

CHAPTER 7GRANT IN LIEU OF TAX ON RAILWAY PASSENGER FARES

In terms of paragraph 6(c) of the Presidential Order constituting the Commission we have to suggest changes, if any, to be made in the principles governing the distribution among the States of the grant to be made available to them in lieu of the tax under the repealed Railway Passenger Fares Tax Act, 1957.

2. The tax on railway passenger fares is one among the taxes which shall be levied and collected by the Government of India but is assigned to the States under Article 269 of the Constitution. The tax was levied for the first time under the Railway Passenger Fares Tax Act, 1957. The Second Finance Commission, which was then at work, was requested to make recommendations as to the principles which should govern the distribution of the net proceeds in any financial year of the tax, among the States. That Commission took the view that the principle for distribution should be such as to secure for each State, as nearly as possible, the share of the net proceeds on account of actual passenger travel on railways within its limits. That share was determined by allocating the passenger earnings among the States on the basis of the route mileage within each State, making due allowance for the wide variations in the density of traffic between the various railway zones and as between the different gauges in each zone. Accordingly, that Commission allocated the non-suburban earnings of each railway by the route mileages located in each State, separately for each gauge and distributed the proceeds of the tax among the States in the same ratio, after setting aside a quarter of one per cent as the share attributable to the Union territories. The Second Commission made its recommendations for a five-year period ending with 1961-62.

3. The Railway Passenger Fares Tax Act, 1957, was, however, repealed and the tax was merged in the passenger fares with effect from 1st April 1961. This step was taken by the Government of India in pursuance of the recommendations of the Railway Convention Committee, which was persuaded by the Railway Board's contention that the levy of the passenger fare tax had limited the scope for raising passenger fares. The Railway Board had at the same time conceded that the States, which would have taken their receipts from this source in computing their resources for the Third Five Year Plan, should not be put into difficulties. The Board had, therefore, suggested that the States should continue to get from the Railways, through the General Revenues, a fixed amount in the following five years. The Convention Committee accepted this suggestion and recommended that Rs. 12.50 crores should be paid annually by the Railways for distribution to the States in the five-year period ending 1961-66, in lieu of the tax. The Fourth Finance Commission had placed on record the almost unanimous view of the States that the fixation of the grant at a specific level had deprived them of a potential elastic source of revenue and had urged that the level of the grant should be raised in the proportion in which the railway passenger earnings had increased since the merger of the tax with the fares. Subsequently, it was suggested to the Railway Convention Committee, 1965, by the Railway Board that in view of the growth in passenger traffic from 1960-61 to 1964-65 and the further growth anticipated in the subsequent years, the amount of the annual grant to the States in lieu of the tax might be increased to Rs. 16.25 crores for the period from 1966-67 to 1970-71. The Railways suggested, as a part of this proposal, that they might pay an additional dividend to the General Revenues at 1% on the capital invested upto 31st March 1964. The additional dividend was estimated at Rs. 18 crores per annum, out of which Rs. 16.25 crores would be paid to the States as grant in lieu of the tax and the balance would be utilised to assist the States in providing their portion of the

resources required for financing Railway safety works. The Convention Committee accepted these suggestions and in pursuance of its recommendations the annual grant to the States was raised to Rs. 16.25 crores from 1966-67. The Railway Convention Committees of 1971, 1973 and 1977 left the quantum of the annual grant unchanged. The amount of this grant is, therefore, Rs. 16.25 crores till the end of the current year. The amount of the grant from 1979-80 onwards is yet to be decided.

4. The Third, Fourth and Fifth Commissions, which had been asked to deal with the distribution of this ad hoc grant to the States, considered that the principle of distribution should be such that the States were generally in the same position in this matter as they were before the repeal of the Act. The Sixth Commission also was of the same view and accordingly worked out the percentage shares of the different States on the basis of the statistics of gaugewise route lengths of railways in each State and the actual passenger earnings from non-suburban traffic for each zonal railway for the four years ending 1971-72.

5. Almost all the States, while communicating their views to us on the principles for the distribution of the grant, have supported the existing principles. A few of them, however, have suggested that some other considerations should be taken into account for determining the distribution of the grant. Himachal Pradesh has proposed that while half the grant may be distributed on the existing principles, the other half should be distributed in the inverse proportion of the railway track length per hundred square kilometre of area. Jammu and Kashmir has asked for the backwardness of States to be taken into account, and in the alternative, has suggested that the contribution of each State in the total passenger earnings of the Railways should be the criterion and not the railway mileage in each State. Manipur, which has no railway line, has suggested that the entire grant should be distributed on the population ratio without reference to the existence or otherwise of railway lines in a State. Meghalaya has suggested that half the grant should be distributed on the existing principles and the other half on the population ratio. Sikkim has suggested that if the grant is distributed on the basis of what the States would have got, had the tax been continued, the road length from Gangtok in Sikkim to Siliguri in West Bengal should be treated as the railway route length within Sikkim. We may mention that there are out-agencies at Imphal in Manipur, Shillong in Meghalaya and Gangtok in Sikkim for booking railway tickets.

6. We are in agreement with the view held by the earlier Commissions that, though the tax on railway passenger fares has been repealed and what the States now receive are not shares in the proceeds of a tax under Article 269 but shares in the grant in lieu of the tax, these shares should be determined in the same manner as if the levy and collection of the tax had continued. The general principle for the distribution of proceeds on taxes and duties under Article 269 as enunciated by the Commissions in the past is that each State should receive from such taxes, as nearly as may be, the amounts which it would have raised if it had the power to levy and collect them. In the light of this principle, we have given consideration to the question as what the principles of distribution should be. If the tax had continued and were to be collected by the States, each State would be competent to collect tax only on railway fares paid within that State, irrespective of the States through which the journeys may be performed. There can be no extra-territorial collection by any State. Railway passenger fares are paid in advance before the commencement of the journey. The tax was collected at source and was a percentage of the fare. It, therefore, appears to us that the most appropriate distribution of the grant in lieu of the tax would be in proportion to the non-suburban passenger earnings from traffic originating in each State. We feel also that the assumption of the earlier Commissions that the railway route lengths falling within each State would be an appropriate basis for working out the shares of the States, suffers from deficiencies. For instance, it is not clear how far the route lengths would reflect differentiations in the capacity for moving passenger traffic over single, double or multiple lines or factors like electric or diesel traction, line capacity improvement works, passenger load factors, etc. It appears to us that the developments

over the last few years in these respects might well have rendered the basis adopted by the earlier Commissions less reliable now than it might have been in the past.

7. We feel fortified in our view that the basis for the distribution of the grant should be in the proportion of non-suburban passenger earnings in each State to the total passenger earnings in all the States by the provisions of the Railway Passenger Fares Ordinance 1971 promulgated by the President in October 1971. This Ordinance was replaced by an Act of Parliament in December 1971. The enactment provided for the levy of a tax on railway passenger fares at a flat rate of 5 per cent of the fare, where the fare was not less than a rupee. The levy was in force from 15th November 1971 to 31st March 1973, whereafter the Act was repealed. The levy was under Article 269 and the net proceeds were assigned to the States by law. The States had agreed that they would re-transfer to the Centre amounts equivalent to their shares since the purpose of the levy (together with a number of others) was to enable the Central Government to defray the expenditure on Bangladesh refugees. This aspect, however, is not relevant for our purposes. For the assignment to the States of the net proceeds of this tax on railway passenger fares, Section 6 of the Ordinance and the Act provided:-

"During each financial year ending on or after the 31st day of March, 1972, there shall be paid to each State (not being a Union territory) such sum of money as bears to the net proceeds of the tax collected under this Ordinance during that year in all the territories of India the same proportion as the aggregate of the fares collected in that State during that year bears to the aggregate of the fares collected in all the territories of India during that year."

8. We have obtained from the Railway Board the statistics of non-suburban passenger earnings of railways for the four years ending 1977-78 (Annexure VII (4) and have worked out the percentage share of different States on the average non-suburban passenger earnings of the railways in each State during these four years. The percentages are set out below:

States	Percentage Shares
Andhra Pradesh	6.99
Assam	2.46
Bihar	9.50
Gujarat	5.28
Haryana	1.97
Himachal Pradesh	0.13
Jammu & Kashmir	0.74
Karnataka	3.21
Kerala	2.61
Madhya Pradesh	5.84
Maharashtra	15.87
Manipur	-
Meghalaya	-
Nagaland	0.26
Orissa	1.73
Punjab	3.81
Rajasthan	5.48
Sikkim	-
Tamil Nadu	6.85
Tripura	0.04
Uttar Pradesh	18.58
West Bengal	8.65
	<u>100.00</u>

9. We recommend that the grant to be made available to the States in lieu of the tax under the repealed Railway Passenger Fares Tax Act, 1957 be distributed in accordance with these percentages in each year from 1979-80 to 1983-84.

10. As stated above, we do not know yet on what basis the Railway Convention Committee would fix the grant payable to the States in lieu of the tax on railway passenger fares from 1979-80 onwards. We are, therefore, unable to work out what the shares of the States would be in accordance with the percentages recommended above. Meanwhile, for the purposes of the assessment of the revenue position of the States, we have calculated their shares on the present level of Rs. 16.25 crores as the annual grant.

11. We next turn to the question of the quantum of the grant. Though our terms of reference do not mention the question of re-imposition of the tax or the re-determination of the quantum of the grant, practically all the States strongly urged that the amount of the grant should be re-determined in the light of what the proceeds would have been had the tax continued in its original form and estimated on the basis of the current earnings from non-suburban passenger traffic. Uttar Pradesh suggested that the Commission may recommend the re-imposition by the Government of India of the tax on railway passenger fares. Most of the State Governments were highly critical about the replacement of the tax by a fixed grant and argued that the States should not be deprived of their due share in the buoyancy of the receipts accruing from passenger fares. Maharashtra argued that the unsatisfactory financial position of the Railways was extraneous to any decision on the quantum of the grants to be paid to the States in lieu of the tax on Railway fares, it being one of the levies under Article 269 of the Constitution. West Bengal discounted the argument that the Railways have to shoulder certain social obligations which should be taken into account when deciding on the grant to be paid in lieu of the railway passenger tax. The State has suggested that the tax should be revived if the amount of the grant were not enlarged to 15 per cent of the railway passenger earnings.

12. Because of the near unanimity amongst the State Governments on this issue, and the strong views expressed by them both in their Memoranda and during their discussions with us, we have thought it appropriate to consider the relevant issues in some detail.

13. We have earlier referred to the Fourth Commission's observations on the representations of the States that the amount of the grant should be increased and to the subsequent consideration given to the matter by the Railway Board and the Railway Convention Committee. At that time the Railways had themselves given weight to the growth in passenger traffic from 1960-61 to 1964-65 and the further growth anticipated thereafter while suggesting to the Convention Committee that the amount of the grant might be raised to Rs. 16.25 crores from 1966-67. It is indisputable that passenger traffic and passenger earnings continued to grow in the later years. If due weight had been given to this consideration as was done at the time the grant was increased to Rs. 16.25 crores, it would be legitimate to expect that the grant would have been increased further at intervals. However, this has not been the case. The Sixth Commission estimated that if the tax on passenger fares had continued the actual collection from the tax in 1969-70 and 1970-71 would have been about Rs. 24.46 crores and Rs. 26.17 crores respectively. That Commission also estimated that in the three years thereafter the tax would have amounted to approximately Rs. 31 crores, Rs. 33 crores and Rs. 36.5 crores, on the assumption that roughly 10.7 per cent of non-suburban passenger fares would represent the tax element. From the figures furnished to us by the Railways we have estimated that, if the tax had been continued in its original form, assuming the average rate of 10.7 per cent of non-suburban passenger earnings

as the tax element, the collections would have been Rs. 56.21 crores in 1976-77, Rs. 61.17 crores in 1977-78 and Rs. 63.22 crores in 1978-79 (BE). Non-suburban passenger traffic in terms of passenger kilometres increased from 68617 million in 1961-62 to 126754 million in 1976-77, or by a factor of 1.85. Average earnings per passenger per kilometre are estimated to have gone up from 2.01 p. in 1961-62 to 4.03 p. in 1976-77 for non-suburban passenger traffic, i.e. by a factor of 2. Non-suburban passenger earnings increased from Rs. 137.73 crores in 1961-62 to Rs. 525.30 crores in 1976-77 i.e. by a factor of 3.8. On the other hand, the amount of grant in lieu of the tax, fixed at Rs. 12.50 crores when the tax was abolished in 1961, was raised once to Rs. 16.25 crores in 1966, and has been stagnant at that figure since then.

14. The Finance Commission may not be the competent body to advise whether it would be appropriate to re-impose the railway passenger fare tax as has been urged by at least one State Government. Nevertheless, we do appreciate the force of the argument put forward by almost all State Governments that a fixed grant is not an adequate replacement of a tax on railway fares, since it does not take into account the considerable buoyancy in the earnings of the Indian Railways caused by the rapid increase in passenger traffic. The increase in average earnings per passenger kilometre from 2.01 paise to 4.03 paise mentioned earlier may have come about because of fare increases necessitated by higher working expenses in the form of increased fuel charges, payment of higher emoluments to Railway personnel, increased costs of stores and spares etc. As such, it may be difficult to insist on a corresponding increase in the grant payable to the States. Even so, we cannot ignore the substantial increase that has taken place in the extent of passenger traffic since 1961-62 as reflected by the figures of non-suburban passenger kilometres. We feel that the States are entitled to their due share arising from the growth in non-suburban passenger traffic by a factor of 1.85 since 1961-62 as it is a major element responsible for the overall increase in passenger earnings from this traffic by a factor as high as 3.8 since 1961-62. The factor of 1.85 would represent a grant of about Rs. 30 crores a year.

15. However, we also appreciate that the Indian Railways as the largest departmental undertaking should be enabled to operate at a profit and should be in a sufficiently strong financial position to service the loans granted for their developmental projects, including the construction of new lines, for which State Governments themselves make repeated demands. We also appreciate the social obligations of the Railways e.g. carriage of suburban traffic and of essential commodities, sometimes at a loss. On the other hand, there is also force in the point urged upon us by one of the State Governments that they also have to bear substantial financial burdens on account of the operations of the Railways, for instance, for the dispersal of traffic carried by the Railways at the destinations.

16. We would suggest that having regard to the various factors mentioned above, the Government of India should specifically refer the question of increasing the quantum of the grant in lieu of the railway passenger fares tax, to the appropriate Railway Convention Committee. Since this Committee carefully examines the overall financial position of the Railways, the dividend payments that should be made to General Revenues, as also the contributions of the Railways to the Depreciation, Development, Pension and other Funds, we can reasonably expect that the Committee would judiciously consider, in the light of the facts stated above, the question of increasing the grant payable to the States.

## CHAPTER 8

GRANT ON ACCOUNT OF WEALTH TAX  
ON AGRICULTURAL PROPERTY

In terms of paragraph 6(d) of the Presidential Order we are to suggest changes, if any, in the principles governing the distribution among the States of a grant to be made available to them on account of wealth tax on agricultural property.

2. Wealth tax on agricultural property was introduced with effect from assessment year 1970-71 by amending Section 2(e) of the Wealth Tax Act, 1957. The amendment was a part of the measures in the Finance Act of 1969. Prior to this amendment, assets defined for the purposes of the wealth tax did not include agricultural property. The effect of the amendment of the Wealth Tax Act in 1969 was that agricultural property stood included in the properties taxable under the Act. This amendment is not applicable to the State of Jammu & Kashmir.

3. Wealth tax is not one of the taxes and duties which, under the provisions of the Constitution, are to be shared with the States either on an obligatory or permissive basis. Nor is it a tax levied or collected by the Centre and assigned to the States. However, when agricultural property was made liable to wealth tax as aforesaid the Central Government decided on its own that the net proceeds of the tax on agricultural land would be passed on to the States as grants-in-aid.

4. The Sixth Commission was required to recommend the principles for the distribution among the States of the grant for the five years from 1974-75 to 1978-79. That Commission took the amount of grant as equivalent to the net collections of wealth tax on agricultural property reduced by the net collections attributable to the Union territories. It considered the tax as being comparable in its incidence to estate duty in so far as the latter related to immovable property. It observed that the location of the property brought to assessment would be clearly identifiable in each case and would provide a reliable basis for the distribution of the proceeds among the States. It recommended accordingly that the grant should be distributed among the States in proportion to the value of agricultural property situated in each State and brought to assessment each year. It did not consider population as an appropriate basis for distribution, since it would have no bearing on the extent or value of agricultural property brought within the tax net. Backwardness of a State of its need for development was also considered as not relevant. The Sixth Commission noted further that collection of the tax would not be an appropriate basis as collection in a State may in some cases relate to property located outside the State.

5. Before making its recommendation the Sixth Commission had consulted the Central Board of Direct Taxes in regard to statistics then maintained by the Department and the possibility of maintaining statistics for agricultural property in each State brought to assessment. While that Commission was informed that the data were not readily available, it observed that it had no doubt that arrangements could easily be made for compilation of the relevant statistics relating to agricultural property located in each State and brought to assessment in a year.

6. The Sixth Commission's recommendations were accepted by the Government of India, to be effective in relation to the net collections in each year from 1974-75 to 1978-79. As we have been informed by the Union Ministry of Finance, the Government of India decided for the years 1970-71 to 1973-74, to adopt the population ratio as the basis for distribution of the grant among the States. For these four years the total amount of the grant payable to the