation rates, distribution of groundnut cake, etc., have been some of the inducements offered in this connexion. Extensive propaganda through the distribution of leaflets, village meetings, posters, etc., was also carried on to popularize these facilities. It was thought that such measures would increase food-crop production by diverting cultivation from non-food to food-crops, and by causing an extension of cultivation of waste lands

hitherto lying uncultivated. As a result of the campaign, there took place some substitution of non-food crops by food-crops during 1941-43, but in 1943-44 it was realized that propaganda work in this direction had reached the limits of its achievement, and that for bringing about further substitution, legislation had become necessary. In view of this the Bombay Growth of Food-Crops Act was passed in May, 1944, under which it has been provided that "in any specified area every cultivator shall grow scheduled food-crops in such area of his holding in the twelve months immediately following the date of the order as bears to the total area of his holding a proportion not less than that which the area of such crops grown by him in the twelve months previous to the date of the order bore to the total area of his then holding." It is further provided that "if the Provincial Government is satisfied that it is necessary in the interests of the Province to increase the production of food-crops in any local area," it may, by an order, prescribe the minimum proportion of a holding on which food-crops shall be grown, and the maximum proportion of the holding on which non-food-crops may be grown. The Act also made provision for the fixation and guarantee of prices of food-crops grown by the cultivators under the orders, and it also gave powers to the Provincial Government to reduce land revenue or irrigation dues in respect of such lands. By an amendment of the Act it has been provided that rent payable by tenants of lands on which food-crops are compulsorily grown may be fixed by Mamlatdars after taking into account such factors as rental values of similar lands growing food-crops in the locality, their local prices, the Government assessment, etc.

This Act has been followed by the Bombay Irrigated Crops Regulation Act, 1944. Its object is to secure the maximum production food-grains on irrigated lands, most of which are devoted to heavy commercial crops like sugarcane. Under this Act, the Commissioners are empowered to prepare schemes for the compulsory growing of food-crops on irrigated lands, and in the event of non-compliance for their forfeiture by Government.

In the meantime, rationing has been introduced in a large number of areas, and in view of the deficit position of the Province in respect of most of the rationed articles, it has become necessary to make arrangements for compulsory procurement of food-grains in order to meet at least a part of the requirements of the rationed areas. Compulsory procurement was initiated in March 1944, through the "Grain Levy Scheme" applied to the

three districts of Sholapur, Bijapur and Ahmednagar. Under this original scheme the cultivators of food-crops were required to sell a proportion of their produce to the Government at fixed prices, the proportion of the "levy" being determined with reference to the land revenue assessment. After six months' experience, a revised Grain Levy Scheme was prepared and made applicable to all parts of the Province except the districts of South Kanara, Ratnagiri, Kolaba, Thana, Bombay Suburban, and the purely rice-producing areas. The revised levy demand has been based primarily upon food-crops acreage, the assessment being considered as one of the factors. It applies to the main cereal crops—wheat, rice, bajri, jowar, and ragi, their prices being fixed by the Government for delivery at the godown. Exemption limits have been fixed for the several grains in accordance with local conditions and consumption habits. In the rice-growing tracts where the compulsory levy is not applied, the Government has made arrangements for voluntary purchase of paddy on a monopoly basis.

The following figures show the results of the grain purchase monopoly and procurement scheme in the Province:

Total Production of All Cereals 1943-44	Total Purchases in 1943-44	Percentage of 2 to 1	Total Production in 1944-45	Total Purchases in 1944-45	Percentage of 5 to 4
1	2	3	4	5	6
Tons	Tons		Tons	Tons	
36,20,480	5,08,214	14.0	30,14,070	6,30,116	20.8

Procurements for the season 1945-46 have been on a much larger scale. Total purchases up to October 1945 were nearly 830,262 tons.

This is not the place to discuss in detail the administrative aspects of the foregoing measures, viz., the "Grow More Food" campaign, rationing, compulsory procurement and monopoly purchases of food-grains. For the present discussion the significance of all these developments is that they have led to a very large extension of Government activity in the sphere of production and distribution of foodstuffs and other rationed articles, and the consequent encroachment of the Government in the field of private trading. Reference may also be made in this connexion, to the

Miscellaneous	1.5
Available for Schemes the Cost of Which Remains to Be Worked Out	11.0
Total	60.0

Out of this sum of Rs. 60 crores, Rs. 50 crores represent non-recurring expenditure, and the rest recurring. The latter is estimated to be spread over as follows:

	Crores of Rupees
1st Year	1.50
2nd Year	1.75
3rd Year	2.00
4th Year	2.25
5th Year	2.50
Total	10.00

The financing of this programme is based upon the following: (i) it is expected that about Rs. 20 crores will be available from the Central Government by way of a subvention; (ii) the post-war reconstruction fund is estimated to reach Rs. 15 crores at the commencement of the first five-year period, i.e. in 1947-48; (iii) during the first five-year period budget surplus is expected to total Rs. 10 crores; (iv) the remaining Rs. 15 crores may be met by additional taxation or by borrowing, or both. If the whole amount is borrowed, the recurrent interest charges are estimated at Rs. 1 crore a year.

As regards the financing of the second and third five-year periods, the Government do not think it necessary or practicable to set forth detailed proposals. They observe, however, that the plans will necessitate some additional taxation, which might well take the form of a sales tax.

§ 3. *The Basis of Financial Reform:* It is not necessary to enter into a detailed discussion about the reconstruction plans and their financing described above. It is obvious that the popular ministry, when it assumes the reins of Government, will find it necessary to modify these proposals, and to work out new ones in the light of their own economic and financial objectives. At this stage, therefore, it contents us merely to indicate some of the uncertainties which inhere in the immediate future, and some of the basic factors in the context of which the financial programme will have to be planned.

(i) It is obvious, in the first place, that financial planning is bound up with the uncertainty inherent in the future consti-

tutional settlement. The nature of the federation, the political boundaries of the Provinces, the division of powers and functions between the federal and Provincial governments,—are matters regarding which it would be wise not to say anything at present. There is, however, one aspect of the future constitutional settlement on which the present study has an important bearing, viz., the division of revenue heads as between the Federal and the Provincial governments. Ever since the Meston Settlement, the Provinces have been handicapped by the maladjustment between expanding activities and inelastic revenues. Since 1936-37, this maladjustment has been to a certain extent corrected by the increasing receipts from the income-tax. Today, the position in most Provinces, and particularly in Bombay, is that financial stability and expansion have come to depend to a large extent on income-tax receipts. It seems, therefore, that if Provinces are to launch programmes of economic development, they should be assured of expanding revenues arising out of the taxable income within their own borders. The arguments in favour of distributing the proceeds of the income-tax according to origin or residence have gained strength in view of the present and prospective programmes of economic planning, and hence, it would be a policy of wisdom to provincialize almost the whole of the income-tax proceeds, the powers of legislation being, of course, retained by the Federation.

(ii) When the larger question of powers and resources is settled, the Provincial Government will have to address itself to certain financial reforms regarding taxation, expenditure, and budgeting, within its own sphere. In the field of taxation, the reconstruction programme must inevitably involve certain necessary additions and readjustments based upon the principle of fiscal justice. For this purpose it would be proper to start with certain provisional assumptions regarding the incidence of taxation, or the distribution of fiscal burden, among the several productive classes and income groups. It must, of course, be realized that a comprehensive examination of incidence must proceed upon an all-India basis, including within its sphere Central, Provincial and local taxation. In the absence of fuller inquiry, it would not be improper to work upon tentative results which could be obtained with the help of a general analysis of incidence before and during the war.

In the pre-war situation, the general analysis regarding the distribution of fiscal burden among the different productive groups made by the Indian Taxation Inquiry Committee in 1926 was

broadly true. Modifying it in the light of the subsequent changes, we may say that before the war, (a) the tax-burden on the "poor classes" (including agricultural and industrial labourers, small-scale farmers, petty artisans, and the low-grade salariat) was fairly high relatively to their income, as these classes had to bear the burden of excise duties, certain customs duties (e.g., on cloth and sugar) and land revenue (in the case of farmers); (b) in the middle class, certain classes were lightly taxed, e.g., the traders and landlords; (c) in the upper-sections, the substantial landholding classes escaped lightly, as compared with the professional classes, merchants and industrialists. This whole income group, however, was lightly taxed in comparison with similar income groups in other countries.

During the war there has been a large increase in the total tax burden, as well as significant changes in incidence. The higher income groups have borne the increments in direct taxation, but in most cases, their incomes have also expanded enormously as a result of war-time inflation. The enhancement of customs duties and excises has affected almost all classes, but it is not possible to say, in the absence of a detailed inquiry into the expenditure patterns of the different classes, how their burden has been distributed. The agricultural classes have had their burden lightened as a result of the rise in the prices of agricultural products, but the subsistence farmer has not gained in any significant measure. The general rise of prices, indeed, may be regarded as a regressive tax on all income groups, of which the pressure has been very severe on the fixed-salary earners in Government and non-Government employment, in whose case the war-allowances have not been in proportion to the rise in the cost of living.

In the light of the foregoing tentative analysis, regarding the incidence of taxation, we may conclude that in the post-war period, readjustments should be effected in such a way as to increase the tax-contributions from the high-income groups in industry and trade, the middle-class traders operating in towns and cities, and the substantial landlords. For this purpose the following tax-measures are worth exploring:

(a) A tax on agricultural incomes with an exemption limit of say, Rs. 500.

(b) A Sales Tax. A proposal for the levy of a turnover tax for financing post-war reconstruction schemes has already been made by the Government. It is proposed to exempt dealers whose

gross turnover is less than Rs. 10,000 per year. Exemptions are also to be given in respect of the sales of foodstuffs, kerosene, matches, motor spirit, cheap cloth, etc. The rate of the tax is  $\frac{1}{2}$  anna in the rupee, or a little over 3 per cent. It is also provided that the tax will be levied on sales to the virtual consumers, and not on those which represent intermediate stages. Possibly this proposal may have to be modified in certain respects to suit the convenience of the tax-payers affected, but on general considerations, it appears to be a desirable measure, worth putting on the statute book.

(c) Inheritance Taxes, including Estate Duties and Succession Duties on non-agricultural property. These come within the sphere of Central legislation, and it is gratifying to note that a bill providing for the levy of an Estate Duty has already been introduced in the Central Legislature. The proceeds of the duty are to be distributed among the Provinces in a manner to be determined by another Central Act.

(iii) In the field of expenditure, it is obvious the reconstruction programme will mean enormous outlays of a recurrent and non-recurrent character. It is fairly certain that Provincial outlays will, in the future, be subsidized by Central subventions, while the Provincial revenues will have to meet some of the demands on the part of local authorities.

Besides the aforementioned expenditure schemes, the post-war period may well witness significant developments in a direction already indicated in our study of war finance. We have noted how the problem of food-supply and price-control necessitated large extensions of Government activity in the field of production and distribution of food-grains through procurement and rationing schemes. They have opened out a vast field for Government activity in the sphere of social and economic welfare, and there is a strong case for their continuance and extension even in peacetime. The existing machinery might be employed for the purpose of stabilization of farm prices so as to maintain a fair level profitably for agricultural operations. Again, compulsory procurement, rationing and price-control may be used for the purpose of subsidizing the consumption of foodstuffs in the case of certain sections of the population, as is done today on a small scale in rural areas. Possibly, a certain element of taxation could be incorporated in the machinery by charging higher prices in urban areas, so as to reduce the inequality of the fiscal burden as be-



tween the towns and the countryside. Lastly, all these schemes when organized on a permanent basis, would tend to eliminate the element of profiteering in a section of private trading which touches most intimately the welfare of the masses. In all these ways, the Government of Bombay may well take the lead in a field of welfare activity which at present lies unexplored.

(iv) One final consideration now remains to be set forth. The programme of economic development already announced covers fifteen years, divided into three five-year budgetary periods. Whatever the modifications in respect of objectives and details which the programme might undergo at the hands of the popular ministry, it will necessarily imply a significant change in budgetary technique. The programme of planned development will render annual budget estimates of revenue receipts and expenditure less significant, if not quite meaningless. Planning will mean a continuity of the expenditure programme for a period of five years or more, and it will be the objective of the financial authorities to balance the receipts and outlays, not annually, but over a "budgetary period" as a whole.

The principle of annual budget balancing has already suffered a good deal at the hands of economic theorists and planners, who have set forth the doctrine of "long-period budgeting" with reference to the trade cycle. It is a commonplace that public revenues, such as the income-tax, customs, excise, etc., exhibit a pronounced sensitivity to the trade cycle. During the "prosperity phase" of the cycle, when prices, production and employment are on the up-swing, the revenues expand automatically, and since public expenditure is to a large extent statutory and rigid, budget surpluses tend to accrue; contrariwise, in a depression period, tax-income as well as non-tax revenues decline, and produce "unbalanced budgets." In view of this, the theory of "deficit financing" and "trade-cycle budgeting" has been advanced by several theorists and practical planners. The idea is that instead of balancing the public account annually, deficit budgeting should be adopted in the depression period so as to avoid the deflationary effect of retrenchment. The accumulated deficits should later be wiped out by budget surpluses accruing in the recovery period and the prosperity phase.<sup>2</sup> There are, indeed, several practical difficulties connected with such long-period budgeting, but it is an inevitable concomitant of economic planning, whether it is di-

<sup>2</sup> For a somewhat fuller discussion of this theory, reference may be made to the present writer's article, "The Nature and Characteristics of a Budget" (Bombay University Journal, July 1940).

rected towards smoothing out the cyclical fluctuations, or towards general economic reconstruction.

It will be recalled that during the depression of the thirties, the Central and Provincial Governments in India pursued ruthlessly the policy of annual budget balancing, and effected large temporary retrenchments in expenditure and imposed additional taxation. It is needless to say that the problem of "depression finance" was more acutely felt in the Central than in the Provincial sphere, owing to the fact that the Central revenues such as the income-tax, the customs, and the excises, exhibited a greater degree of cycle-sensitivity. In the Provincial sphere, however, the problem was by no means insignificant; we have seen that Bombay's revenues suffered by about Rs. 2 crores in the depth of the depression. Now that the income-tax forms an important source of Provincial revenue, the cycle-sensitivity of the revenue structure has been augmented. Indeed, with the exception of land revenue, most of the Provincial sources—income-tax share, excise, forests, stamps, scheduled taxes, etc.—are to a large extent dependent upon the price and income fluctuations.

What has been said above is sufficient to make out a case for long-period budgeting. The case is reinforced by the financial necessities implied in the programme of planned development.

## APPENDICES

- Appendix A:* A Note on the Development of the Land Revenue System in the Province of Bombay.
- Appendix B:* A Note on Indian Excise Policy, with special reference to Excise Administration and Policy in the Province of Bombay.

## APPENDIX A

### THE BOMBAY LAND REVENUE SYSTEM

§ 1. *Introductory:* Land Revenue has been the most important source of Provincial finance since 1921. It contributed nearly 30 per cent of the Provincial revenue during the Reform period; and though its relative importance has diminished under Provincial Autonomy, it still remains one of the mainstays of Bombay's revenue structure. The basis of this tax, its assessment and revision have been the subject of fierce controversies in the past; even today they constitute a fiscal problem of the first magnitude. It would not, therefore, be out of place to give a somewhat detailed history of the development of the Land Revenue System in Bombay along with a description of its technique. The legislative attempts to modify the system during the last few years will also be treated in some fulness.

The Bombay land system is based upon the *ryotwari* principle under which the Government fixes the land revenue with each individual occupant, whose rights are hereditary and transferable, subject to the payment of the Government assessment. The relationship between the Government and the occupant of land is legally a tenure, commonly called the "survey tenure." Though, however, the major portion of the land in the Province comes under survey tenure, there are large tracts where the Government has "alienated" its right of collecting assessment in favour of certain persons and religious institutions. Such "alienated" lands came into existence as a result of *inams* or gifts for personal or political service. In the early years of British rule in this Province, claims for such *inams* were made by numerous persons. The Government, therefore, ordered an official inquiry in 1841, and later, in 1852, appointed the Inam Commission to investigate these claims. As a result of its findings, four types of Inams were recognised—viz., (i) Personal; (ii) Devasthan (Religious Institutions); (iii) Hereditary Service; and (iv) Political. The holders of such *inam* lands—the Inamdars and Sardars—constitute a class of landlords who pay a nominal or "quit rent" (*Judi*) to the Government. Again, there are certain estates in Gujerat and Konkan in whose case hereditary ownership has been recognised by the Government in certain classes, such as the Talukdars and Khots. In this way a variety of tenures has sprung up in these parts, involving tenancy problems of great difficulty.

For the present, we are not concerned with the Inam Tenures or the Taluqdari and Khoti tenures described above. Our present task is to describe the direct relationship between the Government and the occupant, on which the land revenue system rests.

§ 2. *Historical Survey of the Bombay Land Revenue System:* The Ryotwari System of land revenue was first introduced in the Madras Presidency in the early years of the nineteenth century as a reaction against the Permanent Settlement. The initial experiments were made in some districts by Colonel Read, whose ideas were later adopted enthusiastically by Sir Hector Munro. In the Bombay Presidency its introduction was favoured by Elphinstone and other administrators in the early nineteenth century. Elphinstone at first instructed the British revenue officers in the newly acquired territories not to make any innovations in the old system except for the purpose of removing known abuses. It soon became evident, however, that the old complicated system could not be worked properly by inexperienced officers whose understanding of it was very imperfect. Hence, it became necessary to construct the system anew, with an accurate land record and fixed principles of assessment. In 1827 a special officer, Mr. Pringle, was appointed to work out such a system. The Pringle Settlement involved, firstly, a field-by-field survey of all cultivable land, and secondly, the fixing of the assessment of each field according to the average "net produce." The system was first adopted in the Poona district, but unfortunately it proved a failure owing to the fact that the survey was inaccurate and the assessment not reduced. Yet the Pringle Settlement accomplished some good things: it did away with the old distinctions between the two types of tenants, *Upris* and *Mirasdars*, and introduced one common survey tenure for all. Again, the assessment based upon the value of land meant the disappearance of the older system with its numerous imposts, *pattis* and cesses.

In 1836 two officers, Mr. Goldsmid and Col. Wingate, were appointed to work out a fresh system of revenue settlement. They started their operations in Indapur taluka of the Poona district, and found that the system which they had in mind gave good results. Soon the operations were extended to other regions, while improvements were also effected in its technique, particularly in the system of classification, by Capt. Davidson. The three officers later met at a Conference and drafted the famous "Joint Report" (1847) which laid down the general principles of revenue assessment. As the survey and settlement operations were extended, it

became necessary to give a statutory basis to the system, and for this purpose, the Bombay Survey and Settlement Act (1865) was passed. This Act was repealed in 1879, when the comprehensive Land Revenue Code was enacted. This, along with its many amendments, and Government Resolutions and Executive Orders, governs the present system of land revenue.

§ 3. *The Technique of Land Revenue Settlement and Revision:* The technique of the system depends upon the operations of survey, classification, settlement, and revision of assessment. The survey operations include the measurement of village lands and the preparation of survey records based thereupon. For this purpose the unit is taken to be the "survey number," with its subdivisions, the *pot* or *phalni* numbers. Theoretically, the survey number is a plot of land which can be cultivated with the help of a pair of bullocks; it differs in different tracts according to the nature of the soil. After fixing the survey numbers, the village map is charted, and on the same basis similar maps of talukas and districts are prepared.

The system of classification of the soil differs in different regions such as the Deccan, Konkan, Gujerat, etc., but ordinarily three types of land are recognised, viz., (i) dry crop; (ii) wet crop; (iii) garden. Each type is divided into three main classes, black, red and gravel, these being further subdivided according to depth and other qualities. Fields are then given their classification value in terms of so many annas in a rupee, in which procedure account is taken of extrinsic circumstances such as "faults" and "advantages" of each plot of land. The assessment is then "settled" on the principle of "aggregate to detail," i.e., the aggregate assessment is first determined for a taluka, and then it is distributed over the several villages and fields. In this latter process the principle adopted is to fix the "maximum rates" for the best type of land, and then to apply lower rates to other lands according to their "anna value."

Once the original settlement is made, revision of assessment becomes due after every thirty years. This process raises important issues such as the basis and the pitch of assessment. In regard to these, we shall first describe the procedure laid down by the Land Revenue Code of 1879 and the subsequent Government Orders and Resolutions; then refer to the legislative attempt made in 1927 to modify the procedure; and lastly, the recently enacted amendment (1939) to the Land Revenue Code.

In regard to revision of the assessment, the Land Revenue Code (1879) laid down that "in revising land revenue, regard shall be had to the value of land and in the case of land used for agriculture, to the profits of agriculture." The calculation, or rather the estimation of the "profits of agriculture," depends upon direct and indirect evidence offered by the statistics of cultivation and occupation; the collection of land revenue, whether it has been made with ease or difficulty; the material condition of the people in general; markets and communications; the history of prices; the statistics of the selling, letting and mortgage value of land; and rental statistics. It is obvious that in estimating the profits of agriculture from these factors the settlement officers are largely guided by their subjective impressions, for which reason it has been said that the whole system depends upon executive discretion. In order, however, to safeguard against undue enhancement, the following provisions have been made:

(1) **Non-Taxation of Improvements.** It is provided that in revising assessment the increased value of land resulting from the improvements on it made by the occupant at his expense will not be taken into account. This provision has a long and complicated legal and administrative history. The original doctrine on the subject was laid down by the Joint Report (1847) which stated that "the full benefit of every improvement such as the conversion of dry into irrigated land by the digging or repairing of wells and tanks, the planting of fruit-trees, etc., will be secured to the incumbent of the land and no extra assessment levied on that account." This principle was then embodied in the Survey and Settlement Act of 1865, and later with some refinements in the Land Revenue Code of 1879. In its final form it appeared in the amending Act of 1886, in which it is thus stated: "In revising assessments regard shall be had to the value of land, and in the case of land used for agriculture, to the profits of agriculture, provided that if any improvement has been effected in any land during the currency of any previous settlement made under this Act or under Bombay Act I of 1865, by or at the cost of the holder thereof, the increase in the value of such land or in the profit of cultivating the same shall not be taken into account in fixing the revised assessment."

(2) Another safeguard consists in the rules limiting the enhancement at any particular revision. The "Orders of 1874" provided: "(a) The increase of revenue in the case of a taluka or group of villages brought under the same dry-crop rate shall

not exceed 33 per cent. (b) No increase exceeding 66 per cent should be imposed on a single village without the circumstances of the case being specially reported for the orders of Government. (c) No increase exceeding 100 per cent shall in like manner be imposed on an individual holding."

These rules regarding the regulation of enhancement were at first made applicable to certain talukas of the Bombay Deccan. The Secretary of State, however, desired that they should apply to the whole Presidency. By Government Resolution of 1884, therefore, they were so extended, and applied to *all* future settlements, exceptions being made only in a few special cases (e.g., Panel Revision).

(3) Besides regulating the percentage increase of assessment, the Government also made provision for the gradual levy of the enhancements. These provisions are as follows: (i) At the Igatpuri Revision Settlement (1885) it was decided that "enhancement in excess of 4 annas in the rupee or 25 per cent of the assessment on a holding will be remitted for the first two years of the Revised Settlement, enhancement in excess of 8 annas in the rupee for the third and fourth years, and enhancement on excess of 12 annas in the rupee for the fifth and sixth years of the Revised Settlement, so that the cultivators may adjust themselves to the increased payment by degrees. These rules, commonly called the Igatpuri Concessions, were extended in 1886 to all future Settlements in the Deccan and Southern Maratha Country. They were also applied to Gujerat from 1895. (ii) Similar rules have been made applicable to the Konkan under the so-called "Bhiwandi Concessions" of 1895. - Under them the enhancements are levied by instalments of 33 per cent every three years. (iii) A special system of concessions based on the same principle are in operation in the Kanara district.<sup>1</sup>

(4) While the foregoing rules govern the revision of assessment, there are others which apply to the actual collection of the assessment once it is settled. Normally, of course, every occupant has to pay the full assessment, which is levied without regard to the fluctuations in his income. Under abnormal conditions such as failure of crops, however, suspensions and remissions of the land revenue are given under certain rules. As a result, the rigidity of the system is slightly softened.

§ 4. *Land Revenue System Under the Reforms:* The whole system of Land Revenue Settlement and Revision described above

<sup>1</sup> For details refer to "Survey and Settlement Manual," Vol. I, pp. 168-174.



came in for a good deal of discussion during this period. It was widely felt that the basis of the land tax was vague and its pitch too high; that the system of revision of assessment was highly empirical and almost entirely dependent upon the personal impressions of Settlement Officers. In this connexion the Joint Parliamentary Committee, which considered the Government of India Act of 1919, observed: "The Committee are impressed by the objection raised by many witnesses against cases in which certain classes of taxation can be laid on the people of India by executive action without, in some cases, any statutory limitation of rates, and in other cases, any adequate prescription by statute of the methods of assessments. They consider that the imposition of new burdens should gradually be brought more within the purview of the legislature. And, in particular, without expressing any judgment on the question whether land revenue is rent or tax, they advise that the process of revising the land revenue assessments ought to be brought under close regulation by statute as soon as possible. The Committee are of opinion that the time has come to embody in the law the main principle on which the land revenue is determined, the methods of valuation, the pitch of assessment, the graduation of enhancement and the other chief processes which touch the well-being of the revenue-payers."

In view of this pronouncement, the Reformed Legislative Council in Bombay soon took up the question of land revenue legislation. In March 1924 Mr. R. G. Pradhan moved a Resolution for the appointment of a Committee consisting of officials and non-officials with a non-official majority "to consider the question of bringing the process of revising the land revenue assessment under closer regulation as recommended by the Joint Parliamentary Committee," and "to report on the nature and form of legislation that should be undertaken towards the end." In June 1924 the Government appointed the "Land Revenue Assessment Committee" with the Honourable Revenue Member, Sir Lallubhai Samaldas, as Chairman. In the absence of a Resolution stating the terms of reference, the Chairman ruled that the Committee should proceed to consider the question of bringing the land revenue assessment under closer regulation by statute as indicated in the Press Note appointing the Committee. As a consequence of this ruling, the scope of the Committee's inquiries was considerably narrowed, and it was unable to investigate several important questions affecting the Land Revenue system as a whole. For instance, the Committee did not consider the vexed question whether land revenue was a tax or rent; nor did it inquire into

the incidence of land revenue in relation to the farmers' incomes. The President, it appears, also ruled out of order the proposal of converting land revenue into an income-tax, as well as the scheme for a permanent settlement of the Government assessment. Some members, in particular Mr. R. G. Pradhan and Mr. R. G. Soman, strongly protested against this limitation of the sphere of the Committee's inquiries, but to no purpose. The Committee confined its labours to the problem of statutory regulation of the land revenue assessment, and considered the question of land revenue reform only in so far as it related to it.

The inquiries and recommendations of the Committee, the subsequent Land Revenue Code (Amendment) Bill (1928), the Bardoli affairs, and the Broomfield Special Inquiry raised a number of important issues in regard to the whole system of land revenue settlement and revision. These may be discussed under the following heads: (1) the basis of assessment; (2) the pitch of assessment; (3) the period of settlement; and (4) legislative control over revision settlements.

(1) **The Basis of Assessment:** In regard to this the legal position was laid down in Section 107 of the Land Revenue Code (1879): "In revising assessments of land revenue, regard shall be had to the value of land, and in the case of land used for the purpose of agriculture, to the profits of agriculture." The vagueness of this statement is obvious. It does not say anything about the precise meaning of "profits of agriculture" or about the method of calculating them. Nor again does it say that "profits of agriculture" are to be the "basis" of assessment; it merely says that "regard shall be had" to them! As Justice Broomfield and Mr. Maxwell remark in their Report on the Special Inquiry on the Revision Settlement of Bardoli, "this vagueness appears to be intentional, and is in accordance with the history of the land revenue system in Bombay." As a fact, the Government of India Resolution of 1902 regarded this vagueness as a definite virtue, since it was calculated to leave the actual settlement to the discretion of the executive officers. Under Executive Orders the Settlement Officers were asked, while calculating the profits of agriculture, to take into account several factors such as the state of communications, proximity of markets, trend of prices, general economic conditions and history of the tract, results of crop experiments and rental value. In taking account of these factors, the settlement officers had to depend upon their personal observations and impressions. In actual practice, however, the Settlement

Officers came to rely more and more upon statistical indices, especially of rentals in the tracts to be settled, inspite of frequent instructions to the effect that too much reliance ought not to be placed on them. The rental figures, however, obviously provided a mechanical basis for revising the assessments (generally in the upward direction), and for this reason, they were greatly favoured by the officials.

The Land Revenue Assessment Committee was not unanimous on this question of the basis of assessment. The Official members, including the three Divisional Commissioners, favoured the rental basis, and suggested the following amendment of Section 107:

"The revision of assessment of land revenue shall be based upon the rental value, but regard shall also be had to the general economic conditions and history of the tract. The assessment shall not exceed half the rental value."

"Rental value means the rent for which any land would let in open competition for that use as defined in Section 48, for which its assessment is to be fixed."

The majority of the Committee, including most of the non-official members, favoured the basis of "profits of cultivation," in calculating which the Settlement Officer was to take into account the following factors: (i) The state of communication. (ii) The proximity of markets. (iii) The trend of prices. (iv) The general economic conditions and history of the tract. (v) The results of crop experiments. (vi) Rental value.

In regard to the last, the Committee observed: "In order to ascertain the rental value, the real rents paid in open competition by tenants to landlords during five years immediately preceding the revision settlement, excluding years of abnormal prices, shall be taken into consideration." The Committee further emphasized that the greatest care should be taken to scrutinize the rental statistics so as to find out their *bona fide* character, and that "the Settlement Officers should be very chary of drawing conclusions from rental figures, unless there is a considerable number of genuine rents in the group of villages for which he has to fix the assessment."

The Land Revenue Code (Amendment) Bill of 1928 embodied the official recommendation in regard to the rental basis of assessment. It was justly opposed by several members of the Legislative Council, and particularly by Rao Bahadur R. R. Kale.

The Bill was thrown out, but the controversy regarding the basis of assessment was raised afresh as a result of the popular agitation in connection with the Second Revision Settlement of the Bardoli and Chorasi Talukas. The Settlement Officer relying largely upon rental statistics, had recommended an enhancement in the assessment, which, though subsequently reduced, was sanctioned by the Government. Owing to the pressure of popular agitation, however, the Government appointed Justice Broomfield and Mr. Maxwell to make a special inquiry into the Bardoli revision settlement. Their report drew pointed attention to the danger of relying upon rental data for the purpose of revising the assessment of land revenue. The same danger was stressed by several economists and publicists who wrote on the subject during these years.<sup>2</sup> As the rental basis has not yet been definitely discarded, it is necessary to lay bare its dangers and defects:

(a) At the outset it must be emphasized that there is no connexion whatever between the theoretical concept "rent" and the actual contract rent paid by the tenant to the landlord. According to the theory developed by Ricardo, von Thunen and others, rent is the payment for "the natural and indestructible powers of the soil"; it is the excess of the produce of a piece of land over the produce of the land on the "margin of cultivation," i.e., land which just pays for the costs of cultivation. The "economic rent" in this sense is what is called "the producer's surplus," measurable either in terms of physical produce of land, or in terms of the excess of price over costs. In its subsequent developments at the hands of Marshall and others, the rent concept almost lost its association with land, and came to be defined as a surplus which any factor might obtain over its cost on account of its scarcity. Obviously the conceptual economic rent assumes conditions of perfect competition and full employment of resources, which can never be fully realized in actual life. The contract rent paid by the tenant, therefore, can have no correspondence whatever with the "economic rent" of the theoretical economists. The former contains a variety of charges like interest on the investments made by the landlord, cost of collection, remuneration for risk, and others which are not of a "surplus" character. The non-applicability of the rent concept to actual conditions of life has been stressed by several theorists. For instance, Wicksell observes: "It is evident that the Ricardo-Von Thunen Theory of rent... is too

<sup>2</sup> Cf. (i) D. R. Gadgil: "The Bombay Land System," 1928. (ii) R. R. Kale: "A Critique of the Bombay Land Revenue Code Amendment Bill," 1929. (iii) V. S. Kale: "A Lesson From Bardoli" (Indian Journal of Economics, July and October, 1929).

abstract for us to be able to expect any direct verification of it by studying the world of reality."<sup>3</sup> And yet many official exponents of the rental basis of land revenue, particularly Mr. F. G. H. Anderson,<sup>4</sup> thought as if rental value were the same as the economic surplus of land.

(b) While it can be readily seen that the actual rents do not correspond to the economic surplus of land, yet the danger inherent in using rental statistics as the basis of assessment of land revenue is not easily realized. Here we have to remember one fundamental point relating to the agricultural economy and the revenue system of the Bombay Presidency, viz., that a large proportion of land is cultivated by owners, and that land under tenancy is comparatively unimportant, especially in the Deccan tracts. This fact has been borne out by several settlement officers and others connected with the revenue and agricultural work in the Province.<sup>5</sup> The exact proportion which the land cultivated by peasant proprietors bears to the total cultivated area cannot be determined for want of statistical material, but there is evidence to show that the proportion is fairly high. This fact was stressed in the Broomfield Report on the Bardoli and Chorasi Talukas, where "cultivation by the owner himself is the normal mode of dealing with land, and leasing is more or less exceptional."<sup>6</sup>

It would appear from the foregoing observations that the initial difficulty about the rental value basis is that rental statistics are not available for large tracts of land in the Province.

(c) The question, then, resolves itself into this: Can rental statistics, wherever they are available, be safely used for the purpose of revision of assessment? In this connexion we have to remember that the statistics of rental values recorded in the village registers are of a highly defective character, and, as the Broomfield Inquiry amply proved, unless very carefully scrutinized, they are likely to be a very unsafe guide for assessment purposes. The fact is that a very large number of incalculable elements enter into the contract rents charged by the landlords in different localities and, therefore, it becomes almost impossible to find out the representative "rental value" of land. As a fact,

<sup>3</sup> Wicksteed: "Lectures on Political Economy," p. 120.

<sup>4</sup> See his "Facts and Fallacies About the Bombay Land Revenue System," 1929.

<sup>5</sup> Reference is invited to: (1) Gadgil: "The Bombay Land Revenue System," 1926, p. 12. (2) R. G. Pradhan: Minute of Dissent to the Report of the Land Revenue Assessment Committee, pp. 51, 52.

<sup>6</sup> See Report, paras. 35-62.

the conditions and elements which go to make up the actual rent differ from lease to lease, so that there is no uniformity whatever in the amount of rent which the tenant pays. Thus, as the Broomfield Report points out, in many cases rent includes interest on loans granted by the landlord, and on permanent investments effected on the property; in other cases, rent includes the expenditure incurred by the landlord on ploughing, manuring, clearing and hedging the land; in still others, a charge is made on account of some special advantage (like fruit trees) which a particular piece of land possesses. As all such factors cannot obviously be entered in the tenancy register, the actual rent figures do not yield even a rough approximation to the true rental value of land.

The foregoing consideration, viz., that in many tracts, owing to owner-cultivation, actual rent figures are not available; and that even where available they show an extreme variety as between one lease and another, have been thus set forth in "the Broomfield Report" (p. 36).

"It has been seen above that in most villages of the Bardoli Taluka, and in some at any rate, of the Chorasi Taluka, cultivation by the owner himself is the normal mode of dealing with land and leasing is more or less exceptional. Where this is the case, it is obvious that the statistics cannot always be relied upon to provide samples of all sorts of land, and that even if the owner possesses more than he can cultivate, he is not likely to lease his best lands at all. But there is another circumstance more seriously affecting rental data obtained under these conditions, viz., that the lease cases themselves more generally tend to show irregular or abnormal features, and a smaller proportion even of those admitted as evidence, can safely be regarded as typical of the village as a whole. . . . The point which we wish to make here . . . is that inferences regarding the rental value of a whole village cannot safely be based on exceptional cases; hence unless leasing of an ordinary, normal character is reasonably plentiful in a village, even the available data lose a part of their value, and especially careful scrutiny of individual cases is necessary in order to discover those which may give a real indication of rental value."

(d) There is, however, a still graver objection to the use of rental value as the basis of assessment. It is that the rents charged by landlords have no correspondence whatever with the true profits of agriculture and, therefore, with the farmer's capacity to pay. In most instances the charge for the hire of land tends

to be excessive on account of the extreme pressure on land and the lack of alternative employment for the farmers. Keen competition among the cultivating tenants often drives up the rents to excessive levels, which ultimately causes defaults in numerous cases. In fact, not infrequently, high rents stipulated by the landlords include an allowance for non-payment. Again, in some tracts rents are known to have gone up to phenomenal levels as a consequence of some temporary factor such as, for instance, the cotton boom of the post-war period. In such cases, rents can have no relation to the true productive capacity of land, or to the net profitability of agriculture; and, therefore, it is highly dangerous to base assessments on rental figures.

This conclusion may be reached in a somewhat different way. If rents were related to the profitability of agriculture, we should find, in a homogeneous tract, a fairly uniform proportion between actual rents and the gross produce per acre. In actual fact, however, no such uniformity is found in tracts for which such figures are available. For instance, in the Survey of Agriculture in Wai Taluka carried out by the Gokhale Institute of Politics and Economics, it has been discovered that the proportion of rents to gross produce shows an extreme range, from 24 per cent in one case to 195 per cent in another. It would, therefore, appear that the actual rents charged contain a variety of elements in each case, and that owing to excessive competition, rack-renting is common. This shows how dangerous it is to base assessments of land revenue on rental values.

While, thus, there are grave objections to the rental value basis from the point of view of fiscal justice, the preference for it on the part of revenue officials is not difficult to understand. In spite of frequent Government instructions to the Settlement Officers not to rely too much on rental statistics, the Officers had come to rely increasingly on a rental "index" invented by Mr. Webb, since it provided a very simple and automatic method of calculating the assessment at revision settlements and, in most cases, favoured an enhancement. The Bardoli episode completely discredited this basis of land revenue assessment and revision, and pointed to the need for devising a system of assessing the land tax which would have a greater correspondence with the true profits of agriculture.

In spite of such warnings, the rental basis has not yet been completely discarded. The original Land Revenue Code (amend-

ment) Bill introduced by the Congress Ministry in 1938 embodied the rental basis of assessment; but of this more later.

(2) The second issue raised by the Land Revenue Assessment Committee was that of the pitch of assessment. The official members favoured a maximum of 50 per cent of the rental value, while the non-official majority recommended 25 per cent of the "profits of cultivation," i.e., the gross produce less all the expenses incurred in deriving those profits. Unfortunately neither party discussed the question of the pitch of assessment with reference to the incidence of land revenue, for finding which, data were and are still inadequate. But there is no escaping such an inquiry; it has been attempted at a later stage.

(3) The third point considered by the Committee was that of the period of settlement. Here, again, there was a sharp cleavage of opinion between the official and nonofficial witnesses and members. The former as a rule favoured the retention of the current period of thirty years; the non-officials preferred a longer period, some even suggested a permanent settlement. This question is also examined later in connexion with the reform of the land revenue system.

(4) In regard to the last question also, viz., the appointment of a standing Advisory Committee of the legislature to examine all revision settlement proposals, the official and non-official elements held divergent views. The officials thought that all revision proposals went through a series of careful scrutinies at the hands of several revenue officers, and that the people concerned had ample opportunities of ventilating their grievances. If, however, the officials thought, a legislative body were to be associated with this work, it would be swayed by political considerations and influenced by local interests. The majority of the Committee, however, thought that these objections were greatly exaggerated. "In their opinion it is unfair to suppose that the non-official members of the proposed Committee would not give absolutely unprejudiced advice and would not place the interests of the state and the community at large above their own personal wishes and the demands of their constituents. They consider that the officials are apt to regard the question of assessment too much from the financial point of view and are liable to ignore the real interests of the masses in their not unnatural desire to bring additional revenue to the exchequer." The Committee, therefore, recommended that "there should be a statutory provision that all



proposals of revision settlement should be placed before a standing advisory committee consisting of six members, of whom no less than four should be elected non-official members of the Legislative Council, elected by that body itself.”<sup>7</sup>

The Land Revenue Code Amendment Bill of 1928 embodied most of the recommendations of the official members of the Committee. Thus, in regard to the basis of assessment, the Bill provided that “the revision of assessment of land revenue shall be based primarily on rental value.” As regards the pitch of assessment the Bill sought to limit it to 35 per cent of the rental value. The Bill, further, made no provision for a “standing advisory committee” of the legislature to consider all revision proposals. The Bill met with overwhelming opposition in the Legislative Council, and was withdrawn by the Government.

During the subsequent years, the need for revising the system of land revenue assessment so as to make it more in uniformity with the farmer’s capacity to pay became increasingly acute. During the depression years the prices of agricultural commodities fell by anything between 30 and 60 per cent, and as a consequence the real burden of the land revenue assessment increased enormously.

§ 5. *The Land Revenue Legislation of the Congress Ministry:* High hopes were entertained in the matter of land revenue reform when the Congress Ministry came to office in August 1937, particularly in view of the following pronouncement contained in the Congress Election Manifesto: “Pending the formation of the fuller programme the Congress reiterates its declaration made at Karachi that it stands for a reform of the system of land tenure and revenue and rent, and an equitable adjustment of the burden on agricultural land, giving immediate relief to the smaller peasantry by a substantial reduction of agricultural rent and revenue now paid by them, and exempting uneconomic holdings from payment of rent and revenue.”<sup>8</sup>

The Congress Ministry was aware of the defects of the Land Revenue System. In his first Budget speech, the Hon’ble Mr. Latthe admitted “the anomalies which had crept into the system of classification of lands and the rate of assessment dependent upon that classification,” and recognised that “our first duty, therefore, was to give relief by way of reduction of the state demand.”

<sup>7</sup> Report, p. 25.

<sup>8</sup> Quoted by Mr. Jambadas Mehta in his speech on the Finance Act Amendment Bill, 1939, (B. L. A. D., Vol. 5, p. 1110).

At that time, the Finance Member could only write off all arrears, except those in respect of the previous year, and reduce the demand in the case of over-assessed lands to the extent of Rs. 5 lakhs. The latter, however, could not be effected, as, in the absence of definite principles, the sum could not be allocated for the intended purpose. It became clear that the question of relief in assessment must be considered as a part of a larger scheme of reform of the land revenue system as a whole. The Ministry, therefore, set about the task of preparing a comprehensive measure dealing with the subject. In April 1939 they presented the Land Revenue Code (Amendment) Bill, which subsequently became an Act.

The general object of the Act is, like that of the Bill of 1928, to place the land revenue system on a statutory footing, and to subject all the processes connected with land revenue assessment to legislative control. The following is an account of the principle provisions of the Land Revenue Code (Amendment) Act (1939).

I. In the first place, the Act provides that the Settlement Officer shall divide the lands to be settled into "homogeneous groups." The following factors are to be considered in forming these "groups": (i) Physical configuration; (ii) climate and rainfall; (iii) markets; (iv) communications; (v) standard of husbandry; (vi) population and supply of labour; (vii) agricultural resources; (viii) variations in the area of occupied and cultivated land during the last thirty years; (ix) wages; (x) prices; (xi) yield of the principal crops; (xii) ordinary expenses of cultivating the land; (xiii) rental values of land used for the purpose of agriculture; (xiv) sales of land for the purpose of agriculture.

After having divided a taluka into such groups, the Settlement Officer shall determine the "standard rates" of assessment for each group. Corresponding rates are then to be applied to individual survey numbers. The determination of the standard rates of assessment raises two issues: the basis of assessment and the pitch of assessment.

II. With regard to the basis of assessment, we have given an account of the discussion raised by the Land Revenue Amending Bills. We have argued the case against the basis of "rental value" so dear to the heart of the officials. Reference has also been made to the Bardoli agitation and the subsequent inquiry by Justice Broomfield and Mr. Maxwell which pointed a warning finger against the use of rental value statistics without proper scrutiny. During the subsequent years nothing had happened to

weaken the case against the rental basis; and yet, the original Land Revenue Code (Amendment) Bill presented by the Hon'ble Mr. Morarji Desai embodied this very basis which was so universally condemned! The original Bill provided that the Settlement Officer shall fix "the standard rates of each class of land in each group on a consideration of the rental values and the economic history of each group." In the Select Committee, however, better counsels prevailed, and the original provision was modified thus: "The standard rates shall be fixed on a consideration of all the factors mentioned in sub-section (2) of Section 117(G)" i.e., all the factors that are to be considered while forming the "groups." Among these factors rental value is only one, and as far as the law goes, not a whit more important than any other. One cannot, therefore, call it the "basis of assessment," though Mr. Desai frequently referred to it as such even after having accepted the Select Committee's amendment.

Though rental value is not legally the basis of assessment, it is to be used for limiting "pitch" of assessment. The Act lays down that the assessment "shall not exceed 35 per cent of the average rental values of such lands for a period of five years immediately preceding the year in which the settlement is directed." This appears to be a very curious provision. While rental value is not made the basis of assessment, the maximum pitch of assessment is fixed in terms of it. Now, as the true rental value of lands in a locality is difficult to determine, and, for that reason, it ought not to be the basis of assessment, it follows that the maximum pitch of assessment also cannot be fixed in terms of it. It would have been more logical to fix the maximum pitch of assessment as a percentage of rental value if, in the first instance, it were possible to find out some representative amount which could be regarded as the true rental value of land in a tract; and if, in the second place, this amount could be looked upon as the true "profits of agriculture" and as a measure of the farmer's capacity to pay. But, as already shown, rental value does not possess this character and, therefore, it cannot be used for limiting the pitch of assessment.

Another important consideration in this connexion is that the fixation of the maximum pitch of assessment at 35 per cent of "rental value" is not calculated to afford any appreciable relief to the peasantry, for the simple reason that rents themselves are generally at an inflated level. In the presence of rack-renting, such a maximum has little meaning. The fact of rack-renting was

admitted by the Revenue Member while introducing the Tenancy Bill, one of the objects of which was to fix "fair" rents. But in the Tenancy Bill one of the factors for determining fair rents was "the assessment of land"! Maximum assessment is thus related to rents; but "fair rents" are to be determined with reference to assessment!

III. The term of the Settlement is retained at 30 years. The Amending Act, however, reduces the limits of enhancement of assessment which were formerly contained in the Executive Orders. It is provided under Section 117-F that the enhancement of assessment at a Settlement shall not exceed 25 per cent in the case of a taluka and a group, and 50 per cent in the case of a village, a survey number or its sub-divisions. The Provincial Government has, however, been empowered to exclude certain lands from the operation of this Section.

The Amending Act retains the safeguard (Sec. 117-H) that increase in the rental value due to improvements in land effected by or at the expense of the holder, "during 30 years immediately preceding the date on which the Settlement for the time being in force expires," shall not be taken into account in fixing the revised assessment.

IV. Under Sections 117-I and J it is provided that the Settlement Officer, after the necessary inquiry, shall submit the report to the Collector, who shall cause it to be published in the regional language. Objections, if any, to the proposals contained in the report can then be submitted to the Collector, who, after taking them into account shall forward the report to the Government with his remarks thereon.

Section 117-K provides that any person aggrieved by the report may within 2 months apply to the Provincial Government to refer it to the Bombay Revenue Tribunal set up by the Bombay Act No. XII of 1939. Till April 1937 the powers of appeal and revision in revenue cases were exercised by the Government. The Government of India Act of 1935, however, provided that such powers should be entrusted to some special tribunal. In accordance with this, the Bombay Government constituted the Revenue Tribunal on the 1st of April, 1937, consisting of the Divisional Commissioners and the Commissioner of Excise. It was, however, thought desirable that in the place of a purely official tribunal, there ought to be set up an independent body to inquire into the complaints and objections of the aggrieved parties

in cases. For this purpose was passed the Bombay Act No. XII of 1939 by which a permanent Revenue Tribunal has been set up. The Act does not lay down the number and qualifications of the members, but it is intended that the tribunal should be presided over by a high judicial officer, and that at least one member should be a senior revenue officer. The powers and jurisdiction of the Tribunal extend to all appeals and revisions in all revenue cases passing under a number of Revenue Acts (see Schedule attached to the Act), chiefly the Bombay Land Revenue Code.

Under Section 117-L it is provided that the Settlement Report, along with the objections and the opinion of the Revenue Tribunal, shall be placed before both the chambers of the Provincial Legislature, wherein it is liable to be discussed by a resolution.

V. Section 117-M introduces an extremely important innovation in the Land Revenue Administration. Under the old system no provision existed for modifying the assessment during the course of a thirty-year period of settlement. An element of elasticity was indeed introduced by the rules relating to remission and suspension of land revenue under certain conditions. But these rules came into operation under special circumstances such as a failure of crops, etc. It is, however, common knowledge that the cultivator's capacity to pay varies from year to year in accordance with the movements of prices of agricultural produce. Section 117-M, therefore, provides that the Government may declare any settlement to have been fixed with reference to specified prices of specified classes of agricultural produce. When such a declaration has been made, "it shall be lawful for the Provincial Government to enhance or reduce the assessment in such area in any year by granting a rebate or placing a surcharge on the assessment by reference to the alteration of the prices of the classes of agricultural produce specified in the declaration."

This provision of which the object is to render the land revenue system elastic by securing a greater degree of correlation between assessment and the farmer's income, is modelled upon the "sliding scale" system adopted in the districts of Montgomery and Lyallpur in the Punjab in 1935. The Bombay scheme, however, differs from the Punjab system in two respects. Firstly, in the former, provision is made for revising assessments in accordance with changing prices in both directions, while in the Punjab scheme maximum assessment rates are fixed in terms of "commutation prices," and only remissions (and not enhance-

ments) are allowable in case of falling prices. Again, the Punjab system provides for variation of assessments not only when prices fall, but also when the matured area and the average yield are less than what are assumed for the purposes of fixing maximum assessments. In practice, however, account is normally taken of price changes alone, the other two factors being regarded as constant unless there are exceptional reasons to the contrary.

The provision in the Bombay Act is subject to a number of objections. In the first place, it is based upon the wrong assumption that the relation between price changes and the profitability of farming is uniform for all types of farming. The fact is that price changes affect the real income of different types of farmers differently. As Dr. Mann pointed out many years ago, a rise of prices benefits only those farmers who produce a surplus of food crops over and above their own needs, and of course, those who produce some commercial crops. But farmers whose produce is not sufficient for their own consumption, and who, therefore, are compelled to purchase some produce from the market, would actually suffer as a result of a rise of prices. The same point has been made out by Sir Malcolm Darling in his classic, *The Punjab Peasant in Prosperity and Debt*.<sup>9</sup> This consideration is of the highest importance in a Province like Bombay, where small-scale farming is the characteristic feature of agricultural economy. It is, therefore, clear that the provision contained in Section 117-M is applicable only to those tracts where there is a close relation between prices and the profits of agriculture, e.g., tracts where only commercial crops like cotton are cultivated.

There is another consideration which has to be remembered in connexion with this provision. It is that while it makes assessments dependent upon price changes, it leaves out of account other factors which are equally important in determining the profits of agriculture and the incomes of the farmers, viz., the actual yield of the season, and the changes in the costs of production. In several tracts of the Bombay Presidency, particularly in the Deccan, agriculture is highly precarious owing to the uncertainty of rainfall. The actual yield of crops, therefore, shows large variations from year to year according to the volume and distribution of rainfall. Obviously, the incomes of farmers show corresponding fluctuations from season to season as a result of this factor, over and above the factor of price change. Again, the

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<sup>9</sup> Pp. 224-26, 1925.

ultimate profitability of farming may also depend upon the several elements in the cost of production, particularly the wages of hired labour, the prices of seed, manure, cattle and implements. Hence, strictly speaking, assessments should be related not only to changes of prices, but also to variations of seasonal yield of crops and to the movements in the cost of production. In practice, however, such a system would give rise to several difficulties; in particular, the task of estimating the yield of crops in the different localities would involve extensive surveys of agricultural conditions over the Province every season, and this would necessitate the delegation of an undesirable amount of power into the hands of subordinate officials, with the consequent danger of corruption. Considering all these difficulties, the Punjab Land Revenue Committee came to the conclusion that the application of the sliding scale to yields would be impracticable.<sup>10</sup> It is, however, equally clear that any system of varying assessments that does take into account the factor of yield is bound to be highly defective.

Another point which deserves to be stressed in connexion with Section 117-M is that its application would have to be made dependent upon the prevalence or otherwise of owner-cultivation as against any form of tenancy. It is clear that where owner-cultivation prevails (and where a commercial crop is produced), price changes would directly affect the income of the farmer. But in case the farmer is a tenant paying either a cash rent or a crop-share rent, the relation between price changes and the farmer's income would not be of a simple or direct character. If the cultivator is paying a fixed money rent, a rise in prices would benefit him, and injure the landlord, who would have to pay an enhanced assessment to the Government. In case of falling prices, however, the tenant-cultivator's income would be reduced, while he would have to pay a fixed rent to the landlord. Under such conditions, if the Government assessment is lowered, the benefit would not reach the cultivator, but would be absorbed by the landlord. If the tenancy is based upon the crop-share system, rising prices would benefit both the parties, but the landlord alone would have to bear the enhanced assessment; in the event of falling prices, both parties would suffer, but the benefit of reduced assessment would be enjoyed by the landlord alone. All this shows that the application of the sliding scale of assessment based upon price changes would give rise to a good deal of injustice wherever tenurial organization prevails.

<sup>10</sup> Report of the Punjab Land Revenue Committee, p. 45.

The foregoing discussion points to certain limitations in the application of Section 117-M. Clearly, its applicability is restricted to tracts where profits of farming are intimately connected with the price factor, i.e., where some commercial crops predominate. Again, the system of changing assessments according to prices would only suit a tract where owner-cultivation prevails, and not to one where tenancy is the characteristic form of agricultural organization. While, thus, the applicability of the provision is restricted, its actual utility is also limited by the fact that profits of farming are dependent not only upon prices, but also upon the seasonal yield of crops.

It does not appear that all these limitations of the Section have been recognized by the Settlement Officers who have conducted revision settlements under the new Act. In the case of the third Revision Settlement of Viramgam Taluka (1940), the Settlement Officer urges the application of this Section on the ground that in that tract there is an intimate connexion between profits of agriculture and prices, and that the prevailing system of tenancy is based upon crop-sharing. The former reason is based upon the fact that in the taluka there is a predominance of a money crop, viz., cotton. The latter reason, viz., the prevalence of the crop-share system of leasing land, does not in our view justify the application of Section 117-M.

In another instance, viz., in the case of the revision settlement of Malegaon Taluka, the Settlement Officer's recommendation regarding the application or otherwise of Section 117-M is based upon the consideration of the proportion of landholders to tenants. In his view the fact that the Taluka consists predominantly of landholders justifies the fixing of the assessment *independently* of Section 117-M. This seems to be contrary to the conclusion arrived at in the present discussion. We feel that the system of varying assessments according to prices should be applied to tracts where owner-cultivation prevails to a large extent, for the simple reason that in such tracts there is a close relation between prices and profits of cultivation, assuming, of course, that a commercial crop is produced. But here the Settlement Officer justifies the *non-application* of the provision of varying assessments according to prices on the ground of the predominance of landholders.

§ 6. *The Future of the Land Revenue System:* Though, in recent years, the importance of land revenue in the fiscal system of the Province has declined, it still remains a major source of



Provincial income; while its administration is so closely connected with the welfare of rural society that its reform is still a fiscal problem of first class importance. In current discussions there seems to be three distinct directions in which land revenue reform in *ryotwari* tracts is advocated. Firstly, some suggest that land revenue assessments should be based upon the income tax principles and procedure. Those who feel that this would constitute too drastic a measure, advocate that the existing land revenue system should be retained, but that it should be modified in respect of the basis and pitch of assessment so that land revenue should be more closely related to the taxable capacity of the peasantry. Still others feel that both the foregoing lines of reform would involve insuperable difficulties, and that, therefore, the whole problem would be simplified if the land tax is permanently stabilised at a low level. These suggestions are discussed in what follows.

§ 7. *Land Revenue and the Income Tax*: In recent years it has been frequently suggested that the system of land revenue assessment should be brought within the fold of the income tax administration. It is claimed that by so doing land revenue could be related to the farmers' capacity to pay from year to year. While, however, the necessity for a closer relation between land revenue assessments and the annual profits of farming may be easily recognised, it may be doubted whether all the several processes of the income tax assessment and collection can be applied with success to land taxation under the peculiar circumstances of our country. The Punjab Land Revenue Committee (1938) which examined this question thoroughly came to the conclusion that the income tax system is not suited to our agricultural economy with "a peasantry largely illiterate, without accounts, and intensely conservative."<sup>11</sup> Among the several difficulties which inhere in the application of the income tax principles and processes to land revenue assessment may be mentioned the following: (1) The first difficulty would arise owing to the fact that an overwhelming majority of the farmers are illiterate and incapable of keeping accounts of their yearly operations. That the farmers would get their accounts done by some literate person in the village is also quite unthinkable. (2) The second difficulty would be that the cost of administration would be excessively high owing to the vast number of assesseses. The number of assesseses, obviously, would depend upon the exemption limit; if this is kept at a high level, say Rs. 1,000, very few persons would be liable for the tax, and consequently the proceeds would be negligible. If the exemption

<sup>11</sup> Report, p. 30.

limit is lowered to, let us say, Rs. 200, the number of assesseses would increase and so would the cost of assessment and collection. Whatever the exemption limit, the net proceeds of the tax would be comparatively low. It is clear that if land revenue is to be converted into an income tax, we shall have to put up with a considerable loss of revenue. But even then it may be doubted whether it would be possible to bring into force a system of annual assessment in the case of farm incomes under the present circumstances.

We feel that though theoretically the policy of converting the land revenue into an income tax on farm income is justifiable, the practical difficulties of such a procedure are immense. It would, therefore, be wiser to find out some alternative directions of reform in respect of land revenue assessment.

§ 8. *Modifications of the Existing System:* There seem to be three main directions in which the existing system needs to be modified so as to make it more in conformity with fiscal justice. In the first place, the basis of land revenue assessment has got to be defined afresh; in the second place, the pitch of assessment has to be lowered and made more uniform from region to region; and lastly, the system of assessment needs to be made more elastic and more closely related to the year to year variations of the farmer's income.

(i) The present position regarding the basis of assessment is quite unsatisfactory. The Land Revenue Code (Amendment) Act of 1939 makes it dependent upon a large number of factors such as physical configuration, rainfall and climate, prices, markets, communications, rental values, etc. The estimation of the profits of agriculture upon a consideration of these factors is bound to involve a large element of conjecture, and for that reason, among others, is bound to be affected by the personal inclinations of the Settlement Officers. It seems necessary, therefore, to relate the assessment of the land revenue to some statistically measurable factors such as "annual value" or "the net produce" of different types of land. The basis of annual value was favoured by the Indian Taxation Inquiry Committee which defined it as "gross produce less cost of production, including the value of the labour expended by the farmer and his family on the holding, and the return for enterprize."<sup>12</sup> The Madras "net produce" system is analogous to this; it also involves the estimation of the gross produce and the probable expenses of cultivation for different

<sup>12</sup> Report, p. 85.

types of land. But even here, much reliance has to be placed upon factors which are not statistically measurable, and to that extent, even the Madras System involves a certain amount of guess-work in the matter of land revenue settlement. The factors which affect the net income of farming are so various, and they operate with so much diversity in the case of different farmers, that it is impossible to reduce them to any uniformity for the purposes of land taxation.

(ii) **The Pitch of Assessment:** Again, the pitch of assessment needs to be equalized as well as lowered generally. This will necessitate a thorough inquiry into the incidence of land revenue in various regions. At present the materials for such a study are scanty, while the methods of inquiry are also not generally agreed upon. In the early years of the present century the problem was examined with his accustomed thoroughness by Rao Bahadur G. V. Joshi.<sup>13</sup> In order to refute the official contention that the Bombay assessment rates were light as compared with other Provinces, Mr. Joshi instituted an inquiry into the incidence of land revenue along the following lines: (i) incidence per head of population; (ii) incidence per acre of cultivated area; (iii) the ratio of assessment to gross produce; (iv) the ratio of assessment to net produce. It will be remembered that nearly twenty-five years later the Taxation Inquiry Committee attempted an inquiry along similar lines.

It is obvious that inquiries (i) and (ii) cannot yield significant results. Owing to the differences in the ratio between agricultural and non-agricultural population, and the diversity in soil conditions, the incidence per head and per acre will not afford any rational basis of comparison as between different Provinces and regions. The really significant inquiry would relate to the incidence of the land revenue assessment on the net income of the farmer. From Dr. Mann's two village surveys, it appears that the proportion of assessment to "the income from land" was 1/6 and 1/11. Mr. Keatinge gives two instances of "economic holdings" where the incidence is about 33 per cent. In more recent studies, we obtain data relating to the cost of production of certain crops in some typical regions of the Bombay Presidency, from which a rough calculation of the incidence of the land revenue can be made. Thus, in the cost studies conducted by the Imperial Council of Agricultural Research,<sup>14</sup> we find the follow-

<sup>13</sup> *Vide Writings and Speeches of Rao Bahadur G. V. Joshi, 1912, pp. 430-482.*

<sup>14</sup> "Report on the Cost of Production of Crops in the Principal Sugar Cane and Cotton Tracts in India," Vol. II, Bombay.

ing proportions as between land revenue and cost of production, business income, and rental value of land.

TABLE NO. 26

AVERAGE PERCENTAGE OF LAND REVENUE TO TOTAL  
COST DURING THE YEARS 1933-34, 1934-35, AND 1935-36

Surat	Poona	East Khandesh	Dharwar
11.9	1.1	8.1	8.9

The Poona percentage is so low because it relates to the irrigated area, where water-rates and not land revenue assessment constitute the principal item of cost.

It is also interesting to note the proportion between land revenue assessment and "business income" of farmers, and the rental value of their land. These latter terms are defined as follows:

(i) The term "farm business income" is used in the sense in which it has been employed by R. B. P. C. Patil and other agricultural economists. It includes: (1) Theoretical profit or loss; (2) the rental value of land which the farmer owns; (3) the labour value of personal or family labour; (4) interest on any capital which the farmer possesses. The farm business income so calculated "represents really not only the cash returns which the man gets out of his holding but the living which he and his family have been able to make on account of their land, their labour and their capital. . . . It is a real measure of the man's actual economic position."<sup>15</sup>

It then appears that "the business income" of the farmer broadly corresponds to the income-tax conception of "taxable income."

(ii) "Rental value" is "actual rent where paid. . . . In the case of owned land the amount charged is what the land would have fetched as rent if it had been rented out."

Table No. 27 has been constructed out of the figures contained in the cost studies referred to above.

<sup>15</sup> Op. cit., p. 5.

TABLE NO. 27

## THE PROPORTION OF LAND REVENUE TO TOTAL RENTAL VALUE AND BUSINESS INCOME

District	Taluka	Village	Crop	Total Acreage	Total Land Revenue	Business Income	Total Rental Value	Proportion of 6 to 7	Proportion of 6 to 8
1	2	3	4	5	6	7	8	9	10
					Rs. As. Ps.	Rs. As. Ps.	Rs. As. Ps.		
Surat	Bardoli	Sandhar	Kharif Cotton	91.15	40- 1- 0	1,931- 6- 3	78-14- 8	2.00	50.7
"	"	Rayasu	"	63.77	36-11- 2	1,862- 6- 4	52- 0- 0	1.97	70.7
"	Jalalpur	Sisodra	"	76.17	26- 3- 4	1,952-11- 9	91-13- 3	1.35	21.32
"	Bardoli	Sandhar	Kharif Jowar	58.65	37- 6- 0	501-13-11	70-12-11	7.41	52.68
"	"	Rayam	"	48.14	39- 7- 9	657- 7- 5	57- 7- 8	6.01	66.69
East Khandesh	Jamner	Garkheda	Cotton	103.44	14- 9- 7	134- 6- 3	25-14-11	10.90	56.25
"	"	Jalgaon	Mamurabad	83.36	27-14-11	679- 8- 0	56- 5-10	2.94	49.55
"	"	Parola	Tamaswadi	67.51	13- 1- 7	1,596-15-10	36-15- 3	0.81	25.13
"	"	Jamner	Garkheda	49.23	18- 2- 3	923- 5- 8	38- 2- 3	1.90	46.9
"	"	Jalgaon	Mamurabad	29.69	27- 5-11	963- 5-11	51- 3- 8	2.70	53.2
"	"	"	Groundnut	13.04	22-12- 8	526- 9- 0	44- 6- 0	2.10	49.9
Dharwar	Gadag	Hulkoti	Kharif Jowar	39.13	5- 9- 2	26- 2- 8	15- 4- 6	21.4	36.2
"	Dharwar	Harobelwadi	" "	39.22	13- 6- 6	8-10- 3	22- 9- 0	—	43.2

The proportion between land revenue and farm business income, and that between land revenue and total rent in Wai Taluka of which the farm business has been surveyed by the Gokhale Institute of Politics and Economics are given in Table No. 28.

TABLE NO. 28

SHOWING RELATION BETWEEN LAND REVENUE, FARM INCOME AND RENT IN WAI TALUKA

(Source: Farm Business in Wai Taluka, Publication No. 7)

Year	1 Land Revenue Rs.	2 Farm Income Rs.	3 Total Rent Rs.	4 Percentage of 1 to 2	5 Percentage of 1 to 3
1936-37	12,067	38,679	18,034	31.1	66.6
1937-38	15,087	49,074	24,474	30.6	61.2

These figures show that as compared with the income-tax land revenue is pitched at a considerably higher rate, and that its real burden is much greater owing to the absence of an exemption limit. The proportion between land revenue and rental value is also much higher than the statutory 35 per cent in the case of most of the villages in the three districts of Surat, East Khandesh and Dharwar. This conclusion would seem to point to the necessity of a fairly general reduction in the land revenue assessments over the whole province.<sup>16</sup> But such a procedure is beset with difficulties, as the Congress Ministry realised, owing to the fact that there are large variations in the proportion between assessment and rent in different regions, and that, therefore, no single or uniform reduction would conform to fiscal justice. If, on the other hand, the pitch of assessment is reduced by different degrees in different regions, a good deal of arbitrariness may result, owing to the inaccuracy of statistics relating to the proportion between rent and land revenue in different localities.

(iii) Fluctuating Assessment: Another urgent line of reform is in regard to the present rigidity and inelasticity of the assessment. The assessment is fixed once for all for thirty years and normally it is levied without regard to the fluctuations in the farmer's income. The farmers are expected to make provision for bad years out of the surplus of the good ones! The official policy in this regard is that the normal assessment does take into account

<sup>16</sup> This conclusion was arrived at on the basis of pre-war cost, price, and income structure. Obviously, it would need to be modified in view of war-time price and cost changes.

the fluctuations of farm income as a result of variations in season. Thus, in a Government Resolution of 1884 it is observed: "It is often asserted that the rigid collection of land revenue in good and bad seasons is incompatible with the sustained solvency of the rayot. It is, however, to be noted in the first place that in a revenue settlement everything affecting the security or insecurity of agriculture in the tract under settlement is weighed and the maximum rate of each group of villages is graduated accordingly. No consideration is more potent in the adjustment of rates than the security or insecurity of the crops in the area under settlement. A taluka is often divided into five or six groups for no other reason than the comparative certainty of the rainfall. Thus, allowance is made in the assessments for the fluctuations of agricultural returns caused by variations of season by what may be called a standing remission co-extensive with the settlement in favour of the less fortunate tracts." For this reason, normally the assessment is to be levied rigidly, exceptions being made only when conditions are really abnormal. Under such conditions rules of suspension and remission come into operation. Thus, when there is evidence of a total or partial failure of crops (below 4 annas or between 4 and 6 annas), suspension may be given in the first instance. Subsequently, whether the suspended assessment should be collected or remitted, would depend upon the Collector's view about the paying capacity of the farmer.

In spite of the system of suspensions and remissions, the land revenue system remains considerably rigid and inelastic. The rules regarding suspension and remission are not meant for normal year-to-year fluctuations of the profits of agriculture due to variations of season, prices and other factors affecting the business of the farmer. This has been evidenced in the past by the comparative stability of the land revenue assessment even during the worst periods of the depression. What is wanted, therefore, is a system which will render the year-to-year assessments more in conformity with the changes in the farmer's income caused by several factors that influence the farmer's business.

In this connexion mention has been already made of the system introduced by the recent Land Revenue Code (Amendment) Act (1939). As noted above, Section 117-M of the Act provides for varying the assessments in accordance with changes in prices in the case of certain settlements. This provision, however, seems to be ill-suited to conditions in which the farm incomes do not move in conformity with prices. It is, therefore, not enough to vary the assessments with prices; they should be made to vary

with several other factors which together go to make up the farmer's income.

At this stage detailed reference must be made to the system of fluctuating assessment operating in certain tracts in the Punjab. In 1935 the Punjab Government introduced the "sliding-scale" system of assessment in the districts of Montgomery and Lyallpur. Under this system, the maximum land revenue rates were fixed in terms of "commutation prices" of certain staple products, and remissions are given from year to year if the prevailing prices are lower, the "matured area" smaller, and the yield of crops less than that adopted for fixing the maximum rates. Normally, however, only price variations are taken into account in determining the remissions to be granted, though, obviously, the yield is as important as prices in making up the farmer's income, and his paying capacity. The Punjab Land Revenue Committee, however, thought that the application of the sliding scale to yields would be impracticable; in fact, it would be attended with several evils, particularly corruption among lower revenue officials whose duty it would be to calculate the probable yields. The Committee further thought that the sliding scale based on prices was also not free from objection; for, there is no uniform relation between price changes and variations of income of different types of farmers. As a general rule, rising prices benefit those farmers who have a surplus of good grains to sell in the market, and, of course, those who produce commercial crops; but they may not increase the real income of farmers who produce for their own needs, and who have, sometimes, to go to the market for sundry purchases. In the case of falling prices, the producers of commercial crops suffer more than those who produce food-crops for their own consumption. For all these reasons, the Punjab Committee held that the sliding-scale system should not be extended to other parts of the province, and that remissions should be given as in the past, after careful consideration of the special circumstances of each tract.

The foregoing discussion points to the conclusion that a perfectly satisfactory system of fluctuating assessment is very difficult to devise and to administer. Theoretically, the assessments will have to be varied according to changes in the net profits of farming; but this latter is affected by a large number of factors such as prices, yields, cost of production, etc. Further, the changes in the factors, particularly prices, affect different types of farming differently, so that it would be unjust to have a uniform system of fluctuating assessments based upon price changes.



§ 9. *Stabilization of Existing Land Revenue Assessments:* In the foregoing sections we have discussed the practical difficulties involved in converting land revenue into an agricultural income-tax, and in modifying the present system so as to make it more in conformity with fiscal justice. In view of these difficulties some have suggested that in the interests of simplicity and economy, the existing land revenue assessments (excepting in those cases where they are palpably excessive) should be declared permanent with reference to some basic price-level, and that in the future the assessments should not be revised unless the prices depart from the basic level by 25 per cent or more. Such a proposal was made by several economists and public men in the past. Justice Ranade and Mr. Gokhale recommended it for all ryotwari provinces. In more recent years, such a proposal has been sponsored by Mr. H. B. Shivdasani,<sup>17</sup> Professor D. G. Karve<sup>18</sup> and others.

It would seem that the proposal derives from the English system of land taxation. In England the land tax was made permanent in 1797 by William Pitt, and in subsequent years the state has allowed redemption of the tax by private owners. Of course, over and above this tax, there exist in England certain levies on the rental value of lands and on the profits of cultivation; but these are a part of the normal income-tax system. Possibly the same system could be adopted here also. Thus the current land revenue assessments may be declared permanent, perhaps subject to redemption at the rate of 30 times the assessment; while an income-tax on agricultural profits, with a suitable exemption limit and graduation, may be imposed.

On grounds of fiscal theory such a reform in land taxation would be wholly desirable. It might, possibly, involve a small revenue loss, but this would be tolerable, and even desirable, if it is occasioned by reduction of assessments on over-assessed lands. Anyway, it is doubtless that if the general Provincial tax structure is to be modernised, land revenue should come to occupy a less and less important place in the fiscal system. From this point of view it would be worth while to investigate the legal and administrative aspects of this proposal of stabilizing the existing land revenue assessments and imposing an income-tax on higher farm incomes.

<sup>17</sup> The Bombay Land Revenue Assessment Committee Report, Appendix II, pp. 106-109.

<sup>18</sup> "Reform of Taxation" in "Economic Problems of Modern India," Vol. II, edited by Mukerjee & Dey (p. 468).

## APPENDIX B

### EXCISE POLICY AND ADMINISTRATION

§ 1. *Indian Excise Policy*: The beginnings of the Indian excise policy and administration can be traced to the Bengal Abkari Regulations of 1791, 1793 and 1800, under which a system of licensing of liquor shops and regulation of the hours of sale of country liquor and harmful drugs was introduced. In the course of the next few decades, there grew up diverse systems of excise administration in the several Provinces. In the interest of uniformity the Government recommended the adoption of the "Central Distillery System" in all Provinces, and this was approved by the Bengal Excise Committee (1883-84), which also favoured the policy of raising the price of liquor and fixing a minimum price for each district. In the meanwhile the Government's policy in the matter of liquor control was criticised by men like R. C. Dutt, K. C. Sen and G. K. Gokhale, who deplored the growing drink habit among the Indians. Similarly, the Anglo-Indian Temperance Association, of which the moving spirits were Mr. Samuel Smith, M. P., and Mr. W. S. Caine, roundly accused the Government of deliberately encouraging the consumption of liquor in order to increase the revenue from excise. These criticisms led the Government to make a clear statement in regard to the nature and aims of their excise policy. This was done in their Despatch No. 29 dated 11th February, 1890, which discountenanced the policy of complete prohibition, firstly, because it would constitute an "intolerable interference with the liberty of the subject," and secondly, because it would be difficult to enforce owing to the vast possibilities of illicit production which the country offered. The *Despatch*, however, recognized the need for restricting consumption of liquor and harmful drugs through such measures as high taxation and restriction of the number of shops and hours of sale. The policy laid down in the *Despatch* of 1890 was, however, criticised in a noteworthy Memorandum (1904) by Sir Frederick Lely, Member of the Governor-General's Council. Government, thereupon, decided to submit the whole question of excise policy and administration to expert examination, and appointed the Indian Excise Committee in 1905 for the purpose. In their Resolution appointing the Committee, the Government restated the aims of their excise policy in clear terms. The Resolution said:

"The Government of India have no desire to interfere with the habits of those who use alcohol in moderation; that is regarded

by them as outside the duty of Government, and it is necessary, in their opinion, to make due provision for the needs of such persons. *Their settled policy, however, is to minimize temptation to those who do not drink, and to discourage excess among those who do; and to the furtherance of this policy, all considerations of revenue must be absolutely subordinated.* The most effective method of furthering this policy is to make the tax on liquor as high as it is possible to raise it without stimulating illicit production to a degree which would increase instead of diminishing the total consumption, and without driving people to substitute deleterious drugs for alcohol or a more or less harmful form of liquor. Subject to the same considerations, the number of liquor-shops should be restricted as far as possible, and their location should be periodically subject to strict examination with a view to minimize the temptation to drink, and to conform as far as is reasonable, to public opinion. It is also important to secure that the liquor which is offered for sale is of good quality and not necessarily injurious to health."

The Indian Excise Committee was asked to examine the excise administration of each Province and to consider how far it was calculated to give effect to the policy laid down. The Committee was also asked to study the problem of enhancing the rates of taxation on country liquor with a view to discouraging its consumption. In their report the Committee observed that the causes affecting the consumption of liquor were many and various—climate, race, religion and caste, occupation, the degree of civilization, etc., all affected the degree of drunkenness in a community. As far as systems of excise administration had any bearing on consumption, they observed that the Central distillery system, as against the "outstill" or farming system, had a general tendency towards discouraging consumption. The Committee also recommended the raising of the rate of duty on country liquor without giving rise to illicit distillation, and proposed the entire prohibition of the sale of liquor to sailors and soldiers, policemen, railway servants on duty and to persons below the age of fourteen.

After this Report was published, various deputations waited on the Secretary of State and on the Governor-General pleading for a restrictive policy in excise matters. In 1913 the Government of India in a circular to the Provincial Governments reiterated their policy and indicated the following measures for its furtherance:

- (1) Every effort should be made to suppress illicit methods of all kinds;

- (2) in order to effect this, the excise staff should be utilized in directions calculated to maintain the closest possible control and supervision over the liquor and drugs traffic, and their work should be facilitated by the adoption, where feasible, of the contract-distillery, in lieu of the outstill system;
- (3) as far as is possible, without unduly encouraging illicit methods, consumption should be discouraged (a) by the levy of as high a rate of duty as is possible, taking into account the special conditions obtaining in the locality and in the neighbourhood; (b) by reducing, as far as possible, and with due regard to legitimate requirements, the number of retail shops for the sale of liquor and drugs; (c) by regulating and closely supervising the hours of sale, the selection of sites, and the general practice adopted in manufacture and vend.
- (4) advisory committees should be appointed where possible, and effect should be given to their recommendations in so far as they are consistent with the general principles now laid down."

Later, the Secretary of State commended the Government of India's excise policy of raising "maximum revenue from minimum consumption."

§ 2. *Excise Policy and Administration in the Bombay Presidency:* At the beginning of the nineteenth century, the excise system of Bombay was that of "farming" the taxes on liquor and toddy. In 1808, this system was abandoned in favour of a tax on "stills" of liquor levied by the Government. The administration of this tax, however, proved to be difficult, and, in 1816, it was replaced by "the sudder distillery system" under which the Government provided walled space within which the Bhandarees were allowed to erect "stills" on payment of the tax. By the Regulation of 1827, however, the "farming" or outstill system was re-introduced. "This system consisted in giving the excise revenue of a particular area in farm to the person willing to pay the highest price for it. He was allowed to set up stills at specified places and distill and sell liquor as he liked. There was no restriction on the strength or price of the liquor and no adequate supervision."<sup>1</sup> In the absence of any restriction on price or production, the outstill system was worked by the "farmers" in such a way as to lead to increased consumption.

<sup>1</sup> *Reviews of the Administration of the Bombay Presidency, No. VXXII, Excise and Minor Ports, 1933, p. 24.*

This evil result of the system was brought to the notice of the Government by a number of officers and Committees during 1827-1878.

The farming system, however, continued till 1878, when a new system was introduced by the Indian Abkari Act. It came to be known as the "District Monopoly System" with "a minimum guarantee." Under this system the right of manufacturing country liquor came to be sold to contractors who carried on production under Government supervision, and paid a duty on each "still." The right of retail vend was auctioned out in each locality, the vendor being bound to obtain his supplies from the contract distilleries at fixed rates. The auction system, however, was found to give rise to several evils; among others, it transferred the control of liquor taxation from the Government to the speculators. The Bombay Government, therefore, adopted in 1912 the system of fixed fees for the licence of retail sale, along with the fixation of maximum selling prices. This system also encouraged unfair dealings on the part of licensees, who made large profits and used a part of them for bribing the excise staff. Later, therefore, this system was replaced by the Madras system of three-yearly auctions. In the meanwhile, attempts were made to restrict consumption by reducing the number of shops, hours of sale and strength of the liquor. The Government, however, were not prepared to adopt prohibition by "local option," i. e., by ascertaining popular opinion in a locality.

§ 3. *Excise Policy Under the Reforms:* Opinion in the Reformed Legislative Council was strongly in favour of Prohibition. It was widely felt that the policy of "maximum revenue from minimum consumption" had not proved sufficiently restrictive; in fact with total and per capita, consumption had actually increased during the fifteen years prior to the inauguration of the Reforms. The Indian Taxation Inquiry Committee (1926) gave the figures as in Table No. 29.

The Government also realised the need for a more restrictive policy, as shown by the following pronouncement of Sir C. V. Mehta, Minister for Excise, in the first session of the Reformed Legislative Council: "It has always been the settled policy of this Government to check the growth of consumption by means of these measures (viz., reducing the number of shops and hours of sale, reducing the strength of the liquor, raising its price by high taxation, etc.) without regard to Provincial revenues. An extension of the policy is now called for, and some direct action is, I think,

TABLE NO. 29

**INCREASE IN THE CONSUMPTION OF LIQUOR AND  
EXCISE REVENUE**

	Population in 1,000	Percentage Increase in Population	Consump- tion in 1,000 Gallons	Percentage Increase in Consump- tion	Revenue in 1,000 Rs.	Percentage Increase in Revenue
1906-07	13,100	—	2,092	—	8,426	—
1919-20	13,669	+4	2,281	+9	22,359	+166

necessary. I do not propose to place any definite scheme before the Council, but I can say that a system of rationing shops is being investigated. The figures of the latest year will be taken as the maximum and no more supplies will be issued. . . . If people have been satisfied to drink a certain quantity, that quantity shall not be increased, and may be curtailed periodically as experience shows."

This policy of rationing was implemented by the following Resolution of 1922: "All country spirit shops should be rationed on the basis of the consumption for the year 1920-21. From that consumption reduced to proof gallons, 10 per cent should be deducted in the case of shops in the Bombay City and 5 per cent elsewhere to arrive at the ration. The quota of each shop should be fixed monthly, and will be the amount (in proof gallons) supplied to that shop in the corresponding month of 1920-21 as shown in the warehouse or distillery accounts, *minus* 10 or 5 per cent as mentioned above."

Though the Government had accepted this policy of rationing, it was felt by many that it was high time the whole excise policy was reviewed with special reference to prohibition by "local option" and other measures. For this purpose the Bombay Excise Committee (1922-23) was appointed with Rao Bahadur Sathe (later, Mr. C. M. Gandhi) as President. The Committee condemned the Government of India's policy as laid down in the despatch of 1905, and observed that the total abolition of the drink evil should be aimed at. It said: "The policy which Government should, in their opinion, lay down in the future, and with as little delay as possible, should be to aim at the total extinction of the consumption of all alcoholic drinks, including toddy, by suitable steps. . . . If prohibition is finally adopted throughout the Province, its

benefits will be incalculable when one considers that the coming generation of young people will not know from personal experience or observation what a liquor shop is. It will remove temptation from grown-up men who are now unable to resist."<sup>2</sup> In another place, it said: "The Committee does not believe that the attempt gradually to restrict and in due course stop entirely the consumption of liquor will create discontent among the drinking classes or alienate their good will; nor do they believe that prohibition of liquor will lead the people to more harmful drugs, especially if the latter are also prohibited as will be proposed hereafter."<sup>3</sup> One of the steps towards complete prohibition, as recommended by the Committee, was "local option," under which the people of a locality would be given the right to decide that liquor traffic should be stopped. The Committee also favoured the adoption of the "rationing" system, and advocated that it should be extended to foreign liquor also, if it was to serve any useful purpose.

The Government in 1924 accepted the policy of gradual prohibition. This raised the question of finding out an alternative source of taxation to replace excise revenue. The Bombay Excise Committee (1922-23) had considered the question of finance, and it had come to the conclusion that ultimately a sum of Rs. 3 crores would have to be found in order to implement the policy of prohibition. The Committee had suggested the following new sources of revenue for the purpose:

	Lakhs of Rupees
(1) Succession Duty	50
(2) Betting Tax	20
(3) Taxation of "Future" Dealings	50
(4) Increase of Local Fund Cess	30
(5) Employee Tax	40
(6) Tobacco Tax	5
(7) Transit Tax	20
(8) Terminal Tax	50

It was felt, however, that the Committee had underestimated the loss on account of prohibition. Again, the last two of the new sources of taxation suggested by the Committee were condemned by the Taxation Inquiry Committee. Obviously, the whole question of finance needed expert examination and the Legislative Council promptly voted in favour of a Resolution moved by Mr. R. G. Pradhan in November 1925 to the effect that "a Committee be

<sup>2</sup> Report, Vol. I, p. 78.

<sup>3</sup> Report, Vol. I, p. 65.

appointed to consider and report on the financial measures that should be introduced in order to give full effect to the policy of prohibition of the traffic in alcoholic drinks and drugs." In accordance with this resolution, the Prohibition (Finance) Committee was appointed in 1926.

The Committee estimated that the direct loss on account of prohibition, viz., loss of excise revenue, would be about Rs. 4 crores. As regards the indirect loss in the form of additional expenditure for preventive establishment, the Committee put down the figure of Rs. 1½ to 2 crores, though some officers like Messrs. Ghosal and Clifford made a much higher estimate. The new taxation measures suggested were:

	Lakhs of Rupees
Succession Duty	100
Irrigation Cess	30
Tax on Exchange Transactions	54
A Tax on Tobacco	30
A Tax on Patent Medicines	10

In addition to these, the Committee recommended that the Bombay Government should obtain Rs. 50 lakhs more from income tax as a result of the modification of the Meston Settlement, and it would save Rs. 56 lakhs when the Provincial Contributions were stopped. The total additional revenue required, therefore, would be Rs. 3.30 crores.

The report of the Prohibition (Finance) Committee was an eye-opener to many enthusiastic supporters of the policy of prohibition. It brought into bold relief the magnitude of the financial problem which the Province would have to face if complete prohibition were to be enforced. It would appear that since the publication of the report, the Government of Bombay also revised its attitude towards the policy of prohibition. It accepted the Committee's estimate of the total loss on account of prohibition and calculated that the revenue derivable from additional taxation would not, on a liberal estimate, exceed Rs. 2 crores. In their Memorandum to the Indian Statutory Commission (p. 360) the Government of Bombay observed: "... in the present financial condition the Government must consider what further outlay in the same direction can be made, especially when the amount that can be made available for the purpose falls short by four crores of the full amount which, it has been estimated, is required to make the policy a complete success. In the circumstances, Govern-



ment, while not abandoning the hope of eventually attaining total prohibition, are forced to the conclusion that, as the path is beset with difficulties which for the present are insuperable, progress must necessarily be slow. Government intend to adhere to the policy of rationing, but the time and stages of further reduction must be judged according to the circumstances of each year."

This changed attitude towards prohibition was generated by administrative difficulties as well. These were particularly stressed by the Commissioner of Excise in his Annual Report for the year 1926-27. The Commissioner, Mr. Ghosal, while admitting that the consumption of licit spirit had steadily decreased since the adoption of rationing, observed that the consumption of foreign spirit and fermented liquor had increased by 15 and 29 per cent during 1923-26. At the same time, the use of illicit liquor was on the increase as shown by the growing number of excise offences. The Excise Commissioner concluded: "The difficulties in this Presidency of enforcing prohibition are really stupendous and difficult to realise. The bases for illicit distillation are available everywhere, and the facilities for importation of illicit liquor enormous. Detection of crime is also extremely difficult. So long as these conditions exist, the reduction in the supply of licit liquor or the raising of prices will not solve the difficulties."<sup>4</sup>

In view of these administrative difficulties the Government decided to stop the progressive reduction of the ration with effect from 1st April, 1928. In some districts the ration was actually raised, additional liquor shops opened, and the strength of the liquor increased. This policy was definitely adopted later, upon the recommendations of the Excise Conference of September 1931.

Let us now review the general results of the excise policy during 1922-1930. In the first place it should be noted that during these eight years there was effected a fair reduction in the consumption of most types of liquor, though there was an increase in a few cases. Table No. 30 is taken from the official publication, *The Financial Position of the Government of Bombay*, (p. 29). While, however, there was progressive reduction of licit consumption, there was a fairly large increase in illicit consumption, as shown by the rise in the excise offences. (Table 31.)

There was, further, some reason to believe, as pointed out by several Commissioners of Excise, that the proportion of detected

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<sup>4</sup> Administration Report of the Excise Department, 1926-27, p. 20.

TABLE NO. 30

**CONSUMPTION OF LIQUOR AND INTOXICATING DRUGS  
(1922-23 AND 1929-30)**

	Presidency Proper		Sind	
	1922-23	1929-30	1922-23	1929-30
	Gallons	Gallons	Gallons	Gallons
Country Liquor	1,791,898	1,288,907	133,290	108,061
Toddy	12,772,591	12,465,156	8,427	21,934
<b>Foreign Liquor:</b>				
(1) Fermented Liquor	890,559	1,023,899	238,206	371,266
(2) Wines	85,450	44,207	9,157	10,095
(3) Potable Spirits	432,077	295,409	40,055	53,863
(4) Denatured Spirits	525,007	231,016	92,000	22,589
<b>Intoxicating Drugs:</b>				
	Sears	Sears	Sears	Sears
(1) Ganja	44,602	31,584	1,118	500
(2) Bhang	8,989	7,902	104,985	72,723
(3) Opium	28,292	21,330	6,086	5,096
(4) Charas	—	—	5,053	6,964

TABLE NO. 31

**OFFENCES AGAINST ABKARI AND OPIUM LANDS IN THE  
BOMBAY PRESIDENCY**

(Source: Excise Administration Reports.)

		Offences to Relating Liquor	Offences to Relating to Hemp Drug	Offences to Relating to Cocaine	Opium
1922-23	Presidency Proper	3,458	161	360	239
	Sind	102	66	5	27
1929-30	Presidency Proper	5,259	742	115	366
	Sind	114	257	3	71

to undetected offences had increased. In the meanwhile, the expenditure on the excise administration increased from Rs. 16.2 lakhs (1922-23) to Rs. 26.1 lakhs (1929-30).

§ 4. *Excise Policy During the Depression:* As already pointed out,<sup>5</sup> the world economic depression began to affect Bombay's finances from the year 1930-31. Among the revenues which suffered, the most important was excise, which is peculiarly sensitive to changes in people's incomes. Again, the decline was also due to the Congress movement of "picketing" liquor shops which was in full force at about this time. In the pre-depression year (1929-30), the excise revenue was Rs. 400 lakhs; in 1930-31, it fell to Rs. 297.4 lakhs, but recovered subsequently as the figures in Table No. 32 show:

TABLE NO. 32

## EXCISE REVENUE

(Source: Bombay Budgets.)

(In Lakhs of Rupees)

1929-30	1930-31	1931-32	1932-33	1933-34	1934-35	1935-36
400.2	297.4	321.2	329.8	343.2	312.13	333.47

We have noted that since 1928 the Government had started relaxing the rationing policy adopted since 1922. The rationing system was, of course, continued, but the rations were fixed not as a percentage reduction of the amount consumed in 1920-21, but on the basis of consumption of the year 1926-27. By 1930, however, it appeared to the Government that in view of the enormous decline in revenue, the whole policy needed to be reviewed in all its aspects. In September 1931 an Excise Conference was convened by Sir Rafiuddin Ahmed, the Minister for Excise, to discuss the following questions: (a) "The fall in excise revenue concurrently with the increase in the consumption of illicit liquor; (b) the steps to be taken to remould the excise policy which has led to the result indicated in (a); and (c) the administrative measures necessary to carry out the policy that might eventually be decided on."<sup>6</sup> The main tenor of the recommendations of the Conference was the relaxation of the restrictive policy, especially in those areas where it had led to an increase in illicit distillation. Among the important recommendations accepted by the Government may be mentioned:

<sup>5</sup> Chapter VI.<sup>6</sup> *Reviews of Administration, No. XVII, Excise and Minor Ports, p. 19.*

(i) Additional liquor shops should be opened where facilities for illicit distillation and importation exist if the existing shops are too far apart. (ii) In areas where there are complaints about monopoly, more shops should be opened. (iii) Wherever the strength of the liquor is so low as to drive the people to purchase foreign liquor or illicit liquor, the strength should be increased. (iv) Cheap liquor should be provided in all border and criminal areas by reducing the still-head duty. In such areas restrictions on the number of shops, strength of liquor and hours of sale, should be relaxed. (v) Measures should be taken to prevent the use of denatured spirit for potable purposes.

§ 5. *Excise Policy Under Provincial Autonomy:* The prohibition question attained new importance with the inauguration of Provincial Autonomy. The Interim Ministry headed by Khan Bahadur Cooper had given prohibition an important place in their programme. With the Congress Ministry, it became the very basis of social and economic policy. In his first budget speech the Finance Minister declared on behalf of the Government: "We... are irrevocably committed to a policy of prohibition... We are not very much deterred by the loss of revenue which prohibition involves."

The course of the prohibition policy and its financial consequences are set below:

(a) The Finance Minister in his first budget speech announced the intention to constitute certain experimental "dry areas," viz., Ahmedabad City, Cantonment and adjacent villages. In 1938-39 the prohibition programme was considerably pushed forward. The "dry-area system" was further extended to cover a number of rural talukas, e. g., Jambusar, Wagra, Newasa, Shegaon, Panthardi Mahal, Ankola and Kumta. A total prohibition scheme was launched in Bardoli and part of the Mandvi Taluka in Surat District. The loss of revenue on account of these measures was Rs. 31.62 lakhs.

In 1939-40 the Finance Minister announced his intention to extend prohibition so as to involve a loss of revenue of the order of Rs. 150 lakhs. For this purpose the Government issued a Notification under the Abkari Act (1876).

In 1939-40 the Ahmedabad "dry area" was converted into a prohibition area," which later was extended from 1st August, 1939, to the rest of Daskroi taluka. Similarly prohibition was

introduced in the town and island of Bombay, Bombay Suburban district and that part of the Thana Mahal which is encircled by the Bassein-Thana creek from 1st August, 1939.

At this stage it is necessary to explain the nature of the two schemes, viz., "the dry area" and "total prohibition." Under the "dry area" or "no-licence scheme, "no sale of alcoholic liquors, opium and drugs is permitted in certain specified areas, and the possession therein of these articles is restricted to a low limit. It is not, however, contemplated that their consumption should be entirely prohibited at once. A beginning is made in these areas by enforcing their cessation indirectly, by making it difficult for persons to obtain them. There is, thus no prohibition against persons who may desire to consume alcoholic liquors or drugs proceeding outside the "dry area," purchasing their requirements and bringing them back in a strictly limited quantity within the "dry area." It is anticipated that the trouble and expense caused by this procedure will normally induce the consumer at least to restrict this consumption considerably.

The scheme has the further object that, whereas under Total Prohibition a local demand can only be satisfied illicitly and without the cognizance of the authorities, under the Dry Area Scheme the local demand would probably to a large extent be satisfied licitly. Thus, by watching the sales of liquor and drugs at shops surrounding the "Dry Areas," Government is able to gauge what is that demand for stimulants and narcotics which is so insistent as not to be deterred by the trouble and expense of importing from outside; and it is this demand of which Government must take account as one for which special provision in preventive arrangements will have to be made when Total Prohibition may be introduced in that area. On the other hand, where it may be found that the sales at the surrounding shops increase very little, Government will be able to assume that in future Total Prohibition can be enforced there with little difficulty."<sup>1</sup>

From the above it will be clear that the Dry Area Scheme is intended to be the first step towards total prohibition. It is frankly of an experimental character, upon the results of which in particular areas, the feasibility of total prohibition would depend. Under the latter, (i) "no country liquor, toddy, wines, spirits, beer, opium or hemp drugs in any quantity whatever may be imported into or possessed within the area by any person"<sup>2</sup>

<sup>1</sup> A Review of the Progress of the Rural Dry Area Schemes in the Province of Bombay, 1938, pp. 1, 2.

<sup>2</sup> Review of the Progress of the Total Prohibition Scheme, 1938, p. 5.

There are, however, exceptions in the case of travelling passengers, Government, hospital and dispensaries, churches, etc. (ii) (a) *Drakshasavas* and other *Asavas* containing spirit; (b) Spirituous preparations and tinctures, and (c) Denatured spirit, are permitted to be imported or transported or possessed in small quantities, the first two under a prescription from a local Registered Medical Practitioner, or practitioner approved by the Collector. (iii) The sale of wine, *Drakshasava* and brandy as also *ganja*, *bhang*, and opium, etc., is permitted to licensed chemists and other dealers on medical prescription. (iv) No licences for the tapping of toddy are granted, except for the purpose of the manufacture of "gul."

The dry area and total prohibition schemes were declared to be successful by the Commissioner of Excise. In his "Review of the Progress of the Rural Dry Area Schemes" (June 1938), the Commissioner observed: "In conclusion it can be said that the Rural Dry Area experiment is so far showing good results in all areas except the coastal portion of Kanara District. It is difficult to estimate precisely how far the reduction in consumption of excisable articles has resulted in the improvement of the economic and social conditions of the people, but clearly its effects cannot be other than beneficial." Similarly the same authority concluded his "Review of the Progress of the Total Prohibition Schemes" in Bardoli taluka and elsewhere in the following words: "On the whole the experiment of Total Prohibition in Bardoli and the five villages of Mandvi may at present be definitely said to be successful and Government have under consideration its extension to Valod Mahal."

§ 6. *The Financial Consequences of Prohibition:* The financial consequences of prohibition in the long run depend upon its economic effects. The general nature of these latter efforts has been examined by a number of economists including Feldman<sup>9</sup>, Carver,<sup>10</sup> Clark Warburton,<sup>11</sup> and Stamp.<sup>12</sup> All these writers have concluded that prohibition, by causing a healthy transference of consumption, tends to have a favourable effect on efficiency and employment. Similar conclusions have been arrived at by Prof.

<sup>9</sup> Feldman: "Prohibition: Its Economic and Industrial Effects."

<sup>10</sup> J. N. Carver: "Prohibition and Liquor Control."

<sup>11</sup> Clark Warburton: "The Economic Effects of Prohibition."

<sup>12</sup> Stamp: "Alcohol as an Economic Factor" (in "National Capital and Other Statistical Studies.")

P. J. Thomas<sup>12</sup> who has studied the effects of the prohibition experiment in the Salem District of Madras. If we accept these conclusions, then we have to agree that prohibition may not involve a net economic loss in the long run.

But such a conclusion is no solace when we are faced with the budgetary problem which it creates. The Congress programme launched in 1939-40 meant a financial loss of nearly Rs. 1.5 crores. This loss would, no doubt, have mounted to nearly Rs. 5 crores when prohibition would become operative over the entire Province.

Let us, for the time being, focus our attention on the 1939-40 programme and its financial consequences. In regard to this, criticism was made in three directions. Firstly, it was argued by some that the financial sacrifice was worthy of a better cause. It was felt, for instance, that this huge sum could have been utilized on certain more urgent measures of relief and reform, such as reduction of land revenue, expansion of compulsory and voluntary primary education, rural development, sanitation and a number of others. It is true that an economist cannot prove the superior worthiness of these alternative lines of economic reform; but commonsense and practical wisdom may have a good deal to say in the matter.

Again, some criticised the Congress Ministry for having adopted unsound measures for making good the loss on account of prohibition. It was obvious that a loss of the magnitude of Rs. 1.50 lakhs must necessitate drastic measures of additional taxation. In fact, it would have justified a thorough-going inquiry into the incidence of taxation among different social classes and productive groups, with a view to framing a comprehensive policy of tax reform. But the Congress Ministry did nothing of the kind. Their most productive tax was the Urban Property Tax, of which the incidence is upon one type of property owners, viz., those who have real property in cities like Ahmedabad and Bombay. The other tax measures, viz., the enhanced electricity duty, tax on prize-competitions, etc., are of minor importance, compared with the magnitude of the financial loss occasioned by prohibition.

Granting the superiority of prohibition as a social aim over other measures like primary education, rural development, etc., and granting that the financial loss occasioned by it could be made good by appropriate measures of taxation, the question might still be asked whether the money spent on prohibition did

<sup>12</sup> Thomas: "Prohibition in the Salem District of the Madras Presidency."

achieve any concrete results. Here one is faced with the difficult task of judging the degree of success attained in curbing the drink habit in the prohibition and dry areas. The Report of the Excise Department for the year 1939-40 admits that considerable difficulties had to be faced in preventing illicit production and importation of country liquor and harmful drugs. Such difficulties are inevitable in a province in which several Indian States are interspersed.



TABLE NO. 33

RECEIPTS UNDER PRINCIPAL HEADS OF REVENUE OF  
THE BOMBAY GOVERNMENT DURING 1921-22 TO 1935-36

(Source: Bombay Budgets, 1935-36 and 1937-38.)

(In Lakhs of Rupees)

Heads of Revenue	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	1934-35	1935-36
Taxes on Income	14.6	3.0	—	—	—	—	—	—	—	—	—	—	—	—	—
Land Revenue	437.2	446.7	398.9	405.8	428.8	354.3	410.3	386.9	381.8	385.2	396.9	374.2	384.6	340.86	374.35
Excise	342.7	422.8	434.6	443.0	395.0	337.2	384.1	383.4	400.2	297.4	321.2	329.8	343.2	312.13	333.47
Stamps	164.4	176.6	179.9	178.1	176.3	167.6	175.4	168.4	177.2	158.1	150.3	158.8	156.4	139.52	142.77
Forest	74.9	70.4	71.5	73.1	75.3	76.6	72.9	73.4	79.8	52.2	56.7	59.7	54.3	48.31	52.10
Registration	13.5	13.0	12.9	12.5	12.8	12.0	11.8	11.8	12.3	10.9	11.4	12.5	16.2	14.39	15.58
Scheduled Taxes	—	2.7	9.4	9.0	15.3	19.6	21.2	21.5	20.1	16.4	19.2	18.8	19.1	17.15	19.24

TABLE NO. 34

## PRINCIPAL HEADS OF EXPENDITURE OF THE BOMBAY GOVERNMENT FROM 1921-22 TO 1935-36

(Source: Bombay Budgets, 1935-36; and 1937-38.)

(In Lakhs of Rupees)

Heads of Expenditure	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	1934-35	1935-36
1. Land Revenue and General Administration	193.4	191.2	187.2	186.7	192.8	192.0	180.0	180.4	192.2	191.3	191.2	173.7	171.5	154.1	148.1
2. Justice	70.1	65.6	68.9	71.4	72.7	74.1	73.3	72.9	75.3	74.6	70.6	64.2	66.6	58.9	61.1
3. Police	186.7	168.5	166.7	169.0	169.4	167.1	164.8	166.6	172.9	189.1	178.4	174.9	173.1	199.9	141.3
4. Education	171.7	171.1	191.8	184.0	195.8	199.6	201.9	197.8	206.2	206.4	194.1	173.6	179.8	153.3	154.0
5. Medical	45.1	44.4	43.2	43.9	47.2	49.9	46.4	46.3	46.3	45.3	42.2	37.9	37.7	41.2	41.4
6. Public Health	28.8	17.4	19.4	22.3	24.6	20.0	21.8	23.0	23.6	21.2	18.6	18.3	18.4	24.3	22.9
7. Agriculture	29.3	23.4	23.8	26.1	26.8	26.9	27.4	28.3	29.2	28.8	27.7	24.2	24.8	21.9	23.6
8. Industries	7.6	2.7	1.5	0.2	0.7	0.9	0.7	0.8	1.1	1.2	1.2	3.4	3.5	4.8	6.0
9. Civil Works	203.0	114.3	108.9	102.9	110.3	141.1	122.6	116.0	110.8	107.3	90.7	72.4	76.1	78.2	85.8
10. Superannuation Allowances and Pensions	48.5	32.3	37.8	30.9	36.3	33.7	31.9	34.3	36.7	31.2	32.3	39.1	33.8	37.9	101.7
11. Contribution to the Central Government	36.0	36.0	36.0	36.0	34.0	28.0	—	—	—	—	—	—	—	—	—

TABLE NO. 35

## REVENUE RECEIPTS OF THE BOMBAY GOVERNMENT FROM 1936-37 TO 1945-46

(Source: Bombay Budgets, 1942-43, and 1945-46.)

(In Lakhs of Rupees)

	1936-37	1937-38	1938-39	1939-40	1940-41	1941-42	1942-43	1943-44	1944-45	1945-46
1. Taxes on Income Other Than Corporation Tax	—	25.00	30.00	55.80	83.20	147.80	218.00	390.00	Revised 331.20	Budget 465.80
2. Land Revenue	344.32	319.65	354.62	343.20	345.54	394.57	406.63	321.51	385.35	381.06
3. Provincial Excise	325.29	321.73	289.77	202.13	221.12	270.95	375.25	535.73	689.50	650.00
4. Stamps	146.99	154.92	144.36	138.93	146.49	162.14	170.20	244.79	271.68	260.12
5. Forest	47.72	43.15	40.60	38.61	44.54	69.76	113.10	219.38	287.46	159.56
6. Registration	15.05	15.25	14.41	13.77	15.02	16.88	20.93	26.90	28.66	26.61
7. Motor Vehicles Acts	41.07	43.69	45.39	41.78	49.72	45.24	43.40	48.38	54.64	46.90
8. Other Taxes and Duties	48.65	53.24	63.96	194.03	235.17	216.30	228.59	330.97	431.74	397.59
9. Irrigation, Navigation, Embankment, and Drainage Works	20.06	22.88	21.99	32.13	40.56	55.54	48.60	41.77	50.28	59.20
10. Debt Service	93.34	72.12	72.21	71.03	70.55	68.69	70.61	65.33	63.16	63.04
11. Civil Administration	89.56	90.53	91.85	110.31	128.96	134.95	160.42	195.00	301.79	373.14
12. Civil Works	38.82	58.09	48.37	48.92	46.09	79.38	80.19	55.67	56.26	55.03
13. Miscellaneous	17.77	22.91	20.27	20.45	19.33	23.11	33.61	30.98	34.89	24.99
14. Extraordinary Items	12.74	0.63	6.84	3.14	2.85	1.08	0.78	14.14	5.76	6.15
Total Revenue	1,241.40	1,243.81	1,244.59	1,314.23	1,448.24	1,686.39	1,970.31	2,520.55	3,212.37	2,909.19

1947

THIS publication is in a sense a continuation of the earlier publication on the same subject, *Federating India*. It carries the discussion of Indian constitutional and political problems a step in advance and discusses developments subsequent to the publication of the earlier book in May 1945. The publication was almost ready for the press by the middle of February, 1947. It therefore reflects and analyses the political situation as it existed on the eve of the announcement by His Majesty's Government of 20th February, 1947, with special reference to the statement of 16th May, 1946, of the Cabinet Delegation and the Viceroy and the subsequent controversies. It deals with all the four important aspects of the Federal problem in India, viz., (1) the incorporation of the Indian States within the Indian Union; (2) the composition of federating units, (3) the division of powers between the Government of the Federation and those of the federating units and (4) the problem of the relations between the two major communities brought to a head by the Muslim demand for a separate state. The last overshadowed all others in political debate in recent years. Consequently it is treated in special detail in this publication. Even when the decision to form two separate states from among British Indian Provinces takes away some of the immediate significance of part of this discussion, it may not be found unhelpful for an understanding of the continuing problems. Though a decision has been taken regarding the division of the country, all the other constitutional problems discussed in this publication still remain with us. The problem of the incorporation of Indian States and the composition of federating units now take the leading position. The problem of the powers of the Union assumes crucial importance in relation to the incorporation of Indian States within the Union. All these problems are dealt with in detail in this publication which offers an integrated solution for all of them.

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12. Congress, Pakistan and Constituent Assembly
13. Constituent Assembly and Indian States

(Statistical tables regarding linguistic Provinces, and a map showing their boundaries.)

**Publications of the Gokhale Institute of Politics and  
Economics, Poona 4**

- No. 1: The Salaries of Public Officials in India—By D. R. Gadgil, 1931. (Out of Print.)
- No. 2: Imperial Preference for India. (The Ottawa Agreement Examined)—By D. R. Gadgil, 1932. (Out of Print.)
- No. 3: A Survey of the Marketing of Fruit in Poona—By D. R. Gadgil and V. R. Gadgil, 1933. (Out of Print.)
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- No. 9: Regulation of Wages and Other Problems of Industrial Labour in India—By D. R. Gadgil, 1943. Price Rs. 5 or 10s.
- No. 10: War and Indian Economic Policy—By D. R. Gadgil and N. V. Sovani. Demi 8vo. Pp. 160. (Second Edition, 1944.) Price Rs. 7-8-0 or 15s.
- No. 11: The Aborigines—"So-Called"—and Their Future—By G. S. Ghurye, Professor and Head of the Department of Sociology, University of Bombay. Demi 8vo. Pp. 232. Price Rs. 8 or 16s.
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- No. 13: Federating India—By D. R. Gadgil, 1945. Demi Pp. 108. Price Rs. 6 or 12s.

**Forthcoming Publication**

Poona: A Socio-Economic Survey: Part II—Sociological, (in Preparation).

**R. R. Kale Memorial Lectures**

- 1938: The Social Process—By Dr. G. S. Ghurye, Professor of Sociology, Bombay University. Price, As. 8.
- 1939: Federation Versus Freedom—By Dr. B. R. Ambedkar, M.A., Ph.D., D.Sc., M.L.A., J.P., Bar-at-Law. Price, Re. 1.
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