CHAPTER 10

FORECAST OF REVENUE AND EXPENDITURE —ARTICLE 275 GRANTS.

102. Paragraph 4 of the Order of the President requires us to make recommendations in regard to the States which are in need of assistance by way of grants-in-aid of their revenues under article 275 and the sums to be paid to those States other than the sums specified in the proviso to clause (1) of that article. In making our recommendations, we are required to have regard, among other considerations, to a number of factors specified in the terms of reference.

103. For the purposes of the scheme of devolution including the grants under article 275 recommended by us, we have accepted the estimate of yield of Central taxes and duties as furnished to us by the Ministry of Finance. We have also assumed that the grant in lieu of the tax on railway passenger fares will remain at the present level of Rs. 12.5 crores per year.

104. The Third Finance Commission considered that 'the total amount of grant-in-aid should be of an order which would enable the States, along with any surplus out of devolution, to cover 75% of the revenue component of their plans'. Such a procedure may help to avoid a situation in which, as a result of the Commission's award, while certain States will have just sufficient means to meet specified revenue commitments, other States will be left with considerable surpluses. Although we agree that it would be within our province to recommend that the grants-in-aid of the revenues of the States should also take into account part or whole of the cost of the revenue component of the State plans, for several reasons, we doubt whether in present circumstances it will be desirable for us to do so.

105. Certain States pleaded for grants for special purposes. The Third Finance Commission suggested in its report that the utilisation of a grant of this kind for a special purpose could be reviewed from year to year by Parliament under article 275 of the Constitution. We have been unable to find any sanction for such an annual review by Parliament under article 275 of the Constitution. Even if a special grant could be made under article 275 such a grant would get merged with the general revenues of the States. A review by the subsequent Finance Commission of the utilisation of the grant may be possible, but cannot be of any practical value. We have,

therefore, not made any special purpose grants but have included certain special requirements in our forecasts of expenditure.

106. In October 1964 we were informed by the Government of India that the question had been under consideration for some time, whether the expenditure incurred by the State Governments on Police forces maintained for the security of their border with foreign countries should be the liability of the Central Government and that the Government of India had since decided that the entire expenditure incurred by the States on such forces as have been maintained for this purpose with the approval of the Central Government would be met by them. No expenditure on this account will therefore have to be met by the States during the Fourth Plan period out of their own revenues and we have accordingly excluded this expenditure from our assessment of the forecast. The Government of Assam have claimed that the Government of India should, as a special case, extend a similar treatment to the expenditure incurred by them on their border with Nagaland. The decision communicated to us by the Government of India is not applicable to this claim and we have included in our assessment of Assam Government's police expenditure the cost of maintaining law and order on Assam's border with the neighbouring State of Nagaland.

107. Although it would constitute part of the States' normal revenue expenditure, we have excluded from our assessment the cost of participation by States in the new all-India services which are proposed to be created for the Education, Medical, Agriculture, Forest and other Departments in the States. The main reason for its exclusion was that decision had so far not been taken by all States on the actual number and grades of posts to be included from each Department and there was no sufficiently firm decision or material on the basis of which reasonably reliable estimates of additional cost could be made. Not all States had given estimates and the estimates which had been received did not show a reasonable degree of consistency.

108. The Second and Third Finance Commissions took into account, in their assessment the likely expenditure on the cost of relief measures, necessitated by unforeseen natural calamities like famine, floods and droughts. The amounts so included were estimated by the Second Finance Commission roughly on the basis of the average annual expenditure incurred over a decade. We have reassessed the amounts likely to be required by each State for this

item on the basis of the figures of gross expenditure for eight years ending with 1964-65 (RE). Where the reassessed figure was lower than the figure adopted by the Second and Third Finance Commissions, we have retained the latter figure. Since eight years' figures were not separately available for Maharashtra and Gujarat, the amounts asked for by them have been adopted for these States. The annual amounts included by us in our estimates of expenditure are given below:

(Rs. lakhs)

S. No.	States	Annual estimated expenditure on relief from natural calamities included in our assessment
1.	Andhra Pradesh	75
2.	Assam	40
3.	Bihar	140
4.	Gujarat	80
5.	Jammu and Kashmir	28
6.	Kerala	10
7.	Madhya Pradesh	30
8.	Madras	50
9.	Maharashtra	60
10.	Mysore	33
11.	Orissa	123
12.	Punjab	197
13.	Rajasthan	93
14.	Uttar Pradesh	75
15.	West Bengal	535
	TOTAL	1569

FOOT-NOTE:

(1) West Bengal's expenditure under head "64-Famine Relief" included some expenditure which was not normally included under this head in other States. The figure of West Bengal is, therefore, not strictly comparable with those of the other States.

(2) No provision is made for Nagaland since no expenditure has been incurred under the head "Famine Relief".

109. We have included in our assessment estimated expenditure on the continuance of any existing schemes for the subsidised distribution of milk and foodgrains and for rural electric supply.

110. In March 1965, after we had received the forecast from the States and concluded our discussions with the representatives of most States, the Government of India sent us a copy of their communication to the State Governments suggesting an increase in the upper monetary limits adopted for debiting the expenditure on individual works or schemes to revenue. From the commencement of the Fourth Plan, it was proposed to increase the existing monetary limits, *i.e.*, Rs. 20,000 for individual works and Rs. 1 lakh for works of the same

character forming part of a scheme to Rs. 1 lakh and Rs. 5 lakhs respectively. The State Governments were requested by us to indicate the increases in their estimated revenue expenditure during the Fourth Plan period occasioned by this enhancement of limits. The States reported varying amounts. Since we have not been able to get any reliable and consistent basis for the increases claimed by the States as a result of this letter of the Government of India, we have not taken into account for any State, the effect of this change of classification on the revenue during the Fourth Five-Year Plan.

111. For the purpose of our estimates, we have not taken into account as expenditure, the estimated loss that will be incurred during the Fourth Plan period by enterprises (including electricity schemes) departmentally managed by the State Governments.

112. We have added in our estimates of expenditure the requirements of the States for payment of annual interest on loans outstanding at the end of the Third Plan period (public loans, Central loans and other loans) on the basis of annual outstanding amounts as at the end of each year (*i.e.*, net of repayments) as reported by the State Governments and the Accountants-General. Interest liability on account of other non-plan loans likely to be raised during the Fourth Plan period has also been allowed in our estimates of expenditure, on the basis of information obtained from the State Governments. The interest liability during the Fourth Plan period on account of the above two classes of loans is as follows:

(Rs. crores)

S. No.	States	Amount
1.	Andhra Pradesh	76·95
2.	Assam	30·20
3.	Bihar	86·08
4.	Gujarat	50·81
5.	Jammu and Kashmir	20·14
6.	Kerala	40·48
7.	Madhya Pradesh	73·53
8.	Madras	79·13
9.	Maharashtra	97·81
10.	Mysore	58·66
11.	Orissa	62·37
12.	Punjab	75·53
13.	Rajasthan	58·01
14.	Uttar Pradesh	104·21
15.	West Bengal	73·73
	TOTAL	987·64

113. We have also included in our assessment of expenditure the requirements for payment of full interest on Fourth Plan loans that will be raised by the States during 1966—71. We have not allowed for capitalisation of any portion of the interest. We have utilised the data obtained from the Planning Commission for our estimates of borrowings by the individual States. For Central loans we have not provided any interest for the year of borrowing while for other loans we have provided for interest for half a year, in the year of borrowing. The amounts estimated by us on this account for each State, for interest payments on the gross Fourth Plan loans are as follows:

(Rs. crores)

S. No.	States	Amount
1.	Andhra Pradesh	43·48
2.	Assam	16·10
3.	Bihar	41·31
4.	Jammu and Kashmir	8·90
5.	Gujarat	25·30
6.	Kerala	22·00
7.	Madhya Pradesh	37·97
8.	Madras	41·61
9.	Maharashtra	51·15
10.	Mysore	29·92
11.	Orissa	31·58
12.	Punjab	29·99
13.	Rajasthan	29·46
14.	Uttar Pradesh	68·38
15.	West Bengal	45·14
	TOTAL	522·29

114. Paragraph 4(a)(iii) of the Order of the President requires us to take into account, for the purpose of determining the needs of States for assistance under article 275(1) of the Constitution, the expenditure likely to devolve upon the States for the servicing of their debt. Elsewhere in this report we have expressed our opinion that the service and amortisation of the market borrowings of the State Governments must form part of the revenue liabilities of the State Governments. We have accordingly included in our assessment expenditure on these items estimated on the basis of the existing practices adopted by the State Governments. This has resulted in

allowing provisions only at nominal rates for some States and for other States at adequate rates which will enable full repayment of the loans on maturity. We feel that the entire question of indebtedness of the States and the soundness of the existing borrowing, interest payment, repayment and accounting practices in this respect should be reviewed on the basis of detailed study and report by a competent body to be set up for the purpose. The rate at which contributions to the sinking fund should be charged to the revenue account by States and the steps necessary to make the accumulations available for the purposes for which they are intended should constitute part of the terms of reference to that body about which we have made further recommendations in a later chapter of this report. We consider it proper to include in our estimates of revenue expenditure, provision for contribution to sinking funds for public loans on the basis in force at present. The amounts included for the five years for the various States on account of sinking fund provision for public loans (including Fourth Plan loans) are as below:

(Rs. crores)

S. No.	States	Amount
1.	Andhra Pradesh	4·94
2.	Assam	11·19
3.	Bihar	9·04
4.	Gujarat	28·41
5.	Jammu and Kashmir	—
6.	Kerala	3·63
7.	Madhya Pradesh	7·19
8.	Madras	8·90
9.	Maharashtra	46·85
10.	Mysore	15·00
11.	Nagaland	—
12.	Orissa	31·49
13.	Punjab	12·15
14.	Rajasthan	16·90
15.	Uttar Pradesh	61·97
16.	West Bengal	28·56
	TOTAL	286·22

115. The instructions in our letter requesting for forecasts of revenue and expenditure from the State Governments required that expenditure on schemes financed by non-plan grants from the Centre

should be included under expenditure and that an explanatory note indicating the Central grants likely to be received should also be furnished. Some States furnished such information but certain other States provided expenditure estimates after deducting the Central grants expected by them. In forecasting their expenditure, State Governments have assumed the continuance of non-plan grants on the existing basis for the following items: (i) labour and employment schemes, (ii) implementation of gold control rules, (iii) rehabilitation of displaced persons, (iv) subsidy in respect of interest on loans for flood control schemes, (v) civil defence expenditure, (vi) expenditure on outside police force borrowed in connection with emergency (in respect of Assam), Additional Punjab Armed Police Battalion deployed in Lahul and Spiti (in respect of Punjab), (vii) Administration of Lahul and Spiti (in respect of Punjab), and (viii) expenditure on Uttar Khand Division (in respect of Uttar Pradesh). The deficits and surpluses arrived at by us are, therefore, derived after taking credit for the non-plan grants expected to be received by the States for such schemes.

116. The Third Plan schemes, more especially in the social service sectors, create liability for 'committed expenditure' during the Fourth Plan period. The expenditure on this account in 1966-67 has been calculated by us on the basis of the estimated level of revenue plan expenditure in 1965-66 in each State as ascertained from the Planning Commission and its composition as assessed on the basis of information furnished by the States. Provision was also made for an annual growth rate of 3·5 per cent in the committed expenditure. The total amount included in our estimates on account of committed expenditure of Third Plan Schemes for all States for the five-year period comes to about Rs. 1,230 crores.

117. In scrutinizing the forecasts of revenue and expenditure presented by the States, we have taken into account the normal caution with which estimat[illegible]nging over a large variety of items and over long period of [illegible] have to be prepared in the interest of sound finance. [illegible] States produced successive revised forecasts either revising the original figures on the basis of further information or including fresh items of expenditure not included in the original forecasts. We have accepted the revisions wherever they were justified on the basis of the latest actuals. While revising expenditure estimates on account of inclusion of such new items, the Commission has taken into account the possibility of accommodating part of the

expenditure on these new items by means of marginal reappropriations in the large aggregate amount of the expenditure budget.

118. Paragraph 4(a)(v) of the Order of the President requires us, while recommending grants under article 275 of the Constitution, to take into consideration the scope for economy consistent with efficiency which may be effected by States in their administrative expenditure. In examining the forecasts of revenue and expenditure we have kept this aspect in mind. We have excluded from our assessment of expenditure items such as loss in the working of public enterprises. We have also assumed full realisation of current interest dues from States corporations.

119. Our terms of reference specify that in making recommendations for assistance to States by way of grants-in-aid, we should have regard, among other considerations, to the creation of a fund out of the excess, if any, of the net proceeds of estate duty (over a limit to be specified by the Commission), for repayment of States' debt to the Central Government. We have given our views elsewhere in this report why we do not think there would be an advantage of any consequence in adopting a scheme of the kind suggested by implication in this part of our terms of reference; in view of that position, we have not allowed any transfers of revenue from the proceeds of estate duty for creation of the proposed fund. We have, however, independently considered the subject of States' indebtedness to the Union Government in another part of our report.

120. It was represented to us by almost all States that their present levels of expenditure for maintenance of public works, more especially roads were grossly inadequate and that application of past growth rates for forecasting the non-plan expenditure on public works during the Fourth Plan period would not meet the need for improving the existing conditions of roads. Some States have, therefore, urged the continuation of the special purpose communications grant while some others have made substantial additions in arriving at the base figure of 1966-67 expenditure on public works in their forecasts. We agree that there is need for improving the standards of public works maintenance in States but for reasons given elsewhere we have not recommended any specific purpose grants. However, to meet the needs of the situation and for according a uniform treatment to the different States, we have estimated the 1965-66 expenditure on public works with reference to past trends over actuals of 1963-64 and have made due allowance for the enhanced standards of maintenance.

121. On the receipts side, we have not included any transfer from Central Road Fund since the amounts are intended to be utilised for financing developmental outlays in the Plan. These receipts may, therefore, be counted as resources for financing the Fourth Plan. We have also excluded any expenditure which was proposed in the States' forecasts to be financed out of Central Road Fund grants.

122. We have allowed transfer to Zamindari/Jagir Abolition Fund from the revenue account in the case of States which have been making such provision from the revenue account. We have taken the view that land reform measures were largely in the nature of basic social reform and that as such the net burden falling on the States' exchequer on account of this reform might appropriately be met out of the revenue budget itself. Even if the Zamindari Abolition Bonds were treated as public loans, some provision for their amortization would have to be made in the revenue budget on the same basis as amortization provision for public loans. Further, increases in land revenue receipts on account of Zamindari Abolition measures accrue in the revenue budget. In view of all this, we felt that it would be proper to make provision in the revenue budget for payment on account of Zamindari/Jagir abolition operations.

123. We have included in the revenue receipts the proceeds of betterment levies and of sale of State property.

124. In the assessment of non-tax revenues of the States, we could take into account only the revenues likely to accrue from schemes completed by the end of the Third Plan period. Receipts arising from the Fourth Plan schemes, including interest on fresh lendings, have been left out since the size of the Fourth Plan and its distribution among various sectors for each State are yet to be finalised. These receipts may, therefore, be counted as resources for financing the Fourth Plan.

125. While examining the forecast of receipts and expediture, we found that some States have shown transfer of proceeds from certain taxes like tax on motor vehicles, sales tax on motor spirit, sugar cane cess, education cess, electricity duty and toll on bridges to funds set apart for meeting specific items of expenditures. Some of these items formed part of non-plan revenue expenditure already included in the forecast while others constituted Fourth Plan expenditure or capital expenditure outside the plan with which we are not concerned. We took the view that we should allow for such transfer of tax revenues not only where the Fund is meant for financing the non-plan revenue expenditure but also when it

is specifically earmarked for a particular purpose outside the non-plan revenue account. This would have the effect of making the balance in these funds which is not being used for non-plan purposes, available for plan expenditure.

126. For determining the needs of the States for assistance under article 275(1) of the Constitution, it was necessary to examine in detail the forecasts of revenue and expenditure furnished by each State, taking into account the trends of growth of revenue and expenditure in the past and the facts and arguments produced in support of the detailed items in the discussion and correspondence with the State Governments.

127. The interest receipts from Electricity Boards and other autonomous enterprises had been estimated by several States on the assumption that they would be unable to pay the entire amount due under this head and that there would be a further increase in arrears, over the levels existing at the end of the Third Plan. In our assessment for the purpose of determining the revenue gap and the requirements of grants under article 275, we have assumed that the States must treat as resource their entire interest dues—excluding interest on Fourth Plan loans. We have not assumed any reduction in the arrears of interest as outstanding at the end of the Third Five-Year Plan, except where expressly indicated otherwise, in the States' own forecast.

128. Many States included in the forecast demands for large increases over present levels and past trends under police expenditure, grants to local bodies and pay and allowance of State employees. These demands by the States were not always supported by firm decisions and detailed data. The Commission therefore decided to include only those increases in expenditure, which were based on firm decisions of the State Government incorporated in orders which committed the Government to liability on that account. As a consequence of this decision we had to leave out a few cases on which proposals calculated to involve commitments are at various advanced stages of consideration and action has been held up awaiting the report of a Commission or the passing of an Act by the Legislature. These are listed in Annexure 1, Part 1. We recommend that in case these propopsals mature into commitments before the President issues orders under article 275 of the Constitution, and the Union is approached by the State Governments, those requirements may also be taken into account by the President in determining the amounts to be granted under article 275.

129. Our estimates of revenue and expenditure take into account all firm Government orders (including orders granting interim reliefs in pay and D.A.) and enactments up to the end of June 1965. We had hoped to take into account all revisions of estimates of States' expenditure on account of pay and allowances of employees of State Governments and local bodies and school teachers intimated to us by the Governments upto the end of July, 1965 on the basis of firm Government orders creating the liabilities but we have not been able to do so in respect of the liabilities created by the orders listed in Annexure 1, Part 2 either because there was not sufficient time after their receipt to reassess the estimates, or the proposals were not accompanied by the basic particulars and other data necessary to enable us to determine the need for additional grants-in-aid. We recommend that the effect of these liabilities may also be taken into account in fixing the article 275 grants to be included in the Order of the President.

130. An assessment of needs of the type undertaken by us cannot obviously take into account various items of requirements which might emerge during the next five years and which cannot be foreseen at this time. An appropriate procedure will have to be evolved to take such needs into account and to afford Central assistance wherever necessary.

131. Our assessment of revenue receipts and non-plan revenue expenditure of different States for the five-year period 1966-67 to 1970-71 made in the manner explained in the preceding paragraphs works out to the following estimates of non-plan revenue gap:

(Rs. crores)

S. No.	States	Non-Plan revenue gap during 1966-71
1.	Andhra Pradesh	202·73
2.	Assam	144·96
3.	Bihar	108·21
4.	Gujarat	113·55
5.	Jammu and Kashmir	66·10
6.	Kerala	188·61
7.	Madhya Pradesh	162·03
8.	Madras	207·32
9.	Maharashtra	44·72
10.	Mysore	202·52
11.	Nagaland	58·46
12.	Orissa	231·85
13.	Punjab	75·03
14.	Rajasthan	130·41
15.	Uttar Pradesh	306·75
16.	West Bengal	183·44
	TOTAL	2426·69

132. After meeting the revenue deficits estimated for the five-year period, the amounts accruing to the following States as their shares of the various taxes and duties (i.e., shares of income-tax, estate duties, Union excise duties, additional excise duties and grants in lieu of tax on railway passenger fares) result in the surplus noted against each State for the five-year period. We do not recommend any grants under article 275 for them:

(Rs. crores)

S. No.	States	Surplus
1.	Bihar	89·25
2.	Gujarat	8·00
3.	Maharashtra	215·66
4.	Punjab	29·83
5.	Uttar Pradesh	17·02
6.	West Bengal	13·97
	TOTAL	373·73

133. The revenue deficits for the five-year period are in excess of the amounts accruing to the following 10 states as their shares of the various taxes and duties (i.e., shares of income-tax, Union excise duties, additional excise duties, estate duty and grants in lieu of tax on railway passenger fares) by the sum shown against each and we recommend that annual grants equal to one fifth of the sum may be given to each of them under article 275 of the Constitution:

(Rs. crores)

S. No.	States	Deficit (5 times annual grant)
1.	Andhra Pradesh	36·10
2.	Assam	82·60
3.	Jammu and Kashmir	32·85
4.	Kerala	104·10
5.	Madhya Pradesh	13·50
6.	Madras	34·20
7.	Mysore	91·20
8.	Nagaland	35·35
9.	Orissa	145·90
10.	Rajasthan	33·65
	TOTAL	609·45