

APPENDIX I

(See paragraph 2)

CORRESPONDENCE WITH UNION AND STATE GOVERNMENTS AND CIVIL ACCOUNTANTS GENERAL AND COMPTROLLERS, AND PRESS NOTE ISSUED BY THE COMMISSION.

- (1) Letter No OSD-135-152/56, dated the 20th April 1956 from Shri M. V. Rangachari, Officer on Special Duty, Ministry of Finance, to the Finance Secretaries, all Part A and Part B States.

As you know, a new Finance Commission is being constituted and will be taking office on the 1st June 1956. As on the last occasion we feel that it will be an advantage if, in anticipation of the formal constitution of the Commission, we gave you some idea of the data which the Commission are likely to require in connection with their work. I am writing this letter after informal consultation with the Chairman-designate and other Members of the Commission. It is not comprehensive and is only the first request for information. Further requests will follow as the Commission's work develops.

2. This letter deals primarily with three matters on which the Commission will, in any case, have to make recommendation to the President, viz., the allocation of income tax and other divisible taxes, the amounts to be paid as grants-in-aid under article 273 of the Constitution, the determination of the States in need of assistance and the grants-in-aid to be paid to them under article 275. There may be other matters which the President may refer to the Commission. The State Governments will be addressed in due course for any material, which the Commission may require to deal with these specific issues, after they have received the formal reference from the President.

3. As regards the allocation and distribution of income tax, the Commission will take into account the considerations which have influenced past settlements. It is, therefore, not necessary in such representations as the State Governments may wish to make to go into the past history in any great detail. It would assist the Commission if each State sends up a self-contained memorandum putting forward its case for the modification, if any, suggested in the present basis.

4. At present three excise duties, *viz.*, those on matches, tobacco and vegetable products, are divided between the Centre and the States. The Commission would welcome any comments the State Governments may have on the existing division and any suggestions in regard to the future allocation of these or other excise duties.

5. Grants-in-aid under article 273 of the Constitution concern only the States of Assam, Bihar, Orissa and West Bengal. The Governments of these States would, doubtless, indicate whether they consider any modification necessary in the amounts of the grants as they now stand prescribed and explain their case for the suggested change.

6. For determining the States in need of assistance and grants-in-aid to be paid to them under the substantive portion of article 275 (1), the Commission would require from all States a forecast year by year of the estimated revenue and expenditure for the five years ending 1961-62. This forecast may be prepared in the form appended to this letter. A number of notes indicating the basis on which the forecast should be prepared and further details which the Commission are likely to require have been given in this form for guidance.

7. The forecast mentioned in the previous paragraph may be prepared for the State as it is at present constituted. Some of these States will be affected by the impending reorganisation. These States should send a subsidiary statement showing the effect on the revenue and expenditure of the transfer of any area from that State to other States, separately for each area going into another State. Thus Bombay will have four subsidiary statements, Hyderabad three, Madhya Pradesh and Madras two each and Travancore-Cochin one. The adjustments between the States due to these transfers will be carried out in the Commission's office here. We shall also make adjustments for any Centrally administered area and Part C State merging in the new States by reorganisation. For the purpose of these statements, it may be assumed that the reorganisation will take place on the lines proposed in the States Reorganisation Bill as introduced in Parliament. The figures may be subsequently readjusted in the light of such changes as Parliament may make in the Bill.

8. I shall be grateful if the memorandum and the statements asked for in this letter are sent to the Secretary to the Commission by the 1st of July 1956 with 7 spare copies.

9. If there is any point on which you require clarification or further instructions, would you kindly write to me?

Forecast of Revenue and Expenditure.

_____ State.

(Rupees in lakhs)

Heads						
	1957-58 Budget	1957-58	1958-59	1959-60	1960-61	1961-62
Revenue						
Total Revenue						
Expenditure met from Revenue.						
Total Expenditure						
Net Surplus						
Deficit						

NOTES

1. Figures should be given by major heads of account.
2. Any modification in the forecast as given to the Planning Commission should be indicated and explained briefly.
3. In the revenue estimates--
 - (a) the State's share of income tax and divisible excises and any grant received under article 271 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; and

- (c) any amount included for anticipated improvements in revenue or any allowance made for the abandonment of any existing source of State revenue or the reduction in the yield should be explained in detail in supplementary notes, indicating the amounts involved in each year.

4. A statement showing the recommendations of the Taxation Enquiry Commission which have been implemented, the resulting increase in revenue, and the estimated additional revenue if the remaining recommendations are implemented, should be attached.

5. In the expenditure estimates—

(a) no allowance should be made for fresh expenditure on development but estimates of such expenditure should be given in brackets below each major head for each year ;

(b) if they include any special item of expenditure, this should be indicated in explanatory notes ;

(c) provision should be included for recurring expenditure on completed schemes in the first five year plan, which would not form part of the provision for the second plan. A rough indication of this increased recurring expenditure included in the forecast may be given year by year ; and

(d) provision should be included for the normal growth of expenditure.

6. Provision for debt services should be confined to interest charges. It should not include any provision for repayment of amortisation or debt but should include provision for any obligatory sinking fund in respect of public loans. The amounts so included in each year should be separately indicated.

7. A subsidiary statement should be attached showing the revenue and expenditure of any area, which would be transferred from the existing State to a new State in accordance with the provisions of the States Reorganisation Bill.

8. A statement should be appended showing year by year the total expenditure on famine and famine relief in the last ten years and the amount of assistance received from the Centre by way of supply of foodgrains at concessional prices.

(2) *Letter No. OSD.153-157/56, dated the 20th April 1956 from Shri M. V. Rangachari, Officer on Special Duty, Ministry of Finance, to the Chief Commissioners of Ajmer, Bhopal, Coorg and Kutch and the Finance Secretary, Vindhya Pradesh.*

I enclose a copy of a letter addressed to the Finance Secretaries of all Part A and Part B States asking for certain material to be furnished in connection with the work of the Finance Commission. I shall be grateful if in respect of your State you would also furnish

information on the lines asked for in that letter subject to such modifications as may be necessary arising out of the present position of your State as a Part C State.

(3) Note dated the 30th April 1956 from Shri M. V. Rangachari, Officer on Special Duty, to the Government of India, Ministry of Finance (Budget Division).

Will the Budget Division kindly arrange to collect the following material for the information and use of the Finance Commission?

- (a) A forecast of the revenue and expenditure of the Central Government by major heads of account for the next five years in the form attached.
- (b) A statement showing for each of the five years ending 1955-56 the grants made to the States from revenue with brief notes regarding the basis on which the grant was calculated and the purpose of the grant. (For purposes of this statement the payment of the States' share of income tax and Union excises should not be treated as a grant.)
- (c) A statement showing the capital grants (but not loans), if any, made to the States in the last five years and provided for in the budget for the current year with explanations as in (b) above.

2. Seven copies of the material assembled may be kept ready for transmission to the Commission by the end of June 1956.

Forecast of Revenue and Expenditure

(Rupees in lakhs)

Head	1956-57	1957-58	1958-59	1959-60	1960-61	1961-62
Revenue						
Total Revenue						

Forecast of Revenue and Expenditure—concl'd.

(Rupees in lakhs)						
Head	1956-57	1957-58	1958-59	1959-60	1960-61	1961-62
Expenditure met from Revenue.						
Total Expenditure						
Net						
Surplus						
Deficit						

NOTES

Figures should be given by major heads of account.

In the section dealing with revenue, no deduction should be made on account of the States' share of income tax or estate duty but a separate statement should be furnished giving an estimate for each year of the divisible pool of income tax and the total of the distributable amount of estate duty.

A statement giving a breakdown by articles of the provision made under Union excise duties must be attached.

Brief explanations should be given of any large variations in the revenue estimates from year to year.

In the expenditure estimates details of the provision included in each year for grants to States should be given.

The share of divisible excises payable to the States and included in the expenditure estimates should be given separately.

As on the revenue side variations in the estimates of expenditure from year to year should be briefly explained.

Both the revenue and expenditure estimates should be on the existing level of taxation and the present scale of normal expenditure. No provision should be included for fresh development expenditure but an indication should be given in a separate statement of the magnitude of the expenditure in each of these five years.

If the estimates of expenditure in any year include special items, this should be indicated in suitable explanatory notes.

A statement should be added showing the recommendations of the Taxation Enquiry Commission which have been implemented and the total annual yield from such taxes included in the revenue estimates. An indication should also be given of the annual increase in revenue that may be expected if the remaining recommendations are implemented.

(4) *Demer-official letter No. OSD-111/56, dated 30th April 1956 from
 Sri M. V. Rangachari, Officer on Special Duty, Ministry of
 Finance, to all Civil Accountants General and Comptrollers.*

We are engaged in the collection of preliminary data for the use of the Finance Commission which, as you may have seen in the papers, will be formally constituted on 1st June 1956. The pattern of borrowing by the States from the Centre in recent years is one likely to interest the Commission and they would want information about the rate of interest and the terms of repayment of the loans taken from the Centre by the various States between 15th August 1947 and 31st March 1956. I shall be grateful if you would kindly have a statement prepared separately for each year in the form enclosed with this letter in respect of loans taken from the Centre by the State Government whose accounts are kept by you. These statements may be compiled and sent so as to reach us by 30th June 1956 at the latest

2. If there is any point on which you require further clarification, will you kindly drop me a line?

Loans from the Central Government taken between 15th August 1947 and 31st March 1956.

State of — — —

(Rupees in lakhs)

Purpose of Loan	Amount sanctioned	Rate of Interest	Date and terms of repayment	Balance on 31st March 1956	Remarks
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1. A separate statement should be prepared for each year.
2. The purpose of the loan should be briefly stated such as "for Bhakra Nangal", "for Tungabhadra", "for rehabilitation of displaced persons", "for Grow More Food", etc.

(5) Letter No. P-70-V (Confidential), dated the 2nd May 1956 from Shri R. C. Joshi, Deputy Secretary to the Government of Bombay, Finance Department, to the Officer on Special Duty, Ministry of Finance.

In its letter No. OSD.135/56, dated 20th April, 1956, the Finance Commission has called for a forecast, year by year, of the estimated revenue and expenditure for the 5 years ending 1961-62 for the Bombay State as constituted at present and also separately for each of the four areas into which it is proposed to be split up.

The reorganisation of the State will not only affect the existing boundaries of the States but will also affect the pattern of revenue and expenditure in the four areas of the present Bombay State due to their integration with the neighbouring States. At present, there is no clear idea of what the administrative set-up in the new States will be or how the present plan will be divided between the different areas. It is difficult to split up the forecast regionwise even on the assumption that the present set up will continue since the accounts are not maintained according to districts.

In the circumstances, I am to request for further clarification as to how the forecast in respect of the four regions into which this State is proposed to be split up can be worked out.

(6) Letter No. P-709/X-FC-1/56-57, dated the 7th May 1956 from Shri B. B. Lal, I.C.S., Finance Secretary to the Government of Uttar Pradesh, to the Officer on Special Duty, Ministry of Finance.

I am directed to acknowledge receipt of your letter No. OSD-137/56, dated April 20, 1956 asking for certain preliminary information for the use of the newly constituted Finance Commission and to seek clarification on the following points:—

- (a) Note 2 in the form enclosed with your letter suggests that if the forecast now to be given varies from that given to the Planning Commission the variation should be explained. It is not understood how this can be done since the forecast intimated to the Commission was in respect of the years 1956—61 while that required now would be for 1957—62. Also the forecast given to the Commission

was not on a year to year basis but in two blocks one showing the aggregate estimates for the first two years and the other for the next three years.

- (b) The implication of the word 'Development' occurring in note 5(a) *ibid* is not clear. Will all Second Plan expenditure be treated as fresh development expenditure and shown in brackets separately? If not, what precisely will be the categories of expenditure which is to be regarded as 'fresh expenditure on development'?
- (c) As regards debt services, it is presumed that interest payable on public loans raised during the period of the forecast and provision for obligatory sinking funds for such loans will also be taken into account. The forecast of public loans given to the Planning Commission for the Second Plan period will form the basis for this purpose. The amount of loans from the Centre, however, which may be received from 1956-57, is a wholly undecided and unknown factor and will depend on the size of the capital outlay during the period of the forecast (1957-62) which may be left uncovered by public loans. Interest charges on these Central loans will inevitably have to be included in the forecast.

2. I am to request that the points mentioned above may kindly be considered and clarified as early as possible.

(7) Letter No. OSD/188/56, dated the 15th May 1956 from Shri M. V. Rangachari, Officer on Special Duty, Ministry of Finance, to the Finance Secretary to the Government of Bombay, (copy with a copy of the letter replied to forwarded to the Finance Secretaries of Madhya Pradesh, Hyderabad, Madras and Travancore-Cochin).

I am directed to refer to Shri Joshi's confidential letter No. P-70-V (Confidential), dated the 2nd May 1956 and to state that for purposes of the Commission it would suffice if any forecast prepared by the State Government for the States Reorganisation Commission on the existing pattern of taxation and administration for the various areas, which are being transferred to other States or constituted into new States, is supplied to them. If no such forecast was prepared but past actuals for these areas were collected in consultation with the Accountant General, these actuals may be supplied.

- (8) *Letter No. OSD-189/56, dated the 15th May 1956 from Shri M. V. Rangachari, Officer on Special Duty, Ministry of Finance, to the Finance Secretary to the Government of Uttar Pradesh, (copy with a copy of the letter replied to forwarded to the Finance Secretaries of all other Part A and Part B States).*

I am directed to refer to your letter No. P-709/X-FC-1/56-57, dated the 7th May 1956 and to state that the replies to the points raised by you are as follows:—

- (a) In view of the disparity pointed out by you it will be sufficient if any variation between the total figures of revenue and expenditure for the years 1958-59 to 1960-61 inclusive in the forecast prepared for the Commission and the figures given for the corresponding years to the Planning Commission are indicated and explained.
- (b) For purposes of the forecast, all expenditure on the second plan to be met from the Revenue Budget may be treated as fresh expenditure on development.
- (c) Interest payable on public loans to be raised during the period of the forecast may also be taken into account. The total amount of the estimated borrowings and the amount included in each year for the servicing of the new borrowings should be explained in a separate note. Unless it is the policy of the Government to have an obligatory sinking fund for all the public loans, no provision need be included for such sinking funds. Similarly, any provision made for borrowing from the Centre and payment of interest thereon may be included and explained.

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- (9) *Letter No. FC.1-B/56, dated 7th June 1956 from Shri H. B. Bhar, Secretary, Finance Commission, to the Finance Secretaries of all Part A and Part B States.*

Will you kindly refer to our letter No. OSD-135-152/56, dated 20th April 1956 in regard to the material required for the Finance Commission?

2. As you may have seen from the paper, the President has made a formal order constituting the Commission and containing the terms of reference to them. I enclose a copy of the order for the information of the State Government.

3. With reference to the two terms of reference not covered by the data asked for in our letter dated 20th April 1956, namely, the distribution of the net proceeds of the estate duty on property other than agricultural land, and the review of the terms of the loans taken by the State Government from the Centre between 15th August 1947 and 31st March 1956, I shall be glad if you kindly send self-contained memoranda setting out the views of the State Government on these matters.

4. At their meeting earlier this week, the Commission considered the subsidiary points on which information should be obtained from the State Governments. I enclose a statement of these points and I shall be glad if you kindly arrange to send a memorandum on each of them separately for submission to the Commission. In compiling this memorandum the figures of receipts or expenditure pertaining to the years 1955-56 and 1956-57 may be based on the revised and budget estimates respectively of these years. For States likely to be affected by the impending reorganisation, separate figures may be given wherever possible in subsidiary statements for the areas likely to be transferred from the State, as at present constituted, to another State, separately for each such area.

5. The additional memoranda asked for in paragraphs 3 and 4 above may be sent with ten copies so as to reach the Commission's office on or before 10th August 1956.

LIST OF SUBSIDIARY POINTS

1. Rates of the principal taxes (agricultural income tax, stamps, motor vehicles, entertainment tax, electricity duty, general sales tax and other taxes and duties) in 1951-52 and the changes therein from 1952-53 to 1956-57.

2. Basis and rates of land revenue assessment (including surcharge, special rates, etc.) in 1951-52, and changes during the period 1952-53 to 1956-57.

3. Excise revenue in 1951-52, the changes therein and the results of prohibition during 1952-53 to 1956-57, and the future plans of the State Governments in regard to prohibition.

4. Amount of food subsidies from State revenue during each of the five years from 1952-53 to 1956-57.

5. Receipts, payments and balances in the State Road Fund and the Famine Relief Fund, if any, for each of the year 1952-53 to 1956-57.
6. Expenditure from State revenue in each financial year from 15th August 1947 to 31st March 1957 on account of relief and rehabilitation of displaced persons.
7. Revenue (indicating separately grants from Government) of local bodies and expenditure incurred by them on roads, education, medical and health services in the last three years for which actuals are available.
8. Mileage of national highways and A, B and C class roads on 1st April 1948, 1st April 1952 and 1st April 1956.
9. Strength of establishment under Police (with separate figures for border police where such police is maintained separately), General Administration, Justice and Jails on 1st April 1948, 1st April 1952 and 1st April 1956.
10. Number of primary schools, pupils and teachers therein on 1st April 1948, 1st April 1952 and 1st April 1956.
11. Number of hospitals and dispensaries, total number of beds, nurses, doctors and midwives, rural and urban separately, on 1st April 1948, 1st April 1952 and 1st April 1956.
12. The nature of economy measures, if any, carried out by the State Government in the years 1952-53 to 1955-56 inclusive and their results.
13. Programme of agrarian reforms in the State, their effect on revenue and expenditure during 1954-55 as compared with 1947-48 and their probable effects during the period 1957-58 to 1961-62.
14. Financial results of the working of State commercial and industrial undertakings like road transport, electricity schemes, industries, etc., for which commercial accounts are maintained, during each of the years 1952-53 to 1956-57.
15. Grow More Food Schemes—1952-53 to 1956-57. Give for each year particulars of (i) gross expenditure, (ii) loans and (iii) grants received from the Centre. Also give estimated increase in food production over this period.
16. Position of taccavi and land improvement loans—advances, recoveries and remissions and write-offs during each of the five years

upto and inclusive of 1955-56 and total outstandings and overdue arrears at the end of each of these years.

17. Revisions of pay and allowances of State employees in each of the last five years and the consequent increase in expenditure.

18. Gross expenditure on Community Projects and National Extension Service schemes and the amount of grants-in-aid and loans separately from the Centre during each of the years 1952-53 to 1956-57.

19. Kilowatts of energy generated in 1948, 1952 and 1956 by (i) State undertakings (excluding purchases from the Damodar Valley Corporation in the case of West Bengal and Bihar) and (ii) private undertakings.

20. Gross expenditure on handloom, small scale industries, handicrafts, sericulture and khadi and village industries in each of the years from 1952-53 to 1956-57 and assistance from the Centre by way of (i) loans and (ii) grants.

21. Particulars of the amounts received from bodies like the Indian Council of Agricultural Research, Indian Cotton Committee, Indian Jute Committee, etc., during 1953-54, 1954-55 and 1955-56, the purposes for which they were received, the expenditure incurred against these grants and whether any matching expenditure was incurred from State revenues. If latter, figures of such expenditure may be given.

22. Particulars of the cesses levied by the State, their purposes, the total proceeds of each cess, the amounts, if any, thereof transferred to local bodies or spent directly by the State Government during 1953-54, 1954-55 and 1955-56.

23. New State enterprises established, or addition to and expansion of existing enterprises, during 1952-53 to 1956-57 and those proposed to be established during 1957-58 to 1961-62. (Only schemes costing Rs. 10 lakhs and over need be given)

24. Debt position of the State showing the total outstanding debt to the public and the Centre on 1st April 1952 and 1st April 1957 and the interest-yielding assets held against such debt (see for illustration the statement at pages 89 and 90 of the Explanatory Memorandum on the Central Budget for 1956-57).

(10) Demi-official letter No. FC.1-B/56, dated the 29th June 1956 from Shri H. B. Bhar, Secretary to the Finance Commission, to the Finance Secretaries of all Part A and Part B States (except Bihar).

Will you kindly refer to Shri Rangachari's letter No. OSD-135-152/56, dated the 20th April 1956, wherein the State Government was requested, *inter alia*, to submit an annual forecast

1. D.O. No. 41/SF/55, dated 11th January, 1955 from Shri M. V. Rangachari, Secretary to the Government of India, Ministry of Finance.
2. D.O. No. 1 (104)-BII/55, dated 13th December 1955, from Shri H. M. Patel, Secretary to the Government of India, Ministry of Finance.
3. D.O. No. F. 1 (104)-BII/55, dated 13th October, 1955, from Shri H. M. Patel, Secretary to the Government of India, Ministry of Finance.

of revenue and expenditure from 1956-57 to 1961-62? In the letters indicated in the margin suggestions for reclassification of certain expenditure from revenue to capital were made to the State Government. We understand that your State Government has accepted all or most of these suggestions and has also given effect to them in the budget estimates of the current year. I would be grateful if, while submitting the forecast of revenue and expenditure, an indication is given of the amounts for 1956-57, under the individual major heads of expenditure, which on account of the reclassifications have been transferred from revenue to capital. In

case any or some of the suggestions contained in the three letters mentioned in the margin have not been given effect to in the budget estimates for 1956-57, the amounts under the different major heads of expenditure, which could be transferred from revenue to capital in 1956-57, if the suggested reclassification is adopted, may kindly be indicated.

(11) Letter No. P-1056/X-FC-1/56-57, dated the 9th July 1956, from Shri B. B. Lal, I.C.S., Finance Secretary to the Government of Uttar Pradesh, to the Secretary, Finance Commission.

I am directed to refer to Shri Rangachari's letter No. OSD-189/56, dated May 15, 1956, and to say that it would appear that even the differences between the figures given to the Planning Commission and those that may be given to the Finance Commission for the period 1958-61 would not be easy to explain. The forecast for the Planning Commission was prepared about two years ago, while the figures being collected for the Finance Commission have taken the budget estimates for 1956-57 as a starting point. This factor in itself is likely to be responsible for a difference in a majority of cases. Moreover, under several heads, the forecast suggested by the State Government

was subsequently revised by the Planning Commission on a total five year basis and the overall forecast thus worked out cannot possibly be broken up on a year to year basis except in a purely hypothetical manner. While, therefore, it may be useful to explain the important variations from year to year in the forecast for the Finance Commission itself, perhaps a comparison of the forecast prepared for the Planning Commission with that prepared for the Finance Commission for a few overlapping years may not be very helpful. In view of these considerations, I am to express the hope that the Finance Commission will not consider it necessary to ask for such variations for the years 1958-61 being explained.

(12) *Note No. 13(2)-B/56, dated the 18th July 1956 from Shri H. B. Bhar, Secretary to the Finance Commission, to the Government of India, Ministry of Finance, Department of Economic Affairs and Department of Revenue (Central Board of Revenue).*

The Ministry of Finance (Department of Economic Affairs)/Central Board of Revenue are aware that the Finance Commission are required to recommend the principles which should govern the distribution of the net proceeds of the estate duty in respect of property other than agricultural land. In the distribution itself, the Government of India has a minor interest as it will get only the share pertaining to the Centrally administered areas. But the Government of India will have to deal with the practical problems involved in the implementation of any distribution scheme and it should be greatly interested in the administrative aspects of the question. The Commission would be grateful if the Ministry of Finance, (Department of Economic Affairs)/Central Board of Revenue will kindly state the principles which, in its opinion, may be adopted for this purpose.

(13) *Letter No. FC.1(4)-B/56, dated the 25th July 1956 from Shri H. B. Bhar, Secretary to the Finance Commission, to the Finance Secretary to the Government of Uttar Pradesh. (Copy, with a copy of the letter replied to, forwarded to the Finance Secretaries of all the other Part A and Part B States, Ajmer, Bhopal, Coorg, Kutch and Vindhya Pradesh).*

I am to invite a reference to your letter No. F-1056/X FC-1/56-57 dated 9th July 1956 and to state that if, on account of the time-lag between the preparation of the forecasts for the Planning Commission and for the Finance Commission, there is likely to be any fairly substantial differences between the two forecasts, this should be suit-

not be possible to compare the annual forecasts for the Finance Commission with those submitted to the Planning Commission on account of the latter having altered the figures on a total five-year basis. In view of this, the provisions under the individual heads in the 1956-57 budget estimates should be deducted from the totals, of the five-year period from 1956-57 to 1960-61, agreed to with the Planning Commission, and the balance amount should be compared with the totals, under these heads, of the amounts for the four years 1957-58, 1958-59, 1959-60 and 1960-61 appearing in the forecast for the Finance Commission. Variations between these two sets of figures should be suitably explained.

(14) *Letter No. FC. 29 (1)-B/56, dated the 24th May 1957 from Shri H. B. Bhar, Secretary, Finance Commission, to the Finance Secretaries of all State Governments.*

I am directed to enclose, for the information of the State Government, a copy of a letter from the Government of India to the Finance Commission intimating two additional references which the President has been pleased to decide should be made to the Commission.

2. In regard to the first reference, namely, that dealing with the distribution of the additional duty of excise on textiles, tobacco and sugar, the Commission would like to have the following information:—

- (a) The rate at which the taxes are now levied on these commodities in your State under the State's Sales Tax Act or other similar law.
- (b) The sums realised by the State Government in each of the last three financial years from such taxes on each commodity and the basis on which the figures of revenue have been worked out.
- (c) The consumption of each of the commodities in the State in the last three years and the basis on which this has been computed.

In furnishing information regarding collection and consumption for the States affected by reorganisation, the figures upto 31st October 1956 may be worked out for the former States and distributed on a population basis among the successor States.

- (d) The total receipts from sales taxes including sales tax on motor spirit and tobacco tax, if any.

3. The Commission would like to have the suggestions of the State Government in regard to the principles of distribution of the net proceeds of this additional duty.

4. In regard to the second reference, namely, the principles of the distribution of the net proceeds of the proposed tax on Railway fares, the Commission would like to have the suggestions of the State Government.

5. It is requested that the material asked for in this letter may be sent to reach the Commission's office by the 30th of June 1957 at the latest

(15) *Letter No. FC.28(1)-B/56, dated the 24th May 1957 from Shri H. B. Bhar, Secretary, Finance Commission, to the Secretary, Railway Board.*

I am directed to state that the President has been pleased to requested the Finance Commission to make recommendations to him as to the principles which should govern the distribution, under article 269 of the Constitution, of the net proceeds of the tax on railway fares proposed to be levied by the Railway Passengers Fare Bill 1957. In this connection the Commission would like to have the following information:—

- (1) the route mileage (separately for broad, metre and narrow gauges) of each zone and the distribution of such mileage among the present States covered by the zone;
- (2) the passenger earnings gauge-wise for each railway zone in the three years ending 1956-57, and distributed by the existing States covered by the zone;
- (3) the passenger earnings of the zone in those three years distributed, amongst the existing States, on the basis of the location of the originating stations in the States;
- (4) the passenger miles in each zone distributed amongst the existing States for those three years.

The Commission would welcome any suggestions which the Railway Board might make for the distribution of the proceeds of the tax.

We would be grateful if the required material is sent to us as early as possible and preferably within a fortnight. The Commission would also like to meet an official of the Railway Ministry later on.

(16) *Press Note dated 12th July 1956 issued by the Finance Commission.*

The Finance Commission have to make recommendations to the President on the following matters:—

- (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;
- (ii) the distribution of other divisible Central taxes like Union excise duties;
- (iii) the amounts to be paid to the States of Assam, Bihar, Orissa and West Bengal in lieu of the assignment of any share of the export duty on jute and jute products;
- (iv) the principles which should govern the grants-in-aid of the revenues of the States out of the Consolidated Fund of India;
- (v) the States which are in need of assistance by way of grants-in-aid of revenues, and the sums to be paid to those States, having regard, among other considerations, to the requirements of the second five year plan and the efforts made by those States to raise additional revenue from the sources available to them;
- (vi) the principles which should govern the distribution of the net proceeds of the estate duty in respect of property other than agricultural land;
- (vii) the modifications, if any, in the rates of interest and the terms of repayment of the loans made to the various States by the Government of India between 15th August 1947 and 31st March 1956.

2. At present 55 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:

State	Percentage
Andhra	5.49
Assam	2.25
Bihar	9.75
Bombay	17.50
Hyderabad	4.50
Madhya Bharat	1.75
Madhy Pradesh	5.25
Madras	9.56

Mysore	1.75
Orissa	2.29
Pepsu	2.78
Punjab	3.23
Rajasthan	3.50
Saurashtra	4.00
Travancore-Cochin	2.50
Uttar Pradesh	13.75
West Bengal	11.25

The shares of the States have to be refixed as a result of the impending reorganisation and new percentages recommended for the reorganised States.

The share to be retained by the Centre also has to be determined.

The present allocation is broadly worked out on the basis of 80 per cent by population and 20 per cent by collection.

The basis of distribution of income tax has always been a matter of controversy. Various bases have been suggested for allocating income tax :

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

3. Three Union duties of excise, namely, those on matches, tobacco and vegetable products, are now divisible between the Centre and the States, and 40 per cent of the net proceeds are distributed among the States on the basis of population. The quantum of the taxes to be transferred to the States, the excises to be continued or made divisible and the basis of distribution all fall to be considered by the Commission.

4. The first Finance Commission recommended that grants-in-aid of Rs. 75 lakhs each to Assam and Bihar, Rs. 15 lakhs to Orissa, and

Rs. 150 lakhs to West Bengal be paid each year in lieu of the assignment of a share of the export duty on jute. This Commission has to consider whether any change in the figures suggested by the first Commission and accepted by Government is necessary.

5. In chapter VII of their Report, the last Commission formulated certain principles to govern the payment of grants-in-aid to the States which they themselves had applied in making their recommendations. This Commission will re-examine these principles in the light of subsequent developments and changes in the practice in other countries, and indicate any changes necessary in them.

6. The Commission have to make recommendations regarding the States in need of assistance and the sums to be prescribed as grants-in-aid of the revenues of such States. At present Assam, Mysore, Orissa, Punjab, Saurashtra, Travancore-Cochin and West Bengal are in receipt of general grants-in-aid as a result of the recommendations of the last Commission. This Commission will re-examine the financial position of all the States and make recommendations to the President regarding the States in need of assistance and the sums to be prescribed as grants-in-aid of the revenues of such States. A large variety of considerations may enter into the determination of the needs of the States and these may differ from State to State. The Commission will also consider the nature of the grants-in-aid, such as whether they should be fixed or progressive, general or specific, conditional or unconditional.

In addition to the general grants-in-aid which some of them may be receiving, Bihar, Hyderabad, Madhya Bharat, Madhya Pradesh, Orissa, Patiala and East Punjab States Union, Punjab and Rajasthan are in receipt of special grants-in-aid for the expansion of primary education. The Commission will assess the results achieved by the specific grants given to these States.

7. The net proceeds of the estate duty on property other than agricultural land is now being provisionally distributed among the States in the same way as the States' share of the net proceeds of taxes on income other than the corporation tax. In other words, it is being distributed by the percentage ratios fixed for the States for income tax except that the Centre does not retain any portion of the receipts except those attributable to Part C States. A more permanent basis of distribution has to be formulated by law of Parliament. An important issue, in this connection, would be whether the duty should be distributed on the basis of percentage

ratios, whether arrived at on the basis of the percentage ratios prescribed for the distribution of income tax or otherwise, or the distribution should be on the basis of assessments, location of the property taxed, residence of assessee, etc

8. Central loans have been given to the States for a variety of purposes ranging from the construction of big irrigation and multi-purpose projects to the construction of minor irrigation works, grow-more-food schemes, famine works, rehabilitation of displaced persons etc. Some of them have also been given loans to cover budgetary deficits. The rates of interest and terms of repayment of these loans vary for different categories of loans. These will be reviewed and any changes necessary in the interests of sound finance indicated.

9. The Finance Commission would welcome the views of those who are interested in and have made a study of these questions. They would be glad if such views could be embodied in a self-contained memorandum and sent to the Secretary, Finance Commission, to reach him on or before 30th November 1956.

APPENDIX II

(See paragraph 4)

THE FINANCE COMMISSION (MISCELLANEOUS PROVISIONS) ACT, 1951,
AS AMENDED BY THE FINANCE COMMISSION (MISCELLANEOUS PRO-
VISIONS) AMENDMENT ACT No. XIII OF 1955.

AN ACT

to determine the qualifications requisite for appointment as members of the Finance Commission and the manner in which they shall be selected, and to prescribe their powers.

BE it enacted by Parliament as follows:—

1. *Short title.*—This Act may be called the Finance Commission (Miscellaneous Provisions) Act, 1951 (Act XXXIII of 1951).

2. *Definition.*—In this Act, “the Commission” means the Finance Commission constituted by the President pursuant to clause (1) of article 280 of the Constitution.

3. *Qualifications for appointment as, and the manner of selection of, members of the Commission.*—The Chairman of the Commission shall be selected from among persons who have had experience in public affairs, and the four other members shall be selected from among persons who

- (a) are, or have been, or are qualified to be appointed as Judges of a High Court; or
- (b) have special knowledge of the Finances and accounts of the Government;
- (c) have had wide experience in financial matters and in administration; or
- (d) have special knowledge of economics.

4. *Personal interest to disqualify members.*—Before appointing a person to be a member of the Commission, the President shall satisfy himself that that person will have no such financial or other interest as is likely to affect prejudicially his functions as a member of the Commission; and the President shall also satisfy himself from time to time with respect to every member of the Commission that he has