

COMMUNICATIONS ADDRESSED TO STATE GOVERNMENTS AND PRESS NOTE  
ISSUED BY THE COMMISSION

- (1) *D.O. letter No. D. 8885-B-II/51, dated the 22nd September, 1951, from Shri M. V. Rangachari, Joint Secretary, Ministry of Finance, Government of India, to the Finance Secretaries of all Part A States.*

As you may have seen from the papers and from answers to questions in Parliament, the Finance Commission is likely to be constituted about the middle of next month and may be expected to commence its work almost immediately. In anticipation of the formal constitution of the Commission, I thought it might be an advantage if I gave you informally some idea of the kind of material which should be prepared by you for presentation to the Commission, so that you might take the collection of the material in hand. This is purely an informal letter which I have shown to the Chairman-designate and which I shall place before the Commission as soon as it is constituted. If the Commission, or any of its members require additional information, I shall write to you further.

2. To begin with, the Commission will be concerned with three problems. The first is the allocation of the States' share of income-tax among the Part A States, which is now regulated by the Deshmukh Award. The second is the determination of grants payable to the States of Assam, Bihar, Orissa and West Bengal in lieu of the export duty on jute under Article 273 of the Constitution. The third is the determination of the general grants payable to Orissa and Assam (and such other States as may now ask for grants) under Article 275 of the Constitution.

3. In regard to the shares of income-tax and the grant payable in lieu of the jute export duty the representations made by the State Governments to Mr. Deshmukh when he was enquiring into this subject and the criticism of the State Governments of the Award made by him will be placed before the members of the Commission. In any further representation which the State Government may wish to make in this matter, it is unnecessary to repeat what has been urged by them in the earlier representations. It will be sufficient if a concise statement of the State's case is now prepared for the use of the Commission and sent so as to reach it by the 15th November at the latest. It will be convenient if six copies

are sent together with six copies of the representation made to Mr. Deshmukh in 1949. It is unnecessary, at this stage, to go into all the past historical arguments for or against a particular method of allocation and it will suffice if the State's case is prepared with reference to the existing circumstances and the needs of the State rather than with reference to historical arguments of rights and wrongs or abstract principles of social justice.

4. As regards general grants-in-aid to the States, at present only Assam and Orissa are in receipt of them. These two States may wish to press for a modification of the sums now paid to them and other States may conceivably wish to ask for grants-in-aid in addition to their share of income-tax and the specific grants, if any, received by them under Article 273 of the Constitution. Here again, it would assist the Commission if each State sent a self-contained statement of its case for assistance supported by a forecast of its revenue and expenditure for the next 5 years. This forecast should be by major heads of account and should be prepared on the basis of the existing level of taxation and expenditure. For the purposes of this forecast the State's share of income-tax and grant-in-aid whether for general purposes or in lieu of the jute export duty, may be taken as 'Nil'. In these States in which any of the former Indian States have been merged, the forecast should include the revenue and expenditure under the State heads in the merged States. The forecast should also provide for the bringing up of the level of administration in these areas to the level of the rest of the State. Subject to this, the forecast of revenue and expenditure should not provide for any further developmental or other expenditure. In determining the amount of Central revenue to be diverted to the State either by way of a share of income-tax or by way of grants, the Commission would doubtless take into account the needs of the State for development. I suggest, therefore, that the case for any increase in the existing grant or for fresh grants-in-aid should be prepared on the basis of the dislocation in the revenue position of the State at the existing level of taxation and expenditure. If the State bases its claim for a further grant on its additional requirements for developmental and other purposes, this should be set out in a separate memorandum and the expenditure involved should not be included in the forecast just mentioned. I enclose a form in which this forecast may be prepared and have added a few explanatory footnotes which may assist in its preparation. If on this, or any other point, you require further elucidation, would you kindly drop me a line?

## Forecast of Revenue and Expenditure

— State.

(In lakhs of rupees)

Heads	1951-52 Budget	1952-53	1953-54	1954-55	1955-56	1956-57
<b>REVENUE</b>						
.....						
.....						
.....						
.....						
<b>TOTAL REVENUE</b>						
<b>EXPENDITURE MET FROM REVENUE</b>						
.....						
.....						
.....						
.....						
<b>TOTAL EXPENDITURE</b>						
Surplus						
<b>NET</b>						
Deficit						

## NOTES

1. Figures should be given by Major Heads of account.
2. In the section dealing with revenue—
  - (a) The State share of income-tax and any grant received under Article 273 or 275 of the Constitution should be shown as nil.
  - (b) Full details should be given of any other grant from the Centre included in the estimate e.g. grant to make good the revenue-gap following federal financial integration, grants for rehabilitation of displaced persons, etc.
  - (c) Any amount included for expected improvement in revenue or any allowance made for the abandonment of any existing sources of State revenue or the reduction in their yield should be explained in detail in supplementary notes, indicating the amounts involved each year.

3. In the section dealing with expenditure—

- (a) No allowance should be made for fresh expenditure on developmental purposes.
- (b) If the estimates in any year include any special item of expenditure this should be indicated in explanatory notes.
- (c) The estimates should include provision for the bringing up of the level of administration in the areas forming the merged States. The amounts so included should be indicated in the explanatory notes.

4. All important variations in revenue or expenditure from year to year should be briefly explained in suitable footnotes.

- (2) *D.O. letter No. F.C. III-51, dated the 14th December 1951, from Shri M. V. Rangachari, Member-Secretary, to the Finance Secretaries of all Part B States except Jammu and Kashmir.*

As you might have seen from the papers the Finance Commission constituted under Article 280 of the Constitution has started its work and I am writing this letter to you on behalf of the Commission in regard to matters affecting the Part B States with which the Commission will have to deal.

So far as the Part B States are concerned, the Commission will have to make recommendations to the President regarding the share of the divisible taxes allocable to each of the States and also to make recommendations in regard to any request from a State for a general grant-in-aid. As you know, the actual payment of the States' share of any divisible taxes is subject to the terms of the agreement between the State and the Centre under Articles 278 and 306 of the Constitution.

At present the only divisible tax is income-tax other than tax on agricultural income and Article 270 regulates the distribution of this tax between the Centre and the States. The Commission would like to have any representation which your Government may wish to make in regard to the allocation of this tax between the Centre and the States and also your State's share of the share allocated to the States.

If in addition to your share of income-tax your State intends to ask for a general or specific grant a detailed note setting out the reasons for this request may also be sent. This statement should be supported by a forecast of the revenue and expenditure of the State for the next five years. This forecast should be by major heads of accounts and should be prepared on the basis of the existing level of taxation and expenditure. The forecast of expenditure should not provide for any further new expenditure on development. In determining the scale of Central assistance whether by way of a devolution of revenue or a general grant from revenue the Commission would doubtless take into account the needs of the State for development. If the State bases its claim for a grant on its requirements for developmental or other purposes this should be set out in a separate memorandum and the expenditure involved should not be included in the forecast just mentioned. I enclose a form in which this forecast may be prepared and have added a few explanatory foot-notes which may assist in its preparation. If on this or any other point you require further elucidation, will you kindly let me know?

The Commission will be glad if the case for your State with seven spare copies is sent to reach them by the 1st of February at the latest.

## Forecast of Revenue and Expenditure

State.

(In lakhs of rupees)

Heads	1951-52 Budget	1952-53	1953-54	1954-55	1955-56	1956-57
<b>REVENUE</b>						
.....						
.....						
.....						
.....						
<b>TOTAL REVENUE</b>						
<b>EXPENDITURE MET FROM REVENUE</b>						
.....						
.....						
.....						
.....						
<b>TOTAL EXPENDITURE</b>						
Surplus						
<b>NET</b>						
Deficit						

## NOTES

- (1) Figures should be by Major Heads of accounts.
- (2) In the section dealing with revenue—
  - (a) the State's share of income-tax received from the Centre should be shown separately.
  - (b) Full details should be given of other grant from the Centre included in the estimate such as the grant to cover the revenue gap following federal financial integration, grants for rehabilitation of displaced persons, Grow More Food, etc.
  - (c) Any amount included for anticipated improvement in revenue or any allowance made for the abandonment of any existing sources of State revenue or the reduction in their yield should be explained in supplementary notes indicating the amount involved each year. In those States

in which internal customs duties have to be replaced gradually by Sales taxes. the revenue from each of the sources should be shown separately for each year.

(3) In the section dealing with expenditure—

(a) No allowance should be made for fresh expenditure on developmental purposes.

(b) If the estimates in any year include any special item of expenditure this should be indicated in explanatory notes.

(c) The estimates should include provision for any additional expenditure that may have to be incurred on the reorganisation of administration in those Unions formed by the merger of a large number of Indian States, viz. Rajasthan, Saurashtra, Madhya Bharat and PEPSU. The amount so included should be indicated in a separate note.

(4) All important variations in revenue or expenditure from year to year should be briefly explained in suitable foot-notes.

- (3) D.O. letter No. F.C. II/(17)/52, dated the 19th September 1952, from Shri M. V. Rangachari, Member-Secretary, to the Finance Secretaries of all Part A and Part B States except Jammu and Kashmir.

The question was raised by more than one State during the Commission's recent visits to the States that one or more of the Union Excises should also be divided between the Centre and the States so as to increase the resources available to the latter. The Commission would be grateful if you would kindly send them a memorandum setting out the views of your Government on this subject. In particular the Commission would like to have the views of the State Government as to whether *all* the excises or only one or more of them should be divided, the relative share of the Centre and the States and the basis on which the States' share of any excise which your Government may wish to have divided should be allocated among the States.

The State's memorandum may be sent as soon as possible with 6 spare copies and in any case by the 10th October 1952.



(4) Press Note dated the 19th February 1952 issued by the Finance Commission

Among the questions on which the Finance Commission will have to make recommendations are:—

- (i) the distribution of the net proceeds of income-tax between the Union and the States and the allocation of the States' share among the States [*vide* Articles 270 and 280(3) (a) of the Constitution] and
- (ii) the principles which should govern the grants-in-aid of the revenues of the States out of the Consolidated Fund of India [*vide* Article 280(3) (b) read with Article 275 of Constitution].

At present, 50 per cent of the divisible net proceeds of income-tax (other than Corporation Tax) is assigned to the States and distributed among them in the following percentage ratios: Assam—3; Bihar—12·5; Bombay—21; Madhya Pradesh—6; Madras—17·5; Orissa—3; Punjab—5·5; Uttar Pradesh—18; and West Bengal—13·5.

Seven out of the eight Part B States are also now entitled to share in the proceeds of the income-tax along with the nine Part A States.

Various bases have been suggested for allocating income-tax:—

- (i) the *collection* of income-tax in the various States;
- (ii) the amount of income-tax realised in respect of incomes, wherever earned, of individuals *resident* in the different States;
- (iii) the collection of income-tax in the various States adjusted with reference to the *origin* of the income;
- (iv) the relative *population* of each State;
- (v) the relative volume of *industrial labour* in each State;
- (vi) the *needs* of the different States according to various criteria; and
- (vii) different combinations of the above factors.

Claims are advanced for grants-in-aid on the basis of needs for balancing the budget, for bringing up the level of administration and raising the standard of social services in certain States and backward regions, for implementing some of the Directive Principles of the Constitution, for economic development, for bearing special additional burdens or dealing with disabilities consequent upon partition, etc., etc.

Further points which arise with respect to grants-in-aid are whether the grants should be general or specific, conditional or unconditional.

Before making their recommendations, the Finance Commission would welcome the views of all who may have made a study of these questions. The views may be set forth in a written memorandum and sent to the Secretary, Finance Commission, Faridkot House, Lytton Road, New Delhi, on or before April 15, 1952.