

## FEDERAL FINANCE

Let us now consider the financial aspects of the new Constitution. Though dealing mainly with the constitutional side, as Finance is an important clog in the smooth working of the Constitution, it would not be possible always to avoid the *financial* aspect proper in the discussion that follows.

Part of the constitutional aspect has already been considered in the volume on **Provincial Autonomy**, and so, we shall avoid going over the same ground in this work as far as possible.\*

We shall attempt in this chapter:

- (1) a general review of the resources of the Federal Government, as provided for in the several clauses of the Act of 1935, and the Instruments of Accession with the several Federated States, as also under such arrangements as have been made by Orders-in-Council, like that recommended by Sir Otto Niemeyer.
- (2) review of the obligations or items of expenditure, imposed upon the Federal Government by the Constitution, and the various Orders of Instruments thereunder.
- (3) the constitutional aspect of borrowing, including the treatment of the existing

\*A proper, logical, comprehensive consideration of the financial aspects of the entire Constitution would be better achieved if the entire Constitution was studied in one work. For reasons explained in the Preface to **Provincial Autonomy**, circumstances have necessitated a separate treatment of the financial aspects of the Federal and the Provincial Governments. A certain amount of repetition or overlapping would be, therefore, inevitable. Wherever possible, however, reference will be made in foot-notes to the volume on **Provincial Autonomy** (Second Edition), with a view to avoid such repetition.

debt and allied obligations, (e.g., in respect of certain Service Funds.)

- (4) A summary of the financial position, its critique, and appreciations of the future trend in matters financial.

No single chapter of the Constitution gives in one place all the financial provisions of the Constitution. Part VII of the Act of 1935 is described by the Act as relating to "Finance, Property, Contracts and Suits." But it does not give all the relevant provisions. Sections of the Act, however, which, directly or indirectly, affect the financial administration of the country, are also to be found scattered in those other parts of the Act which deal with the power of the Governor-General and procedure of the Legislature; the rights and duties of the Public Services; Judicial Department; and the Defence organization.

Financial obligations arising out of the several Reserve Departments, such as that of Defence, External Affairs, Ecclesiastical matters, Excluded Areas and tribal districts, together with the amounts payable under the Constitution to the Representative of the Crown in its relation with the Indian States, federated or not, will also involve a considerable financial strain on the Constitution. The entire Chapter, again, relating to the Indian Railways, comprising Sections 181-199, has profound financial bearing upon the Constitution. Similarly, the provisions in regard to the Secretary of State, his Advisers and department, (Part XI Sections 278 to 284) as well as Section 302 relating to the High Commissioner for India; and 304 and 305 relating to the Acting Governors-General and the Secretarial staff of the same, have financial implications, which

have a considerable significance, upon the working of the Constitution. Lastly, though Burma and Aden have been separated from India, the separation of Burma particularly has an immense financial reaction upon the Constitution and administration of India, which can only be glanced at in the survey that follows.

### I. FEDERAL RESOURCES OF REVENUE

Broadly speaking, the Act of 1935 seeks to make a clear division of resources between the Federal Government, and those of the component units. So far as the Federating States are concerned, their financial obligations will depend, in a large measure, upon the terms of the individual Instrument of Accession of each State. To the extent that the provisions of the Act prescribe these obligations to contribute to Federal resources, they are outlined and critically considered below more particularly. As regards the British Provinces, the division of resources and obligations is more thoroughly attempted in Schedule VII, which, primarily, is intended to provide Lists of Federal, Provincial, and Concurrent subjects for legislation; but which necessarily contain items that serve as excellent subjects for taxation or revenue levied and collected upon the authority of the Federal or Provincial Legislation as the case may be.

#### I

1. Customs Duties, including export duties.
2. Excise Duties on tobacco and other goods manufactured or produced in India except—
  - (a) Alcoholic liquors for human consumption;
  - (b) Opium, Indian hemp and other narcotic drugs and narcotics; non-narcotic drugs;

- (c) Medicinal and toilet preparations containing alcohol, or any substance included in subparagraph (b) of this entry.
3. Corporation Tax.
4. Salt.
5. State lotteries.
6. Taxes on income other than agricultural income.
7. Taxes on the capital value of the assets, exclusive of agricultural land, of individuals and companies; taxes on the capital of companies.
8. Duties in respect of succession to property other than agricultural land.
9. The rates of stamp duty in respect of bills of exchange, cheques, promissory notes, bills of lading, letters of credit, policies of insurance, proxies and receipts.
10. Terminal taxes on goods or passengers carried by railway or air; taxes on railway fares and freights.
11. Fees in respect of any of the matters in this list, but not including fees taken in any court.

### Provincial Government

#### II

1. Land revenue, including the assessment and collection of revenue, the maintenance of land records, survey for revenue purposes and records of rights.
2. Excise Duties on the following goods manufactured or produced in the Province, and countervailing duties at the same or lower rates on similar goods manufactured or produced in India—

- (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 subparagraph (b) of this entry.
3. Taxes on agricultural income.
  4. Taxes on lands and buildings, hearths and windows.
  5. Duties in respect of succession to agricultural land.
  6. Taxes on mineral rights, subject to any limitations imposed by any Federal Legislature relating to mineral development.
  7. Capitation taxes.
  8. Taxes on professions, trades, callings and employments.
  9. Taxes on animals and boats.
  10. Taxes on the sale of goods and on advertisements.
  11. Cesses on the entry of goods into a local area for consumption, use or sale therein.
  12. Taxes on luxuries, including taxes on entertainments, amusements, betting and gambling.
  13. The rates of stamp duty in respect of documents other than those specified in the provisions of List I with regard to rates of stamp duty.
  14. Dues on passengers and goods carried on inland waterways.
  15. Tolls.

16. Fees in respect of any of the matters in this list, but not including fees taken in any court.

Considering these Lists\* in the aggregate, it is impossible not to notice the fact that while all the progressive or elastic and productive sources of revenue are reserved for the Federal Government, all the inelastic and obviously burdensome items are assigned to the Provinces. The only relief to the Provinces—such as it is—is to be found in the terms of Section 138 relating to the division of the Income Tax Proceeds, after a time, between the Units and Federation; and of Section 142, under which certain subsidies are to be paid by the Federal Government to certain Provinces. Both these subjects have been investigated into, and the necessary aid to the Provinces thereunder has been recommended by Sir Otto Niemeyer, whose report has been considered in some detail already in the volume on **Provincial Autonomy** under the new Constitution to which reference may be made.

The provisions of Section 137, requiring uniform taxation, and centralised collection of such items as

- (i) Succession duties to property other than Agricultural Land;
- (ii) Stamp duties mentioned in the Federal Legislative List;
- (iii) Terminal taxes on goods or passengers carried by railway or air; and
- (iv) Taxes on railway fares and freight

\*In the concurrent Legislative List, there are a number of items, which might be utilised for taxation, though it is not clear that the law-making power will also include the power to pass legislation taxing such acts as marriage and divorce (Item VI), wills, intestacy and succession, save as regards agricultural lands (Item VII), or transfer of property and other agricultural lands, (Item VIII) by means of stamp duties or registration fees.



may afford financial aid to the Provinces in the future. But the fact that they are to be imposed and collected by the Federal Government, for distribution of the net proceeds\* among the component units, will not permit the Province to vary the rates, and graduate the burden to the differing abilities of their citizens. This will render Provincial revenue from these sources utterly inelastic, and unsuitable for any ambitious project of social reconstruction or economic development in the Province. Besides, the section reserves to the Federal Government the right to impose a surcharge on all these items of revenue for their own exclusive use. This means that the property, wealth, and business acumen of every Province is, in the ultimate analysis, open to the Federal Government for its own particular, and, generally, unproductive purposes, without any corresponding obligation to contribute directly or substantially towards the economic development of the Provinces. Section 140, holding out a remote, unlikely hope of the Federal Government some day distributing among the component units part of the proceeds of the Salt Duty, Federal Excise and Export Duties,—if an Act of the Federal Legislature authorises it to do so,—is misleading in the very hope it engenders. Viewing the position as it is to-day, there appears no chance of the Federal Government ever having such a superabundance of funds as will admit of this generosity to the Provinces and the Federated States. The only exception to this appreciation of that section may be found in sub-section (2) of that section, which requires one-half or more of the net proceeds of the jute export

\*cp., Section 144.

duties to be distributed among the jute-growing provinces. Sir Otto Niemeyer has recommended that 5/8ths of such proceeds should be made over to those Provinces. It must be admitted that the Provinces of Bengal, Bihar, and Assam have derived substantial aid to their resources from this concession. But, even so, the case of the jute-growing Provinces for the entire proceeds of this export duty should not be lost sight of altogether. Besides, those who endorse the principle underlying that provision in the U. S. A. Constitution, which forbids the Federation to levy any such duty on the product of a State, cannot altogether deny the justice of the claim made on this account by the jute-growing Provinces.

It must also be remembered that, though the list of revenue resources made available to the Provinces under the Act may seem imposing, many of the Provincial items are really made over to the local bodies like Municipalities and District Boards. Section 143 (2) expressly permits these sources of revenue to remain at the disposal of the bodies which now enjoy them, until the Federal (or Provincial?) Legislature may otherwise direct. Even Section 141 is no real protection or safeguard to the Provincial Governments in face of an extravagant or impecunious Federal Government, as is most likely to be the case. For though without the prior sanction of the Governor-General, given in his discretion, no Bill or amendment can be introduced in the Federal Legislature affecting any of the taxes or duties in which Provinces may be interested, or by which they may be affected, (e.g., those succession, stamp or terminal duties on passengers, fares or freight, which are levied



by the Federal Government for distribution among the units, or which impose surcharges on them, or on the Income Tax), that would not necessarily or for ever prevent such proposals being mooted in or passed by the Federal Legislature.

The Governor-General is enjoined, it is true, not to give his prior sanction to any Bill or amendment in the Federal Legislature,

"unless he is satisfied that all practicable economies and all practicable measures for otherwise increasing the proceeds of Federal taxation,..... would not result in the balancing of Federal receipts and expenditure on revenue account.\*

But even that injunction will not always enable him,—even if he is so inclined,—to be an effective protector and guardian of Provincial interests. The reason is quite clear. His primary and Special Responsibility, imposed by Section 12, is to see to the financial stability and credit of India as a whole. Given the present state of the Central finances; and given the nature of the burdens imposed upon the Federation, it is impossible to see how the Governor-General will ever be able to protect or safeguard the interests of the Provinces in this behalf, consistently with his own primary responsibility in that regard. Even when their resources expand, or exceed their obligations, a democratic Federal Government of India may be trusted to discover new and useful channels for additional Federal expenditure, so that no accession to Provincial resources is feasible.

The real position of the Revenues and Expenditure of the Federal Government of India may be appreciated

\*Cp. Section 141 (2).

from the Budget Estimates for the Government of India in 1937-38.\* They provided for a total net revenue, on the then (i.e., the 1st of March 1937) existing basis of taxation, of 79.99 crores; and an aggregate net expenditure of 83.41 crores. This meant a deficit of 3.42 crores. This the Finance Minister proposed to meet partly from the existing revenue reserve (Rs. 184 lakhs), and partly from additional taxation.† But this does not present a complete picture, even though the Niemeyer recommendations in regard to aid to the Provinces had been adopted and acted upon in part, and though settlement with Burma had also been arrived at. The Instruments of Accession with the various States have yet to be executed; and they might affect materially important items of revenue as well as expenditure. Future improvements in revenue are difficult to forecast at the present moment, while room for retrenchment in expenditure is exceedingly limited, if it exists at all, given the meticulously protected position of the services and other vested interests.

The main factors which affected the Central finances, in the Budget for 1937-38, and would continue to affect them even after the Federation comes into existence, may be summarised, in the language of the Finance Member, as follows:—

‡“ But apart from the changes of form, there are two major changes of scope which affect the estimates for 1937-38. I refer, of course, to the separation of Burma and to the Niemeyer

\*See Table appended.

†The sugar excise was increased from Rs. 2/- per cwt., and estimated to yield Rs. 115 lakhs; and the silver duty was raised from annas 2 to 3 per oz. yielding Rs. 50 lakhs

‡Vide Budget Speech of the Finance Member, 1937-38, Para. 12.

Award, including in this term all the other alterations consequent upon the introduction of Provincial Autonomy. The effects of these changes run through practically every head of the Budget.....

From Table I of the Financial Secretary's Memorandum it will be seen that the general effect of the Separation of Burma is a **net reduction of Revenue of Rs. 138 lakhs**, and a net increase of Expenditure of Rs. 92 lakhs—these figures taking no account of a betterment of Rs. 13 lakhs in the net balance of the P. & T. Department. **The net cost of separation is therefore Rs. 233 lakhs.** At this stage I should explain that on the Revenue side we have taken credit for the receipt, under the Amery Award, of

- (i) Rs. 2,29 lakhs in respect of the debt and other liabilities taken over by Burma, and
- (ii) Rs. 94 lakhs in respect of Burma's liability for pensions in course of payment on the 31st March 1937.

Apart from these the net loss on account of separation would be Rs. 5,56 lakhs. Needless to say all these figures are of a provisional character. There are many uncertain factors to be taken into account, particularly under the heads Customs and Taxes of Income; and, moreover, the final material for the calculation of the annuities payable by Burma will not be available until some time after the 31st March.

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**As regards Provincial Autonomy, the net results are a reduction of Rs. 51 lakhs in Revenue combined with an increase of Rs. 1,34 lakhs in Expenditure, i.e., a total cost to the Centre of Rs. 1,85 lakhs.**

The sum of these two figures, viz., Rs. 418 lakhs represent the extra burden on our budget (i.e.,

additional to that assumed in earlier years) arising from the constitutional changes due on 1st April next. The charges assumed in earlier years including the devolution of 50 per cent. of the Jute Duty, and the subventions to the N.W.F.P., Sind and Orissa, amount to more than as much again."

\* \* \* \*

Later on, the same authority observes:

"Have we in the disappointment of the year 1936-37 any reason for doubting the soundness of the conclusions of the Niemeyer Report in regard to the ability of the Centre to bear the cost of the successive stages by which the new Constitution is being introduced? A year ago I prophesied that with the help of a Revenue Fund of Rs. 2 crores, we could see our way through 1937-38, and that thereafter the normal growth of revenue would provide step by step for the liabilities which would come upon us from year to year. Our Reserve Fund has turned out to be somewhat less than we expected, and Revenue has shown a distinct falling off. Contrary to our hopes, therefore, we are between Rs. 1½ crores short of a balance in 1937-38; and unless we assume a growth of revenue during the year greater than we have any right on past experience to expect, this should connote a deficit in 1938-39 too of something like the same amount. Are our calculations then all wrong and, are we pursuing a chimaera in judging that we can finance the new Constitution? I do not think so.

\* \* \* \*

On the whole I do not think that I shall be indulging in unjustifiable optimism if I say, as a result of considering the various factors at work, that there is no reason why the Niemeyer prognostications should not be realised in the long run, and that even in the nearer future his programme can be fulfilled with the help of no more than a very

\*Vide. Budget Speech of the Finance Member, 1937-38, Para. 25.



modest addition to our resources, which I should estimate to be roughly from Rs. 1½ to Rs. 1¾ crores by which we are short of a balance this year. Of course, I am always pre-supposing the absence of internal disorder or external strife. How are we to find this extra amount?"

Considering only British India, then, the revenue position under the new Constitution is satisfactory neither to the Provinces, nor to the Centre. The former are crippled by want of funds and deprived, at the very start, of any hope to develop any of their available resources which may have been kept undeveloped all this while; or undertake any projects of social reconstruction or economic betterment of their people which may be long overdue.\* The latter, already sunk to the neck by the intolerable burdens of unproductive expenditure, are unable to say whether, in spite of reserving all productive and elastic resources for themselves, they would really be able to make both ends meet in the new regime. In the passages cited above from the Budget speech, no account is taken of the very probable increase in Federal expenditure simply because of the institution of the Federation. This may amount, on the existing scale of such expenditure, from Rs. ¾ crore to 1½ crores per annum. But of this we shall treat elsewhere.

#### Federated States and Federal Revenues

Let us now consider the financial position, as outlined in the Constitution Act, from the point of view of the States intending to federate. The provisions of the Constitution introduce certain novel features, or make new arrangements, which need to be carefully studied by every intending member of the Federation.

\*See Chapter VII Provincial Autonomy (2nd Edition) pp. 309-363.

Broadly speaking, there is a discrimination in favour of the Provinces,

- (i) In regard to the subventions from Federal Revenues to what are called Deficit Provinces, viz., Sind, Orissa, Assam, North-West Frontier Province, Bihar, and Bengal, aggregating over Rs. 4.5 crores.
- (ii) In regard to the remission of debts due from them, included, of course, in the foregoing; but, nevertheless, in the manner of this concession, as well as in its extent, it is a material point worth noting by itself. The States in debt or deficit will get no such consideration.
- (iii) In the distribution of certain resources, like the taxes on jute export or income, etc. The Provinces will obtain, when the scheme recommended by Sir Otto Niemeyer matures, an advantage in which the States will not participate to the same extent as the Provinces. Nor will relief in regard to Succession Duties, Stamp Duties, Terminal taxes on goods and passengers by rail or air, under Section 137, help the States. They will only make themselves liable to the surcharges for Federal purposes under these heads in the bargain, even if we discount altogether the undesirable re-action of introducing some of these taxes in States where they do not exist at all. The experience of the Australian Commonwealth, in regard to the distribution of the surplus by the Commonwealth among the member States, is very discouraging; and there is every reason to fear it may be repeated in India.
- (iv) Some additional liabilities are imposed upon the Federated States, which the latter are not in law or ethics bound to assume; and which, once assumed, will have to be maintained by contributions from the States as also from the



Provinces, the benefit, however, not being shared equally.

- (v) A new viewpoint is adopted of the liabilities on the Federal Revenues, which would make the gross obligations of the Federation upon the new members thereof, i.e., the States, much more heavy and considerable than appear at first sight.

#### Altered Angle of Vision

Take the last first. The definition of Federal Revenues, as given in Section 136, runs:—

“Subject to the following provisions of this Chapter with respect to the assignment of the whole or part of the net proceeds of certain taxes and duties to Provinces and Federated States, and subject to the provisions of this Act with respect to the Federal Railway Authority, the expression “Revenues of the Federation” includes all revenues and public monies raised or received by the Federation, and the expression “Revenues of the Province” includes all revenues and public monies raised or received by a Province.”

It is noteworthy that:

- (a) There is no mention in this definition, of the revenues of a Federated State, or even of Federated States collectively. It is difficult to imagine the purpose behind this omission, unless it be that, while for the purpose of charging the Provinces with all the liabilities of the Federation only those resources are to be required, or brought into operation, which are or can be included in the above definition, wide as it is,—for the corresponding purpose in regard to the States no limit is imposed by law.
- (b) The omission cannot but be regarded as significant. Perhaps it is also intentional. For the States have, in fact, been mentioned in the earlier part of the section, where it speaks of a

future distribution of proceeds of certain taxation among the States as well as the Provinces; and they have been quite clearly omitted in the portion of the section giving the actual definition of Federal and Provincial revenues.

The definition of Federal Revenues is, it must be admitted, wide enough, in all conscience. It will include both the ordinary, recurrent revenue,—in the shape of proceeds of taxes, duties, rates and fares on transport services, postage dues, fees for other services rendered by the State;—as also monies “raised or received” by way of Loans, Bonds, Deposits, Treasury Bills, or any other form of raising the wind (e.g., Contributions ordered from units). The inclusion of such non-recurrent forms of receipt under the ordinary revenues is open to the most serious objection, on constitutional as well as financial grounds. In the first place, it confounds in one and the same category two essentially different classes of public resources,—tax-yield, and proceeds of borrowing or the like. By this confusion into one category of two different categories, efficiency in financial administration will be gravely jeopardised.\* This, in its turn, would endanger India's public credit. For, once the administering authority is freed from the obligation to observe the generic distinction between current, normal revenues derived from taxation, etc., and the non-recurrent resources derived from public borrowing or windfalls, there will be inevitable and unconscious laxity, which cannot but militate against the continued correctness, economy, and efficiency of financial administration, and therefore of the national credit.

\*Cp. Section 33 (2) for an obvious inconsistency with this Section 136.

This apprehension is strengthened by the provisions of Section 150, defining the charges on the Federal Purse. As this subject, however, is discussed at some length in the volume on **Provincial Autonomy**, we need not repeat those arguments here.

Under the several provisions of the Constitution Act, the States would have to contribute to the Federal Purse, directly or indirectly, in a variety of ways. Let us enumerate the sections of the Act which affect the States in this behalf.

The Federation will raise its revenues from:

(a) Ordinary taxation, to which the States will be expected to contribute in normal times:

- (i) Customs Duties (Items No. 19 and 44 of the Federal Subjects).
- (ii) Export Duties (Items No. 19 and 44 of the Federal Subjects).
- (iii) Excise Duties on commodities other than alcohol, opium, Indian hemp, narcotic and non-narcotic drugs, whether intended for human consumption or for use in medicinal and toilette preparations (Item No. 45).
- (iv) Salt (Item No. 47).
- (v) Corporation Tax (Item No. 46) after 10 years.

(b) Ordinary Taxation to which the States will **NOT** be expected to contribute in normal times.

- (vi) Taxes on Income, other than agricultural (Item 54) and surcharge on Income Tax.\*
- (vii) Property Taxes, i.e., Taxes on capital value of individual's assets, or of companies, (other than agricultural land) (Item 55).

\*Cp. Section 137 (3).

(c) Extraordinary revenue, to which the States will be expected to contribute in times of financial stringency, which is chronic in all democracies, more particularly in Federations, and still more particularly in India, viz.,

(viii) Surcharges on Income-Tax.\*

(d) Extraordinary sources of revenue to which States will not be expected to contribute even in times of financial stringency.

(ix) Surcharges on Succession Duties (Item No. 56) Section 137.

(x) Surcharges on Terminal Taxes on goods or passengers carried by rail or air, and on taxes on railway freights and fares.

(xi) Surcharges on Stamp Duties in respect of Bills of Exchange, Cheques, Promissory Notes, Bills of Lading, Letters of Credit, Policies of Insurance, Proxies and Receipts; (Item No. 57, Section 137).

(e) Sources of revenue not derived from taxation, to which the States, or their people, have to contribute, directly or indirectly, viz.:—

(xii) Fees in respect of matters included in the Federal List.

(xiii) Profits (if any) on the working of the Postal services, including Postal Savings Banks.

(xiv) Profits (if any) on the operation of Federal Railways.

(xv) Profits (if any) from Mint and Currency operations.

(xvi) Profits (if any) from any other Federal enterprise; e.g., Reserve Bank.

(xvii) Direct contributions to Paramount Power, from Federated or non-Federated States, under Treaties, etc.

\*cp. Section 138 (3).

In addition to the taxes and sources of revenue thus listed under Section 104:—

"(1) The Governor-General may by public notification empower either the Federal Legislature or a Provincial Legislature to enact a law with respect to any matter not enumerated in any of the Lists in the Seventh Schedule to this Act, including a law imposing a tax not mentioned in any such List, and the executive authority of the Federation or of the Province, as the case may be, shall extend to the administration of any law so made, unless the Governor-General otherwise directs.

(2) In the discharge of his functions under this section the Governor-General shall act in his discretion."\*

Taken in the terms in which it is couched, this extra-Schedule authority for taxation by the Federal (or Provincial) Government may involve the Federated States in heavy burdens. This is the more so, as the Governor-General is entitled, under this Section, to act in his discretion, i.e., without consulting his Federal Ministers, if he so think proper. If the States have expressly kept themselves out of this, they may be a little better protected; but it is exceedingly doubtful if they would be allowed to keep out of this. The entire scheme of Federal Finance, as evidenced by the chapters and sections of the Act dealing with that branch of the administration, seems to contemplate uniform burdens, from which no federated unit will be allowed to claim exemption, unless the same has been expressly and legally provided for.

\*It is not absolutely clear; but it seems likely that the States not being on the Sea-coast, or not having ports of their own, might be forced to contribute even to the Provincial Purse, by such duties as those levied by the Port authorities at Bombay or Calcutta on passengers and their luggage. Even such items of taxation as, for instance, a duty on raw cotton grown in the Bombay Presidency, or exported through the ports of that Province, may have to be borne by the States affected. There is no provision in the constitution to prevent such imposts by Provinces. Section 297 will not avail, since it only applies to provincial attempts to restrict movements of goods, or to attempts at discriminatory treatment as between members of a common Federation. Nor will States be exempt from contributing indirectly to any new industry conducted as Government monopoly from which handsome profits may be derived.

All taxes, forming the normal or abnormal sources of Federal revenue, will be imposed and collected by the Federal Government; and some of even those which are not normally federal revenue. The States may contract themselves out by the special provision in the sections concerned, e.g., (Sections 138 and 139); or by the operation of an agreement under Section 125, in consideration of paying a lump sum in respect of such tax receipts collectable in their jurisdiction, and payable to the Federal Government. But, until they do so, they will be liable to a most vexatious exercise of Federal authority within their jurisdiction, and so impair their internal autonomy which no State can sincerely welcome.

Apart, however, from the political aspect of these provisions, the financial aspect proper is disquieting enough, to the States as much as to British India. The Federal Government will keep for itself exclusively Customs, including Export Duties, Imperial Excises, Salt, Corporation Tax, and Income Tax,—a stated proportion,—Taxes on the capital value of non-agricultural assets of individuals or companies, and a surcharge, during financial emergencies, on Income Tax. This may involve many States, who to-day levy Customs or Excise Duties of their own, into surrendering those sources of their revenue to the Federation. The consideration for this surrender is difficult to perceive. Sections 147 and 149 do, indeed, provide for certain refunds or remissions of State dues, or commuted payments for the surrender of "privileges and immunities." But the language of those sections is anything but expressive; and their working would avoid complication and misunderstanding—only by a miracle.



## Refunds to States Customs

There are several considerations of constitutional law or usage worth remembering in these two Sections 147 and 149. The set-off, etc., is allowed in consideration of the remission of cash contributions payable by the Federating States in respect of paramountcy payments, or other dues from the States to Suzerain. Apart from the remission of such payment, the term "**privilege or immunity**" is singularly inept, if it is to apply to such inherent rights of local sovereignty as the Maritime and even inland Customs duties levied by the States, or the issue of their own currency, metallic or paper. Where such rights have been surrendered by specific agreement, the States cannot, of course, at this time, raise afresh these matters as immunities, rights, or privileges, for the sacrifice of which in federating, they ought to be compensated in some form, *e.g.*, by remission of cash contributions due from them. But, where these are ancient and still surviving rights of local sovereignty, and where they have been exercised as such from time immemorial, it seems a violent departure from existing practice to treat them as on a par with the rights and privileges or immunities enumerated in Section 147 (6).

The Government of India have managed, by a long series of treaties with the inland States, to abolish, over the greater portion of the land, internal Customs Duties, which in effect amounted to Transit Duties. Now, on the eve of the Federation, their threat to those Maritime States, who, having their own sea-ports, are entitled to and do levy their own Customs duties, either on the British Tariff Schedule, or, in rare cases, at their own rates, to re-introduce

against them these obsolete transit duties in the form of a Customs cordon is a frank violation of the spirit if not the letter of the treaties still subsisting. Their offer to compensate individual States by a cash subsidy for the sacrifice of this their ancient right is itself an admission that the pressure they exert on the States concerned to join the Federation and sacrifice this revenue needs some substantial justification, or some presentable camouflage. Even if the States do not find this offer sufficient bribe to surrender their ancient right, they are not all in a position successfully and profitably to defy the Government of India. But that does not make the case of the British Government of India any more just or reasonable; and if the States concerned do eventually surrender, it will be no proof that they admit themselves to have been in the wrong.\*

It must be admitted, of course, that the demand of the Maritime States to keep the whole of the Customs revenue collected at their ports for themselves is not absolutely just. Even when there is no suspicion of unfair or illegal practices to swell the State's revenue from this source, a good proportion of this revenue, it must be admitted, is derived from people other than those of the State concerned. On the former, this impost is a burden, which, in justice as well as reason, ought to go to the common purse,—that of the Federal Government of India. But, essentially sound and unassailable as this theoretic position is, it is nevertheless impossible to apply it rigorously in India without causing greater injustice. The Indian Federation is not the ideal union of all equal and autonomous communities. There is neither free consent nor equal benefit

\**cp.* however Articles XIV and XV of the Instrument of Instructions to the Governor-General.

expected of this association. Besides, Treaties, however obsolete, have a sanctity, which the British Government of India at least ought to be the last to question, even indirectly,—seeing how adamant they have shown themselves in protecting and safeguarding the much less sacred rights of the Public Servants and British capitalists in this country. Finally, the States so situated can claim this particular source of their ancient revenue as being no more than a proper utilisation of a gift of nature to them. In the case of many a British Indian port, its present importance is due to acts of man rather than gifts of nature, e.g., the layout and termination of railway lines. These have succeeded in taking away a great portion of the trade the States ports formerly enjoyed. It is only recently that they have begun to counteract in some slight measure the effect of these manmade attractions to trade. The claim of the States, therefore, to retain for themselves the whole of the Customs duties collected at their ports, is impossible effectively to resist on grounds of international advice, or even of National economics, let alone political justice or sanctity of treaties.

A general measure, like the present Act, will scarcely be a suitable means to abrogate those rights, even if the acceding States interested in such rights themselves waive them, and agree to accept some *Quid pro Quo* for such waiver. Room is left, no doubt, in the concluding lines of Section 147 (6), which would safeguard such rights of the States, and yet permit them to be compensated for the whole or partial surrender of such rights on entry into the Federation. But satisfactory arrangement under such clumsy, complicated

provisions is extremely difficult to make; and that is why the greatest difficulty is being even now experienced in respect of the Customs rights of the "Maritime States."

### States and Excise

Similarly, also, the field for Federal Excise was deemed to be considerably restricted, both by the Percy Committee, and in the Memorandum of the Government of India. The recent introduction of a countervailing excise on steel, sugar, etc., opens up infinite possibilities of such indirect taxation of State subjects for Federal purposes. The States will not be able to claim exemption from such Federal Excises on industrial output in their own territories, either under Section 147, or under Section 155. Even the industries conducted as collective State enterprise in any State may not, in all likelihood, escape Federal Taxation by way of surcharge on the Income Taxes, Corporation Tax (when it becomes applicable to the States), or Excise, should the particular production be liable to Federal Excise.

The revenue position, then, of the Federation as well as of the units,—whether States or Provinces,—is anything but satisfactory, as revealed in the Constitution. Existing resources are either inadequate for the purpose of everybody concerned; or are possible to replenish at a normal and economic cost, which no one who has the welfare of the Indian people at heart can contemplate without a shudder.

## II—FEDERAL EXPENDITURE

Let us now turn to the expenditure side of the Federal Finance. The definition of Public Expenditure,



as given by Section 150, has already been commented upon in the volume on **Provincial Autonomy**, and so, need not be repeated here.

The Constitutional provisions in respect of Expenditure are to be found, among others, in the following sections:—

Section 11—excluding certain Departments of State, e.g., Defence, External Affairs, Ecclesiastical Affairs, and Tribal areas. Expenditure in regard to these is outside the control of the Legislature, though the Instructions of the Governor-General require him to keep his Ministers in touch with the expenditure on Defence by holding joint consultations between his Counsellors in the Excluded Departments and Ministers. Various other sections, dealing with these departments, including salaries, pensions, etc., of the officers and staff under the same are made expressly charged on the Revenue of the Federation, and as such, non-votable by the Federal Legislature, and so non-controllable.

Section 12 (1) (b)—imposing a Special Responsibility on the Governor-General to safeguard the financial stability and credit of the Federal Government. Under this he can arrogate to himself practically dictatorial power, over Federal finances.

Sections 33-36—prescribing the financial procedure in regard to expenditure of the Federal Government. Under these, certain items of expenditure cannot be voted upon by the Federal Legislature; and authorise expenditure upto a certain extent even on those departments in which the Legislature is entitled to vote the grants. The device of Supplementary Estimates is also to be found in these sections, tending to weaken still further the control of the Federal Legislature upon the expenditure of the State in India.

Section 150—defining Federal Expenditure and its purposes.

Sections 200-230 and Sections 240-253. These relate to the Courts, their establishments and expenditure by way of salaries, pensions, allowances of Judges, pensions, gratuities, decrees and awards against the Government or any official of the same. Other administrative expenditure in connection with the Courts of Justice in India, as also in regard to other services to which appointments are made by the Secretary of State or the Governor-General in his discretion, are also placed outside the control of the Legislative Vote.

Liability in respect of (i) the Public Debt, and other obligations of the Federal Government, including

(ii) payments, to the representative of the Crown in its relations with the Indian States,—Section 285-7;

(iii) contributions to the States under the terms of Sections 147-149,

(iv) subventions to the Provinces under the terms of Sections 137-142,

are also outside the vote of the Federal Legislature. No possible relief is to be thought of under any of these non-productive heads of public expenditure.\*

#### Scale of Federal Expenditure

The financial aspect of these provisions may be translated into figures as follows:—

Items which are to-day non-voted, and which will be "charged upon the revenues" of the Federation under the new Constitution, according to the Budget estimates of 1937-38 of the Government of India:

(In lakhs of Rs.)

Staff, Household and Allowances of Governor-General	15.54
Public Service Commission	4.95

\*The distribution of the proceeds of certain taxes, duties, etc., e.g., those under section 137 or 139 levied by the Federal Government on account of federated units; or the refund of a share of income tax (Section 138) or of the Jute Export Duty (140), are not included in the above as these are not Federal Expenditure proper.



Ecclesiastical Department .. .. .	27.82
Tribal Areas .. .. .	192.05
External Affairs .. .. .	52.24
Baluchistan .. .. .	64.94
<b>Total ..</b>	<b>357.54</b>
<b>Add: Payments to Representative of the Crown</b>	<b>105.55</b>
Interest on Debt (nonvoted amount) ..	1323.65
Defence Expenditure (net) .. .. .	4462.00
Pensions .. .. .	286.00
Grants in aid to Provinces .. .. .	316.00
<b>Total ..</b>	<b>6850.74</b>

This is out of a total expenditure of about 80 crores or 86% roughly of the total. It does not, of course, tell the whole tale, since it takes no note of that portion of the interest, etc., payment, for which the Federal Government would be responsible, and which would be charged on the Federal Revenues, but is supposed to be received from the Railways, Post Office, Provincial Governments, etc. Nor does it include such Pensions as those on account of Civil Administration Charges. The grants to the States under Sections 147-149, if the Federation is achieved as planned, have been estimated to add another crore to this class of expenditure; while the expenses of the Federal Court, the Advocate-General, the Counsellors, Financial Adviser and their staff, would likewise add considerable amounts to such non-votable expenditure.

### Defence Expenditure

There is every reason to fear a steady expansion in these items. Thus the charges of Defence must grow inevitably in the near future,\* even after allow-

\*The debate in the Indian Legislative Assembly, on September 5, 1937, on a non-official resolution to reduce defence expenditure, brought forth a clear warning from the Army Secretary that the expenditure may very soon have to be increased.

ance has been made for the tardy and scanty refund made to India by the British War Office towards the cost of the disproportionately heavy army maintained by India on British Imperialist account; and even after allowance has been made for the relief due to the separation of Burma, who would now provide for her own defence. The purpose, officially recognised, of maintaining such a heavy Defence provision, is said to be to protect India against aggression from without, and, secondly, against disorder or anarchy from within. The natural defences of India, and the characteristics or equipment of her immediate neighbours, are scarcely taken into account in framing and maintaining this expenditure, thanks mainly to the demands of British Imperialist ambitions. Not only is there the inevitable tendency for increasing costs in this department free from the salutary control of the Legislature, because of constant innovations and advances in the art and equipment for warfare; but the demands of British Imperialist diplomacy involve India in an incessantly shifting morass of international relations, in which she must maintain an utterly disproportionate military preparedness. Were this of any material benefit to India directly, there might be something to be said for keeping out the Defence Budget of the Legislative vote. As it is, the States and Provinces will alike feel it an unmitigated burden, unrelieved by any counter gains to the parties who shoulder it. For the States, the burden is all the more indefensible, some of them at least maintain their own Defence forces, however obsolete their equipment, and however inefficient their direction. Notwithstanding Treaty obligations for the States' Defence, these additional burdens will have to be

shouldered by the States as the price of the privilege to join the Federation.

### Debt Charges

As for the expenditure on account of the so-called Public Debt of India, the legal, constitutional position has been examined in detail by a Select Committee of the Indian National Congress in 1931, to whose Report attention may well be directed in this connection. The only remark we need add, from this standpoint, is that in the years that have followed, the legal, or moral, or even economic justification has in no way improved.

Confining our attention only to the financial aspect, we find the provision for reductions of the existing debt, or its avoidance in the future, is dangerously low in the present Budget. Material developments, or improvements in the Social Services in the country, have been deferred so long, that all possible haste will have to be made by the Federal Government to part with a respectable proportion of such items of revenue, as, though levied and collected by the Federal Government, are intended for distribution, wholly or partially, among the units composing the Federation. Almost every Province has an immense leeway to make up in education and public health, industrial development and agrarian reconstruction. And all that would need money, even after the Congress limit of official salaries has been enforced all round. True economy, for the benefit of the people, while limiting the maximum salaries, must guarantee a living wage to the lowest grade of public servants. If the Congress thus re-grades salaries upward as well as downward, it may be doubted if any very great saving will be made by such regrading. The States

are notoriously backward in what might be called the moral and material progress of the people under their charge. If, in spite of such considerations, they still join the Federation, and cripple still further their financial resources,—none too strong,—they will be jeopardising, not only their own local Sovereignty, but also their chances of material progress within their jurisdiction,—which alone could justify their continued existence as independent units, such as they are:

### Non-Voted Expenditure

Section 33 classifies among "the expenditure charged upon the revenues of Federation", and, therefore, non-votable by the Federal Legislature:

- (i) Salaries and Expenses of the Governor-General and his office;
- (ii) Debt, Sinking Fund, Redemption, and Loans charges or service of the Debt;
- (iii) Salaries and allowances of Ministers, Counsellors, Financial Adviser, Advocate-General, Chief Commissioners, and staff of the Financial Adviser;
- (iv) Salaries, Allowances and Pensions of Federal Court Judges, and Pensions of other High Court Judges;
- (v) Expenditure in connection with Defence, Foreign Affairs, Ecclesiastical Affairs, Tribal areas and other special responsibilities of the Governor-General;
- (vi) Grants or the payments to the States;
- (vii) Grants for purpose of the administration of excluded areas;
- (viii) Judgment decrees or other awards of courts;
- (ix) any other expenditure required by this or any act of the Federal Legislature to be so charged.

All this, put together, may amount to more than 4½ths of the total recurring revenues of the Federation.\*

The Legislature would have no right to vote on any and all of those items.†

### Authenticated Schedule of Expenditure

The procedure relating to an authenticated schedule of expenditure, as defined in Section 35, is quite capable of vesting absolute and overriding power in the Governor-General in such matters of finance. The possibility of submitting Supplementary Estimates, and an authenticated schedule of the same, as contemplated in Section 36, only adds to this absolutism. If the terms of these Sections were carefully scrutinised, it would seem that, under the new dispensation, India would have little more than a shadow of financial autonomy.

To meet these extraordinary obligations being imposed upon the Members of the Federation,—States and Provinces included,—resources are proposed to be added to the Federal fisc which have hitherto not been part of the all-India sources of revenue. The Federated States are not bound, in ethics or under treaty obligations, to shoulder any portion of the pre-Federation Debt. Nor need they assume the corresponding Pensions charges of the Government of India, which the present Constitution seeks to impose upon them. If

\*See ante p. 434. Appendix II of the Financial Secretary's Memorandum gives the following distribution (1937-38):—

Voted:	..	..	..	Rs. 90.12 crores
Non-Voted	..	..	..	" 106.88 "
			Total	" 197.00 "

But this includes the Gross Charges of the Railways and Postal Services which amount to 80 crores, and which, under the new Act, will, so far as Railways are concerned, be outside the Legislative control definitely.

†cp., Section 34 (1).

the States accept without reserve that item in the Federal List of subjects, as given in Schedule VII to the Government of India Act, 1935, they would make themselves liable for burdens against which they receive no benefits whatsoever. This debt was never incurred for the benefit of any of the States, nor with their consent. A considerable portion of it was even used to aid in their further subjugation, where absolute annexation was not adopted.

### Financial Equilibrium before Federation

The show that is being made of the Central Budget balancing before any of the States consent to Federate will not deceive anybody, since

- (1) the presence of a continued deficit on account of the Railways.\*
- (2) the shrinkage in the important item of the Customs Revenue;
- (3) the addition of still more liabilities in respect of the grants to be made to certain of the Provinces, aggregating some 4½ crores of Rupees

\*In the Budget for 1937-38, the Railways are estimated to show a small net surplus; but the main causes which made for the long continued deficit in this department are even now not ended; and so one is entitled to assume, as Sir Otto Niemeyer throughout his Report apprehended, this to be a very doubtful source of surplus revenue. The Experts' Railway Enquiry Committee of 1937 have thrown a cold douche on any hope of obtaining aid from this source hereafter. The accumulated deficit on Railways account between 1930 and 1937, aggregating some 62 odd crores, has been written off. This means that to that extent the burden of debt on the general tax-payer has been increased. Any expectation of even a future contingent relief to the general revenues when the Railway again made a surplus, is finally negated.

In their own interests, it would be best for the States intending to federate, to suggest and insist that before they accede, the Federal Budget be split up into two,—say, for a period of 20 years at the most,—one containing all the items which do not concern the Federated States, because these represent charges incurred before the States became part of the Federation; and because in respect of these they had received no benefit; and the other containing all items of really common concern. The States, we need hardly add, would be well advised to restrict federal obligations only to the latter. The suggestion may be said to be impracticable but there is good precedent for it in the Act itself. (e.g., Section 138).



per annum from the commencement of the new regime;

- (4) the loss, also, in respect of the disappearance of the Central Revenues derived from Burma, estimated at 2.38 crores of net reduction of revenue;
- (5) the additional charges in respect of the new Constitution itself, about 1 crore per annum;
- (6) the remission of contribution from the States, and the refund of some portion of revenues to certain States in respect of ceded districts, etc., another  $\frac{1}{2}$  crore or more, and
- (7) the dangerously low provision in respect of the reduction of avoidance of debt,

make a gap of some 12 crores per annum, which makes it impossible for the Central, or Federal Budget really to balance, even with a very much reduced provision for reduction or avoidance of Debt in the near future.\*

Financial jugglery might make two sides seemingly equal; but in reality there is no evidence of such equilibrium being possible when the Federation is established; much less would it be maintained for long thereafter.

Under such circumstances, the Government of India's present Budget cannot be assumed to be balancing,—whatever might be said of the Provincial finances being placed on an even keel, especially after the Niemeyer Report.†

\*Economics on account of the Debt charges due to the conversion of the higher interest bearing Debt into a lower interest bearing obligation has made for some immediate saving, which, however, in the long run would mean no real relief to the Indian tax-payer, since the conversion terms are far too liberal.

†The Conference of the Provincial Financial Ministers, in the 1st week of June 1937, in Bombay, was, however, unanimous in bewailing the financial lot of the Provinces, under the new dispensation. It is more than doubtful if any of the grandiose schemes for provincial developments of the new ministries in the Provinces would anywhere be possible to accomplish, simply for lack of funds, under the prevailing canons of national economy.

### III—BORROWING POWERS OF THE FEDERATION

The borrowing powers of the Federation are regulated by Chapter II of Part VII of the Act of 1935. Under Section 161, the powers of the Secretary of State to borrow in England on the security of the revenues of India are abolished,—except in so far as any such borrowing is necessitated during the transition period pending the establishment of the Federation. These powers are to be exercised, when the Federation has been proclaimed, by the Federal Government under Section 162:—

“162. Subject to the provisions of Part XIII of this Act with respect to borrowing in sterling, the executive authority of the Federation extends to borrowing upon the security of the revenues of the Federation within such limits as may from time to time be fixed by Act of the Federal Legislature and to the giving of guarantees within such limits, if any, as may be so fixed.”

The authority of the Federal Legislature in this respect is, however, subject to the overriding powers of the Governor-General, on whom a special responsibility is imposed by Section 12 (1) (b) for the maintenance of the financial stability and the credit of India.\* Borrowing, moreover, is an executive act, in which the influence of the Governor-General, and the counsel of his Financial Adviser, would necessarily preponderate, because of the several discretionary and extraordinary powers vested in him by the Constitution. The purpose of borrowing, its terms and conditions of interest, repayment etc., even if prescribed by legislation in any given instance, would be materially influenced by this executive head of the Government. Any Loan which is intended to nationalise large-scale

\*Cp. Article X of the Instructions to the Governor-General, (p. 214) who must make it his duty to see that a borrowing or budgetary policy is not followed which would seriously prejudice the credit of India.

productive enterprise, or start it afresh, may quite possibly be vetoed by the Governor-General, particularly if it has a tendency to expropriate capitalist British vested interests.\* How far borrowing will help the responsible Federal Government, if and when it comes inot being, in face of the enormous first mortgage created by the Act in respect of the British Imperialist vested interests and the existing Debt of the Government of India,†—to realise its plans for economic development and social reconstruction in the country, is not so much a Constitutional as a Financial question. Accordingly we need not dwell here at length upon it.

We may, however, notice the constitutional difference in treatment, in this matter of borrowing, between the British Provinces and the Indian States. Both are free to raise Loans in the public market, or borrow from the Federal Government.‡ But whereas, under Section 163, the Federal Government have some sort of a control over the Provincial borrowing, not only in regard to those loans which the Federal Government themselves make to the Provinces, but also in regard to loans sought to be raised in open market by a Provincial Government outside India, no such control or supervision is insisted upon as regards borrowing by a Federal State either in the open market, or from the Federal Government. Whereas Section 163 relating to Provincial Governments' borrowing insists upon prior consent of the Federal Government for raising loans outside India; and imposes certain conditions under certain circumstances for borrowing in India, Section 164, relating to

\*cp. Section 299.

†cp. Section 157 and Sections 302 to 313.

‡cp. Sections 163 and 164.

borrowing by the Federal States is very liberal in comparison.

"164. The Federation may, subject to such conditions, if any, as it may think fit to impose, make loans to, or, so long as any limits fixed under the last but one preceding section are not exceeded, give guarantees in respect of loans raised by, any Federated State".

Whether this liberal treatment will help the States is a different question. Many of the States are already considerably indebted to the Government of India,—the aggregate running into over 50 crores. In more than one case that Government has been forced, either to write off particular amounts of the debt, or take very drastic steps to effect recovery. With the possible exception of not more than a dozen leading states, financial administration in these relics of medieval India is by no means conspicuous for its soundness or economy. Occasions for financial waste and extravagance are much more numerous; the possibilities for economy and retrenchment limited; and the mechanism for adequate and efficient check upon spending practically unknown in the States. The Rulers are more parasites than protectors; their Ministers and advisers more skilled in sycophancy than in financial acumen or administrative integrity; and the secret, invisible exploitation, to which the States are subjected by the minious or mandatories of the Paramount powers, so intense, incessant and exacting, that any scope for sound budgeting or healthy finance must be altogether discounted in a vast majority of these ancient haunts of vice and waste. The States, as already noted, have a long leeway to make up in the economic development of their territories. This concession in the matter of borrowing may, therefore, seem, at first sight, to be a substantial inducement to make up for



the arrears. In view, however, of the immense burdens of the Federal regime; and in view of the known laxity of financial administration in the States, it is more than doubtful if this provision will aid them in the task before them.

#### IV—AUDIT

In the Federation, the Provinces, as well as the States, the only guarantee,—if the phrase may rightly be used,—for a sound, economical financial regime under the Constitution is to be found in the provisions regarding the appointment of an Auditor-General for India, as also for the Provinces if so desired. Under Section 166:—

- "166—(1) There shall be an Auditor-General of India, who shall be appointed by His Majesty and shall only be removed from office in like manner and on like grounds as a judge of the Federal Court.
- (2) The conditions of service of the Auditor-General shall be such as may be prescribed by His Majesty in Council, and he shall not be eligible for further office under the Crown in India after he has ceased to hold his office:

Provided that neither the salary of an Auditor-General nor his rights in respect of leave of absence, pension or age of retirement shall be varied to his disadvantage after his appointment.

- (3) The Auditor-General shall perform such duties and exercise such powers in relation to the accounts of the Federation and of the Provinces as may be prescribed by, or by rules made under, an Order of His Majesty in Council, or by any subsequent Act of the Federal Legislature varying or extending such an Order:

Provided that no Bill or amendment for the purpose aforesaid shall be introduced or moved without the previous sanction of the Governor-General in his discretion.

- (4) The Salary, allowances and pension payable to or in respect of an Auditor-General shall be charged on the revenues of the Federation, and the salaries, allowances and pensions payable to or in respect of members of his staff shall be paid out of those revenues."

The appointment of the Auditor-General of India by the King may be justified on the ground of securing the completest possible independence for that officer, and an absolute security of tenure, to enable him to do his work fearlessly and efficiently. However sound in intention or in working, this arrangement would necessarily detract from the supreme authority of the Indian Government, and of the Indian Legislature to appreciate the bearings of sound financial administration on the success of the new democracy.

The work of the Auditor-General of India may, however, serve to keep open the eyes of the representatives of the people as regards the financial administration of their country. Under Section 168, he is entitled to give directions to the accounting staff in India as regards the methods and principles of keeping accounts both for the Federation, and for the Provinces wherever so permitted. And though, under Section 169, the Auditor-General reports only to the Governor-General of India as regards the accounts of the Federation,—and not to the Federal Parliament of India directly,—the Governor-General is required, by the same section to submit the same to the Legislature.\* Whether the mass of the Legislators will fully understand the mysteries of the accounts laid before them in the Auditor-General's Report, or appreciate and adopt the lessons of financial economy contained therein, remains to be seen.

#### V—SUMMARY

On a general review of the Constitutional aspect of Federal Finance, it appears that:—

\*The same practice is ordained upon the Governor of a Province as regards the accounts of the Province.



- (1) Revenue resources are unevenly distributed between the Federation and the units. They are utterly inadequate for the Provinces at any rate to undertake any serious project of economic development or social reform. The system is neither simple nor productive. The new items of revenue contemplated in the Constitution might prove burdensome, and cause complications.
- (2) Much of the Expenditure is outside the control of the representatives of the States and Provinces in the Federal Legislature. Almost all the Federal Expenditure is unproductive and burdensome, due mainly to the Imperialist or exploitive fountain-springs of the new Constitution. The charging of some of these burdens upon the new members of the State in India, is open to question on ethical, historical, as well as economic grounds.
- (3) Borrowing powers, though liberal in conception, are unlikely to be of any real help in the task of Provincial, State, or National development, or social reconstruction, in view of the rigid mortgage imposed by the Act on account of the existing Debt.
- (4) Redistribution of the National wealth, by means of a proper system of taxation, or appropriate lay out of the public expenditure, is all but unthinkable in view of the heaviness and rigidity of the burdens imposed.
- (5) Accounting and Audit provisions of the Act may help to induce a degree of soundness and economy in the financial administration,—if those who have the right to review the accounts and benefit by the lessons of the review are able to do so.

## STATEMENT OF THE EXPENDITURE CHARGED TO REVENUE OF THE CENTRAL GOVERNMENT

(In Thousands of Rupees.)		Budget Estimate 1937-38
HEADS OF EXPENDITURE		
DIRECT DEMANDS ON THE REVENUE		
1. Customs	...	1,19,12
2. Central Excise Duties	...	8,55
3. Corporation Tax	...	5,80
4. Taxes on Income other than Corporation Tax	...	69,40
5. Salt	...	1,06,72
6. Opium	...	25,37
7. Provincial Excise	...	4,33
8. Land Revenue	...	6,00
9. Stamps	...	16,13
10. Forest	...	20,33
11. Registration	...	9
12. Charges on account of Motor Vehicles Taxation Acts	...	2,05
Total	...	3,83,89
CAPITAL OUTLAY ON SALT WORKS CHARGED TO REVENUE		
5A. Capital outlay on Salt Works	...	36
REVENUE ACCOUNT OF IRRIGATION, ETC. WORKS		
17. Interest on Works for which Capital accounts are kept	...	7,44
18. Other Revenue Expenditure	...	3,91
Total	...	11,35

## STATEMENT OF THE REVENUE OF THE CENTRAL GOVERNMENT.

(In Thousands of Rupees.)		Budget Estimate 1937-38
HEADS OF REVENUE		
PRINCIPAL HEADS OF REVENUE		
I. Customs	...	42,60,50
II. Central Excise Duties	...	7,16,00
III. Corporation Tax	...	1,44,94
IV. Taxes on Income other than Corporation Tax	...	12,85,06
V. Salt	...	8,25,00
VI. Opium	...	49,53
VII. Land Revenue	...	18,53
VIII. Provincial Excise	...	21,12
IX. Stamps	...	36,05
X. Forest	...	14,62
XI. Registration	...	91
XII. Receipts under Motor Vehicles Taxation Acts	...	2,81
Total	...	73,75,06
IRRIGATION, ETC.		
XVII. Works for which Capital accounts are kept—Gross Receipts	...	4,80
DEDUCT—Working Expenses	...	3,84
Net Receipts.	...	96
XVIII. Works for which no Capital accounts are kept		
...	...	5
Total	...	1,01

## POSTS AND TELEGRAPHS

XIX. Posts and Telegraphs	...	11,15,93
Gross Receipts ...	...	10,38,95
DEDUCT—Working Expenses	...	

Net Receipts. 76,98

## DEBT SERVICE

XX. Interest	...	71,35
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## CIVIL ADMINISTRATION

XXI. Administration of Justice	...	1,39
XXII. Jails and Convict Settlements	...	2,10
XXIII. Police	...	25
XXIV. Ports and Pilotage	...	21,27
XXV. Lighthouses and Lightships	...	8,55
XXVI. Education	...	1,50
XXVII. Medical	...	1,85
XXVIII. Public Health	...	2,96
XXIX. Agriculture	...	2,47
XXX. Veterinary	...	5,98
XXXI. Cooperative Credit	...	
XXXII. Industries	...	19
XXXIII. Aviation	...	1,24
XXXIV. Broadcasting	...	5,50
XXXV. Indian Stores Department	...	17,75
XXXVI. Miscellaneous Departments	...	16,73
Total	...	91,73

## CURRENCY AND MINT

XXXVII. Currency	...	66,80
XXXVIII. Mint	...	39,69
Total	...	1,06,49

## CIVIL WORKS ETC.

XXXIX. Civil Works	...	34,71
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## MISCELLANEOUS

XLII. Payments from Indian States	...	69,77
XLIV. Receipts in aid of superannuation	...	7,49
Carried Over	...	

## CAPITAL ACCOUNT OF IRRIGATION, ETC.

WORKS CHARGED TO REVENUE	...	
19. Construction of Irrigation, etc., Works Financed from Ordinary Revenues	...	

## POSTS AND TELEGRAPHS REVENUE ACCOUNT

20. Posts and Telegraphs Interest on Debt	...	72,75
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## POSTS AND TELEGRAPHS CAPITAL ACCOUNT

CHARGED TO REVENUE	...	
21. Capital outlay and Telegraphs	...	7,05

## DEBT SERVICES

22. Interest on Debt other Obligations	...	45,94,10
DEDUCT—Interest transferred to—	...	
Railways	...	28,17,90
Irrigation	...	7,44
Posts and Telegraphs	...	73,23
Other Commercial Departments	...	6,88
Provincial Loans Fund	...	
Provincial Governments	...	5,52,57
Commuted Value of Pensions	...	23,86
Total Transfers	...	34,81,88

Net 11,12,22

23. Appropriation for Reduction or Avoidance of Debt	...	3,00,00
Total	...	14,12,22

## CIVIL ADMINISTRATION

25. General Administration	...	1,72,73
26. Audit	...	1,01,35
27. Administration of Justice	...	7,30
28. Jails and Convict Settlements	...	23,10
29. Police	...	30,07
30. Ports and Pilotage	...	28,70
31. Lighthouses and Lightships	...	8,55
32. Ecclesiastical	...	27,82
33. Payments to Crown Representative	...	1,04,88
34. Tribal Areas	...	1,92,05
35. External Affairs	...	52,24
36. Scientific Departments	...	72,01
Carried Over	...	

## STATEMENT OF THE REVENUE OF THE CENTRAL GOVERNMENT—CONCLD.

(In Thousands of Rupees.)

HEADS OF REVENUE	Budget Estimate 1937-38
<b>Brought Forward</b>	
XLV. Stationery and Printing	25,34
XLVI. Miscellaneous	38,91
Total	1,41,51
<b>DEFENCE SERVICES</b>	
XLVII. Defence Receipts—Effective	4,80,79
XLVIII. Non-Effective	41,31
Total	5,22,10
<b>CONTRIBUTIONS AND MISCELLANEOUS ADJUSTMENTS BETWEEN CENTRAL AND PROVINCIAL GOVERNMENT</b>	
L. Miscellaneous Adjustments between Central and Provincial Governments	
<b>EXTRAORDINARY ITEM</b>	
LI. Extraordinary Receipts	3,23,11
LII. Transfers from Revenue Reserve Fund	1,84,09
Total	5,07,20
<b>RAILWAY REVENUES AS PER RAILWAY BUDGET</b>	30,13,74

## STATEMENT OF THE EXPENDITURE CHARGED TO REVENUE OF THE CENTRAL GOVERNMENT—CONT.

(In thousands of Rupees.)

HEADS OF EXPENDITURE	Budget Estimate 1937-38
<b>Brought Forward</b>	
37. Education	24,11
38. Medical	22,10
39. Public Health	22,00
40. Agriculture	58,28
41. Veterinary	10,61
42. Cooperative Credit	53
43. Industries	9,14
44. Aviation	25,04
45. Broadcasting	15,35
46. Indian Store Department	23,51
47. Miscellaneous Departments	16,32
Total	10,42,79
<b>CURRENCY AND MINT</b>	
48. Currency	14,77
49. Mint	19,23
Total	34,37
<b>CIVIL WORKS ETC.</b>	
50. Civil Works	2,87,23
<b>MISCELLANEOUS</b>	
54. A Famine Relief	46
55. Superannuation Allowances and Pensions	2,79,77
56. Stationery and Printing	41,98
57. Miscellaneous	54,55
Total	3,76,76

STATEMENT OF THE REVENUE OF THE CENTRAL GOVERNMENT—CONCLD.		STATEMENT OF THE EXPENDITURE CHARGED TO REVENUE OF THE CENTRAL GOVERNMENT—CONT.	
(In Thousands of Rupees.)		(In Thousands of Rupees.)	
HEADS OF REVENUE	Budget Estimate 1937-38	HEADS OF EXPENDITURE	Budget Estimate 1937-38
<b>MISCELLANEOUS CAPITAL OUTLAY CHARGED TO REVENUE</b>		<b>MISCELLANEOUS CAPITAL OUTLAY CHARGED TO REVENUE</b>	
55. A Computation of pensions financed from Ordinary Revenue	6,38	55. A Computation of pensions financed from Ordinary Revenue	6,38
<b>DEFENCE SERVICES</b>		<b>DEFENCE SERVICES</b>	
58. Defence Services—Effective	42,84,27	58. Defence Services—Effective	42,84,27
59. Defence Services—Non-Effective	8,41,90	59. Defence Services—Non-Effective	8,41,90
60. Transfers to Defence Reserve Fund	1,42,25	60. Transfers to Defence Reserve Fund	1,42,25
		Total	49,83,92
<b>CONTRIBUTIONS AND MISCELLANEOUS ADJUSTMENT BETWEEN CENTRAL AND PROVINCIAL GOVERNMENTS</b>		<b>CONTRIBUTIONS AND MISCELLANEOUS ADJUSTMENT BETWEEN CENTRAL AND PROVINCIAL GOVERNMENTS</b>	
61. Grants-in-aid to Provincial Governments	3,14,27	61. Grants-in-aid to Provincial Governments	3,14,27
62. Miscellaneous Adjustments Between the Central and Provincial Governments	1,63	62. Miscellaneous Adjustments Between the Central and Provincial Governments	1,63
		Total	3,15,90
<b>EXTRAORDINARY ITEMS</b>		<b>EXTRAORDINARY ITEMS</b>	
63. Extraordinary charges	1,19	63. Extraordinary charges	1,19
64. Transfers to Revenue Reserve Fund	...	64. Transfers to Revenue Reserve Fund	...
		Total	1,19
<b>RAILWAY EXPENDITURE AS PER RAILWAY BUDGET</b>		<b>RAILWAY EXPENDITURE AS PER RAILWAY BUDGET</b>	
		TOTAL EXPENDITURE CHARGED TO REVENUE	29,98,92
<b>REVENUE TOTAL</b>		<b>REVENUE TOTAL</b>	
	1,19,41,88		1,19,34,71

## CHAPTER XII THE DEFENCE OF INDIA

The question of India's National Defence has been touched upon in the preceding chapters more than once, e.g., while discussing the powers of the Governor-General, or of the Federal Legislature. But these discussions have been more in the nature of passing references, than as part of a specific and comprehensive examination of the Constitutional provisions in regard to our National Defence.\* This chapter is, therefore, devoted to a comprehensive consideration of the Constitutional aspect of the Defence of organisation of India as a nation.

Sections of the Constitution Act (1935) relating to the organisation and provisions for the Defence of the country are scattered throughout the Act of 1935. They

\*\*\*It was natural that the authors of the Report, writing in the crisis of the spring of 1918, after mentioning with admiration the services rendered to the common cause by Indian arms, and expressing satisfaction at the increased recognition which was being given to such services, should have contented themselves with noting the urgency and importance of the Army questions which would emerge after peace had been attained. But this does not alter the fact that the constitutional future envisaged by Mr. Montagu's declaration of 20th August, 1917, and the new scheme elaborated in the Report and embodied in the Act of 1919, inherently involved a tremendous question which is not, we think, formulated or indeed referred to in the Report, viz., what, in view of the resolve that British India should advance to the goal of self-government within the Empire, is the nature of the arrangements which must be contemplated and in due course reached for her external defence and her internal security? We feel strongly that it would be a great disservice both to Britain and to India for this question now to be shirked, or for a method of treatment to be adopted which is confined to the search for temporary expedients wrapped up in soothing generalities, which only serve to foment suspicions of the bona fides of British policy on the one hand, and to divert attention from the ultimate and fundamental difficulties which Indian politicians themselves will have to face on the other. The best service we can render in this regard is to set out, plainly and fearlessly, for the consideration both of the British Parliament and of the political leaders of India, the special features of India's military problem which must be provided for before Army administration can be a function of a self-governing India."

Report of the Indian Statutory Commission, Volume I Survey.—Paragraph 112.