GOVERNMENT OF INDIA

MINISTRY OF STATES

# INDIAN STATES FINANCES ENQUIRY COMMITTEE



## FIRST INTERIM REPORT

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# BARODA

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# BARODA

## INTEGRATI FEDERAL FINANCES

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# I.—INTRODUCTORY

## Terms of Reference

We were appointed by the Government of India (Ministry of States) in their Resolution No. F. 60-IB/48, dated the 22nd October 1948 to enquire into the finances of Indian States and Unions of States with the following Terms of Reference:—

"To examine and report upon:—

(1) the present structure of Public Finance in Indian States and Unions of States;

(2) the desirability and feasibility of integrating Federal Finance in Indian States and Unions of States with that of the rest of India, to the end that a uniform system of Federal Finance may be established throughout the Dominion of India;

(3) whether, and if so, the extent to which, the process of so integrating Federal Finance in the Indian States and Unions with that of the rest of India should be gradual and the manner in which it should be brought about; and the machinery required for this purpose, especially as regards the legislative groundwork and the administrative organisation necessary for the imposition, assessment and collection of Federal Taxes;

(4) the results of such a policy of integrating Federal Finance upon the finances of Indian States and Unions and the consequential financial adjustments and relations which should subsist between the Governments of the Indian States and Unions on the one hand and the Government of India on the other;

(5) the measures which the Committee may consider necessary and/or desirable for revising, in the light of present day conditions and standards, and having regard to the requirements of modern administration, the structure of Provincial Finance and, in particular, the levels and sources of Provincial Revenues in Indian States and Unions of States;

(6) any other consequential and/or cognate matters which the Committee may consider as arising out of the foregoing terms of reference."

2. In a demi-official letter dated 8th February 1949, we were advised by the Ministry of States that the Baroda State was likely to be merged into the Bombay Province on the 1st May 1949 and that our report and recommendations in respect of that State were, therefore, required as early as possible in advance of our main report, in order to enable the Government of India to come to a decision on certain matters connected with the merger.

## Preliminary Remarks

3. We have made a study of the general problem of federal financial integration of Indian States and have also made sufficient progress with our detailed enquiries over the whole field to be in a position to submit the interim report required by Government regarding Baroda State. We do not expect that our conclusions in respect of this State will need modification after our enquiry in regard to the other States and Union is completed.

4. In the course of our enquiry, we have had several informal discussions with the Dewan of Baroda. The technical data required by us was collected after local investigation and discussion at Baroda and we take this opportunity of expressing our gratitude to the Dewan of Baroda and the officers of the State for the full co-operation extended to us. One of us (Mr. Dandekar) has also had informal discussions with representatives of the Federation of Baroda State Mills and Industries and we have kept ourselves informed of the views of local commercial interests on questions likely to arise after the merger, in respect particularly of taxation matters. Finally, at a formal meeting of the Committee with representatives and officers of the Bombay and Baroda Governments, we covered the whole field of major problems arising out of this case, and were able to reach agreed conclusions on most points.

## Scope of the Enquiry

5. In view of the impending merger of the State, we are not concerned in this case with the first and the fifth terms of reference; in fact, in a subsequent communication the Government of India were pleased to agree with our suggestion that these two terms of reference should be withdrawn altogether. Furthermore, in this case the second term of reference is, in effect, already answered for us in the affirmative by the very fact of the decision to merge the State into the Bombay Province; and as regards the third term of reference, it becomes largely otiose, for there can be no question of invoking any principle of gradualness after there has been a complete merger into the Dominion of India, as distinguished from mere "accession" however all-embracing. Accepting, therefore, Baroda's complete "federal" financial integration with the Central Government as a fact, in consequence of its becoming an integral part of the Bombay Province itself, we have to deal only with the 4th and 6th terms of reference, which (suitably reworded) are as follows:—

"To examine and report upon:—

(4) the results of such a policy of integrating Federal Finance (in Baroda) upon the finances of (Baroda), and the consequential financial adjustments and relations which should subsist between the Government of (Bombay) on the one hand and the Government of India on the other;

(6) any other consequential and/or cognate matters which the Committee may consider as arising out of the foregoing terms of reference."

6. The reason for dealing with the "federal finance" problem of this State, even to the limited extent indicated above, is, we presume, that our recommendations may be of assistance to the Government of India in deciding the financial adjustments, if any, subject to which the State should be merged into the Bombay Province, so far as only the "federal" financial aspect of the problem is concerned.

## II.—ANALYSIS OF THE PROBLEM

### Constitutional Position

7. As we see it, the constitutional position is that the Ruler of Baroda has decided, by agreement with the Dominion, "to cede to the Dominion Government full and exclusive authority, jurisdiction and powers for and in relation to the governance of the State" and "to transfer the administration of the State to the Dominion Government on the 1st day of May 1949." As from that day the Dominion Government has been "competent to exercise the said powers, authority and jurisdiction in such manner and through such agency as it may think fit." We take it, therefore, that whatever may be the intervening arrangements for a short period, ultimately the decision to merge the State into the Province of Bombay will be given effect to by an Order of the Governor-General issued under Section 290-A of the Government of India Act, 1935, as adapted by the Indian (Provisional Constitution) Order 1947. The relevant portions of this Section are reproduced below:—

"Where full and exclusive authority, jurisdiction and powers for and in relation to the goverance of any Indian State or of any group of such States are for the time being exercisable by the Dominion Government, the Governor-General may by Order direct—

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(b) that the State or the group of States shall be administered in all respects as if the State or the group of States formed part of a Governor's or a Chief Commissioner's Province specified in the Order;

Provided that if any Order made under clause (b) of this sub-section affects a Governor's Province, the Governor-General shall, before making such Order, ascertain the views of the Government of that Province both with respect to the proposal to make the Order and with respect to the provisions to be inserted therein."

It follows that after the necessary Order under Section 290-A of the Government of India Act, 1935, is issued by the Governor-General, the

Bombay Government and Legislature will exercise in the area newly added to that Province only those powers which they are now exercising in the Bombay Province under the Act; while, in the same area, the Dominion Government and Legislature will exercise powers in respect of "Dominion" subjects, precisely as they are now doing in Bombay Province as at present constituted.

## Basis of Approach

8. (*a*) The foregoing statement of the constitutional position furnishes the proper basis for our approach to this problem. On the date of the merger, the Baroda State as such will cease to exist. It will first be incorporated substantively into the Indian Dominion; and immediately thereafter, it will be divided into two "functional" entities; the "Central" Government aspect and functions of its administration will remain merged with the Government of India; while in respect of its "Provincial" administration, it will be merged into the Bombay Province under Section 290-A of the Government of India Act, 1935.

It follows that as from that date, the "Central" assets, liabilities, functions and sources of revenue of the former Baroda Government will vest in the Dominion Government while the "Provincial" assets, liabilities, functions and sources of revenue will vest in the Bombay Government. On the same principle, the Customs rights of the Baroda State under the agreement of 1936 with the Government of India will vest with the Dominion Government; the postal compensation hitherto payable to the Baroda Government will cease; and any special arrangements at present subsisting between Baroda and the Central Government in regard to Excises, Salt, Opium etc., will also be terminated.



(*b*) But the merger will also have certain further consequences, particularly upon the finances of the Bombay Province, which, however important in themselves, it would be outside our terms of reference to examine. The merger of the "provincial" administration of Baroda into that of Bombay will give rise to increased expenditure in certain directions, and will lead to important savings in others: and in certain fields, there will be increased revenues, while in others notably in the field of "Central" revenues and expenditure, there will be a net decrease. A careful consideration of all these matters, however relevant and necessary in any complete picture of the financial consequences of the merger, is clearly *not* relevant in the narrow context, of integrating only the "federal" finances of Baroda with those of the Central Government, to which alone we, by our terms of reference, must confine ourselves. Moreover we are of opinion that even if we were free to deal with the wider field of "merger finance", it would be incorrect to confine our attention to the problems arising out of the Baroda merger alone; our survey would have to be more extensive and we would be compelled to deal with the *other* States of Gujarat and Deccan which have also been merged into

Bombay in the last eighteen months. Clearly, such an extensive enquiry into the financial problems arising out of mergers of numerous State into Bombay (and other provinces), would be totally foreign to our terms of reference.

(c) We propose, accordingly, to deal with this case in the same manner as with other States and Unions with which we are concerned: namely, as a case of a *continuing* State integrating with the Central Government in the field of federal finance. The fact that such integration will occur in a merger context will make some, but not a significant, difference to our conclusions and recommendations; for the essential basic principles will remain the same, as will be seen both from our General Report (which will follow in due course) and from our second Interim Report concerning Travancore and Cochin (which we shall be submitting very soon).

## Practical Issues

9. Having clarified, in this way, the basis upon which alone the matter can be properly dealt with, we consider that the *practical* approach to the problem consists essentially in examining the following issues:—

(i) What are the specific functions, revenues, Capital assets and liabilities which the Centre must retain before making over the "Provincial" administration of Baroda territories to the Government of Bombay under Section 290-A of the Government of India Act, 1935?

(ii) What will be the consequences of such a step on the residual, or "Provincial", finances of Baroda State (regarded as a continuing State to be subsequently merged into the Bombay Province); and, to the extent that such consequences will be adverse by reason merely of federal financial integration, what would be the approprite remedies?

(iii) What adjustment will be necessary between the Central Government and the Government of Bombay (as successors to the Baroda "provincial" Government) in regard to the *current* assets and liabilities of the State, after all the specific productive and unproductive *capital* assets have been allocated between the two Governments on a *functional basis*?

(iv) What other consequential matters will require to be dealt with?

In Section III of this Report, we have dealt with the first issue and have also indicated, in general terms, the principles according to which the assets and liabilities of the State must be allocated between the two successor Governments. The other issues are examined in detail in the subsequent sections of the Report.

NOTE.—As indicated in paragraph 8 above, this Report deals only with the integration of the federal finances of Baroda with those of the Government of India as a result of the Order to be issued under Section 290-A of the Government of India Act, 1935. Consequently, the expression "date of the merger" wherever it occurs in this Report has reference to the date from which the Order to be issued by the Government of India under Section 290-A of the Government of India Act, 1935, has effect (and not to the 1st of May 1949, when the administration of the State was taken over under the Extra-Provincial Jurisdiction Act).

## III.—GENERAL PRINCIPLES

### Allocation of Revenue and Expenditure

10. Immediately upon federal financial integration, resulting from the issue of the Order by the Government of India under Section 290-A of the Government of India Act, 1935, the following items of "Central" Revenues and Expenditure, together with the administrations of the Departments concerned, must be taken over by the Central Government, as being properly within their *functional* ambit :—

(1) **"Central" Revenue Departments—**

Customs;
Income-tax;
Central Excises;
Cultivation and Manufacture of Opium;
Railways;
Telephones.



(2) **Other "Central" Departments—**

Defence, other than non-I.S.F. Units and Establishments;
Aviation;
Broadcasting (already taken over);
Meteorology;
Archaeology;
Patents, Copyrights, Trade Marks;
Registration of Joint-stock Companies and Firms;
Accounting and Audit.

All the remaining Departments and Revenues of the Baroda State are functionally of a "Provincial" character, and will, therefore, pass to the Government of Bombay.

### Allocation of Capital Assets

11. As regards *Capital* Assets and Liabilities of the State as at the date of the merger, the correct basis for allocation is again the *functional* basis, which,

stated in general terms, will operate as follows :—

(1) All *unproductive* specific Capital Assets connected with the "Central" functions and departments enumerated in the preceding paragraph, together with their current liabilities and outstandings (including pending assessments, refunds and claims outstanding, and arrears etc.), should be taken over by the Government of India.

(2) Similarly, all *productive* specific Capital Assets connected with all "Central" functions and departments (*e.g.*, Railways and Telephones) should be taken over by the Government of India, together with the *specific* public or other debt, *and* the current cash balances, liabilities and outstandings, if any, relating to them. A complete list of such assets and debts exists, and their book values are known.

As regards the relative Depreciation Funds, which are not separately invested in ear-marked investments, they will be taken over as deduction from the book values of these assets, *except* to the extent of any excess of current (or liquid) assets that may be available after meeting the current and "funded" liabilities of the State.

(3) The residual specific Capital Assets (both productive and unproductive), together with any *specific* debt, and current liabilities and outstandings connected with them, will go, again on the *functional* basis of allocation, to the Bombay Province.

The Depreciation Funds, if any, connected with such assets will be dealt with in the manner indicated at the end of sub-paragraph (2) above.

(4) In this way, neither the Government of India, nor the Government of Bombay, will have to pay any "compensation" either to the Baroda State or to each other for "acquiring" these assets or revenues; they will in fact merely "succeed" to these revenues and assets, as well as to the specific debts, liabilities and expenditure associated with them, as the "functional successors" to the Baroda State in the "Central" and "Provincial" fields of Government respectively. This position is not affected in any way, even if the case were regarded purely as that of a continuing State, integrating with the Central Government only in respect of all "federal" functions, including finance, and retaining to itself the entire field of "provincial" functions and finance.

**Allocation of Current Liabilities and Liquid Assets**

12. There remain the problems of allocation of the liquid or Current Assets (such as Bank Balances, Cash, Investments, Securities, Loans and Advances etc.) of the State as on the date of the merger. This allocation will stand on a somewhat different footing. The proper procedure here is first to allocate the

current and funded *liabilities* of the State between the two successor Governments and to place at the disposal of each equivalent current assets (so far as may be available) to meet such liabilities. The allocation of the liabilities themselves should be upon the *functional* basis, coupled with the principle of public convenience. These liabilities, as shown in the Baroda State accounts (enumerated in their order of "priority") are of the following types:—

(*i*) Current or "Banking" liabilities due to *outsiders* whether funded or not, and Trustee liabilities;

(*ii*) Liabilities in respect of *specific* "functional" Funds, such as Education, Village Uplift Funds etc.;

(*iii*) Capital Reserve Funds;

(*iv*) Specific "Revenue" Reserves or Funds;

(*v*) General (*i.e.*, non-specific) Development Funds;

(*vi*) Depreciation Funds, not specifically invested—[*vide* paragraph 11(2) *supra*.]

13. The grouping of liabilities in order of priority as above, and their allocation between the two successor Governments, purely on a functional basis within each category or group, together with an equivalent allocation of current or liquid assets will, in the main, present no difficulty. Moreover, as it should be one of the express conditions of the merger that assets so allocated in respect of specific Funds and Reserves shall be expanded by the Government concerned on the purposes specified, *within* the territories, and for the benefit of the people of *Baroda*, no special advantage or disadvantage will be conferred upon either of the successor Governments by this process of allocation. Nevertheless, apart from certain questions of detail, the following question of principle will arise for determination in this connection:—

(1) Where, between 31st July 1948 (the last account closing date of the State) and the date of the merger, any re-appropriations may have been made by the present Government of Baroda, with *retrospective* effect, in respect of Funds relating to "Central" functions (*e.g.*, out of Railway and Military Capital Reserve Funds), so as to affect those funds adversely, should such retrospective re-appropriations be accepted?

(2) How should any surplus of liquid assets over current liabilities (if such should be the case on the date of the merger, as it was on 31st July 1948), be dealt with?

(3) How should any surplus of current liabilities over liquid assets, (if such should be the case on the date of the merger), be dealt with?

**Plan of Detailed Working**

14. A detailed working showing the net revenue effect of integrating all "Central" Revenues and Expenditure Departments into the appropriate

Departments of the Government of India has been set out in Section IV, of this Report. Certain matters of detail arising out of such integration are also dealt with there. Finally, in the concluding paragraphs of that Section of the Report are contained our considered recommendations concerning the revenue adjustments which will be necessary to ensure that the finances of the Bombay Province should not be adversely affected by the (*net*) loss resulting from the present "Central" revenues and expenditure of Baroda going to the Central Government, *i.e.*, in consequence merely of the integration of the "federal finances" of the State with those of the Central Government.

As regards the allocation of the Assets and Liabilities of the State between the two successor Governments, a detailed working in accordance with the principles set out in paragraphs 11 and 12 above will be found in Section V of this Report. It also deals with certain miscellaneous matters which will necessarily arise in this connection and indicates broadly the physical technique to be adopted in implementing the proposals.

The workings and suggestions (in Section V) are based on the position as at the last account-closing date (31st July 1948). They are, therefore, entirely illustrative being designed merely to indicate the precise lines on which the allocation should be worked out with reference to the *actual* Assets and Liabilities shown by the accounts when closed at the time of the merger. The final allocations between the two successor Governments will thus remain indeterminate for some considerable time after the date of the merger.

## IV.—INTEGRATION OF "CENTRAL" REVENUES AND EXPENDITURE

### "Central" Revenues

15. The average annual revenue realised in Baroda from "Central" taxes, and from other "Central" sources of Revenue (such as Railways etc.), amounted to Rs. 185·72 lakhs, on the basis of actuals for three financial years of the State 1945-46, 1946-47 and 1947-48. This revenue will, after the merger, accrue wholly to the Government of India; its detailed computation is embodied in Statement I attached hereto.

The choice of the basic period for the computation requires some explanation. Having regard to the conflicting directions in which the component elements of Revenues in various States have moved in the past and are likely to move in the future, we have considered it proper to take the average of three (latest) *completed* accounting years of the State as the basis for our computations of the revenue which will be lost to the State as a result of federal financial integration. The date fixed for the integration of the State's administration with Bombay (1st May 1949) falls nine months after the commencement of the State's financial year 1948-49; we have, therefore excluded this incomplete year from the calculations, more especially as the actuals for this period of nine months will, for numerous reasons, be an unreliable guide for computing the revenue of a whole financial year on a *pro-rata* basis.

## Specific Matters relating to "Central" Revenues

16. Certain notes concerning the basis of computation of each item of "Central" Revenue are appended to Statement I itself. What follows are some further explanatory notes and certain specific recommendations concerning some items:—

(1) **Customs Duties** on foreign trade, which are already levied at the Indian Tariff rates and in accordance with the principles embodied in the Indian Sea Customs Act, will go wholly to the Central Government. The administration of Customs should accordingly be wholly taken over by the Central Government, *together with* all the "unproductive" capital assets, outstandings, liabilities, claims, etc. connected therewith *vide* paragraph 11(1) *supra*]; moreover, such State staff as may be wholly or substantially employed on "foreign" (as distinguished from "internal") customs work, should also be taken over by the Central Government in appropriate grades and on terms not less advantageous than in the State's Service. We recommend accordingly.

In our view no "transitional *limitations*" will be necessary to the application, *proprio vigore*, of the Indian Sea Customs Act, Import-Export Tariff and all the other relevant Acts, Ordinances and Rules to Baroda; but necessary steps should be taken to secure legal "continuity" in respect of matters done or pending under the Baroda Acts at the time of the merger. This may involve—

(i) extending not merely the legislative but also the executive and administrative competence of the Central Government and also the judicial authority of its Courts to the territories of the State;

(ii) amending the Sections concerned with the "extent of application" of the aforementioned Indian Acts and Ordinances so as to include the territories of the Baroda State;

(iii) providing that all matters and proceedings pending under, or arising out of, the pre-existing Baroda Acts shall be disposed of under *those* Acts by, so far as may be, the corresponding authorities under the corresponding Indian Acts;

The present arrangements for pooling and sharing customs revenue with Baroda will automatically terminate; but there will remain outstanding the division of customs revenue collected by the State up to the date of the merger. The manner in which this should be dealt with is indicated in Section V of this Report in connection with the allocation of Assets and Liabilities.

(2) **Corporation Tax, Income-Tax and Super-Tax** (other than taxes on Agricultural Income.)

The general position as regards "taking over" by the Government of India, including the transitional provisions required for ensuring legal "continuity of proceedings", will be the same as for the Customs Department; *vide* sub-para. (1) above.

There is, at present, a combind staff for the Income-Tax and Sales Tax Departments. We recommend that such part of this joint staff as is wholly or substantially engaged on Income-Tax work *and* has not less than two or three years' experience of Income-Tax work (assessment, survey and clerical) should be taken over by the Central Government for Income-Tax work, and the rest by the Provincial Government for Sales Tax work in Baroda territories.

In view of the fact that taxes on income are normally assessed in respect of the profits of the "previous year", and the *Indian* rates of tax are, (and have been), considerably higher than those now (or in the past) in force in Baroda, we recommend that suitable "transitional" provisions should be enacted to provide that profits accruing or arising in Baroda State right up to the date of the merger (under section 290-A of the Government of India Act, 1935), if not *otherwise* taxable in India, should be taxed as follows:—

(i) income, profits and gains of periods which are the "previous years" of Baroda assessment years 1948-49 and earlier should be assessed in accordance with *Baroda Income-Tax* and at the *Baroda rates* appropriate to the assessment year concerned;

(ii) income, profits and gains of all subsequent periods may be assessed according to the *Indian law* and rates, but as respects so much of such income as relates to the period or periods up to the date of the merger, the *rates of taxes* applicable should be those of the State as on the day preceding the merger.

The effect of this will be that Indian *rates* of tax will become effective only in respect of incomes of periods *subsequent* to the date of the merger, the Indian *law* will be effective only in respect of incomes of periods subsequent to the end of the "previous" year relevant to the State's assessment year 1948-49, and that in respect of incomes of periods relevant to the State assessment years 1948-49 (and earlier) the State law *and* the State rates will continue to be effective.

One important modification which the interests concerned are anxious to secure is that in respect of transactions of the period beginning from the end of the "previous year" relevant to the State assessment year 1948-49 and ending with the day preceding the merger (the income of which would, according to the above proposals, be assessable under the *Indian law* but at *Baroda rates*), the following provisions of law should *not* be invoked:—

Section 18 of the Indian Income-Tax Act.
,, 18A ,, ,, ,, ,,
,, 23A ,, ,, ,, ,,
,, 16 (1) (c) and (3) ,, ,,
Act XXII of 1949 (concerning payment of taxes *before* "recognition" of Transfer of property).

We support this request, but (except as regards Act XXII of 1949 which replaced the Transfer of Property Ordinances) would restrict the concession only to the assessment of the income of the period in question.

Unlike Customs and Central Excise Duties, Income-Tax is not at present a divisible revenue between the State and the Government of India. Subsequent to the merger of the State into Bombay, however, 50 per cent. of the net income-tax collections (other than Corporation Tax and taxes on "federal emoluments" etc.) made in the territories of the State by the Government of India will be divisible among *all* the provinces of India in accordance with the division ratios now in force. Bombay's share of the "divisible pool" may, therefore, require to be enhanced (from the present 21 per cent.), in view of the addition to its population and needs, and to the collections that will be made in that province in future, in consequence of the merger of Baroda. We recommend that this revision should be undertaken *at once*.

Certain other issues which arise in connection with Income-Tax are dealt with below:—

(a) **Double Income-Tax Relief.**

Where double-taxation has already occurred, or may (perhaps) inadvertently occur even after the merger, we recommend that relief should continue to be given in accordance with the existing D.I.T. Relief arrangements between India and Baroda. After the merger, however, double-taxation should be rare, if cases were properly distributed in accordance with the provisions of Section 64 of the Indian Income-Tax Act, so that two officers may not deal with the same case.

(b) **"Remittances".**

Under the Indian Income-Tax Act, incomes, profits or gains accruing or arising in Indian States are not taxable in India, unless they are received *in*, remitted to or brought into "British India", or are *deemed* to have accrued or arisen or been received in "British India". This position must continue unchanged in respect of transactions up to the date of the merger.

Therefore—

(i) Any movement of funds to/from Baroda from/to "British India" on or after the date of the merger should have no significance, being merely an *internal* movement of funds *within* "British India";

(ii) Funds which may be already physically in Baroda on the day preceding the merger should not be treated as "remitted" to "British India" subsequently by the mere fact of the merger.

(iii) Remittances *to* Baroda from "British India" or anywhere else *prior* to the date of the merger would have significance only in relation to the pending assessments of *the State* (or to any later assessments of which some part would be assessable at

State rates) in respect of incomes of "previous years" (whole or part) up to the date of the merger. Their relevance to the corresponding Indian Assessments would be, not *qua* remittances, but only *qua* "information", *e.g.*, as material (under Section 34) disclosing possible escapement of income which might (had its existence been known have been *otherwise* taxable under the Indian Income-Tax Act in any case.

We would suggest the issue of instructions in the above sense by the Central Board of Revenue at the earliest opportunity; we apprehend that in the absence of some such specific instructions there is some danger, especially in the case of junior Income-Tax Officers, of a misunderstanding concerning this highly technical matter.

(c) **Disputed Indian Assessments.**

We were given to understand that in a number of cases assessments have been made, or are contemplated, *in India* in respect of income, profits and gains claimed by the (Indian) Income-Tax Officers, but denied by the assessees, to have accrued, arisen or been received, or as deemed to have accrued, arisen, or been received, in "British India". In many of these cases there are appeals pending at various stages. It has suggested to us that *in such of these cases only as are now in appeal*, the portion of the disputed profits taxable in India might, as a matter of compromise, be computed on the principles and according to the formulate embodied in the Indo-Pakistan Double Taxation Avoidance Agreement. We incline to support the settlement of these cases, on the occasion of the merger, on the lines suggested, *on condition* that the assessees concerned agree in writing that no *further* claim for Double-Taxation Relief would be entertainable in respect of assessments so settled, either against the relevant Baroda assessment or the relevant Indian assessment, notwithstanding that the double-taxation may in fact have resulted even on the modified basis of assessment.

Although this matter is not strictly one arising out of the merger, we recommend the above proposal for consideration by the Finance Ministry (Revenue Division).

(d) **Individual "Immunities" from Taxation—**

(i) There are only three such cases of private concerns. Two of them (Sheth Shantidas Mangaldas of Ahmedabad and Sir Homi Mehta of Bombay) have not yet set up the industrial concerns in respect of which they were to have enjoyed some limited immunity from Income-Tax in Baroda. They will accordingly be automatically entitled to the various concessions already available to "new industries" under the Indian Income-Tax Act in India, and it is, therefore, in our opinion, unnecessary to go beyond those concessions so far as these two cases are concerned.

The third case is that of Messrs. Tata Chemical Industries Ltd., Mithapur. The maximum scope of the present concession in this case is that the company should not pay more Indian and Baroda taxes, *in the aggregate*, than the amount payable at the *higher* of the two rates of taxes. There is, moreover, a clear provision that any "federal", taxes levied under the authority of the "Federation of India" shall always be payable. In the circumstances, no special "protective" provision is in our opinion necessary for this case also.

(ii) As regards the Ruler, and such political pensioners of the State as may now enjoy any taxation immunities, we recommend that their existing taxation immunities, whether under the State Law or under the Indian Income-Tax Act, should be protected. If the continuance of these immunities cannot (as we think) be ensured by executive instruction or statutory (exemption) notifications, necessary provisions should be made by appropriate legislation.

(e) **Capital Gains Tax.**

We recommend that Capital Gains Tax should not be leviable in respect of any Capital Gains accruing in the State prior to the merger.

(f) **Business Profits Tax.**

We recommend that the commencing date of the first "chargeable" period should be the date of the merger. Business profits of earlier periods should not be charged to B.P.T.

(3) **Opium (cultivation and manufacture)**

This department of the State is "Central" and should, on merger, be taken over by the Central Government in accordance with the procedure indicated under sub-para. (1) above in respect of Customs Department. Thereafter, the issue of opium to the Provincial Government for sales in Baroda territories may be done in the same way and on the same terms as elsewhere in the Province.

As in the case of Customs, "transitional" provisions will be necessary to ensure legal "continuity of proceedings".

(4) **"Central" Excise Duties**

The "taking over" procedure will be the same, *mutatis mutandis*, as that indicated in sub-para. (1) above in connection with Customs, including the necessary "transitional" provisions required to ensure legal "continuity of proceedings".

We do not consider that there will be any difficulty in the way of introducing the whole range of Indian "Central" Excise Duties in Baroda at full Indian rates.

The present arrangements for pooling and sharing Central Excise Duties with Baroda will automatically terminate on merger. But there will remain "in suspense" a large amount of such revenue previously collected (relating to a period of nearly three years); the question of the possible division of this revenue between the Central Government and the Government of Bombay in accordance with the pre-existing formulae will, therefore, arise. This problem has been dealt with under "Assets and Liabilities" in Section V of this Report.

### (5) Salt

If this Department still exists, it will have to be taken over by the Central Government. The "taking over" process including the "transitional" provisions required to ensure legal "continuity" of proceedings would be the same as for the Customs and "Central" Excise Departments.

### (6) Department of "Internal" Customs Duties

This is *not* a "Central" Department; and we understand it has already been wound up. But if it still exists, it will be necessary for the Bombay Government to take it over and to liquidate it as soon as possible after the merger, as internal customs duties cannot, under any circumstances, be continued thereafter.

### (7) Railways

On merger, the Central Government must take over the entire Railway system [including any "foreign" lines worked as part of the State Railway system and any State lines now "worked" by other (Indian) lines], together with all the staff, Assets, Liabilities and Funds [*vide* paragraphs 11 (1) and (2) and 12 *supra*]. The entire staff should be taken over in appropriate grades and on terms not less advantageous than in the State's Service.

We suggest that the portions of the State Railway system which are in Saurashtra may, on the date of the merger, be made over to the Saurashtra Government for working as part of the Saurashtra Railways system, upon terms to be mutually agreed.

The Railway Depreciation Fund and Capital Reserve Fund, Provident Fund, Staff Benefit Fund (?) and Betterments Fund are carried by the State; the State also carries certain Railway "Deposits" and has made Loans and Advances for Working Capital to the Railways. All these should be computed as on the date of the merger, and continued to be borne in the books of the Railway; but the treatment of these balances in the books of the Government of Baroda should be as shown below (in Section V) under Assets and Liabilities.

(8) **Telephones**

This Department should be dealt with on the same lines as recommended above in the case of Railways.

(9) **Postal "Immunity"**

The Baroda State now enjoys the privilege of receiving free of cost, from the Government of India, "Service" Postage Stamps of the value of Rs. 1·25 lakhs. This privilege should cease with the merger of the State into Bombay; precisely for that reason, the value thereof has been taken into account by us in computing the "revenues" of the State which will not go to Bombay.

### "Central" Expenditure

17. Statement II attached hereto shows that expenditure of a "Central" character incurred by the State during its last completed fiancial year (1947-48) amounted to Rs. 59·86 lakhs. After merger, this will have to be wholly borne by the Central Government.

We have already indicated, in paragraph 15 *supra*, the reasons for not including the State's financial year 1948-49 among the basic years for our revenue computations in this case; those reasons are of equal, if not greater, validity in connection also with the computation of the expenditure which will be saved to the State as a result of federal financial integration. It only remains to add that the reason for taking the actual figures of 1947-48 only, instead of the average of the three years ending 1947-48, as the basis for computing such expenditure, is that, unlike revenues, expenditure has a tendency not to go below the level reached in the latest year, especially if (as in this case), its trend in recent years has been steadily upward. We consider, therefore, that subject to certain modifications indicated in Statement II, the expenditure actually incurred on "Central" subjects in Baroda during 1947-48 affords the most reliable measure of the expenditure which will be saved to the State upon the integration of its "federal" finances with those of the Government of India.

### Specific Matters relating to "Central" Expenditure

18. Certain notes concerning the computation of some of the items of "Central" expenditure are appended to Statement II itself. What follows are some further explanatory notes and recommendations concerning some items:—

(1) **Customs Department;**

(2) **Central Excise Department;**

(2A) **Opium (cultivation and manufacture);**

(3) **Income-Tax Department.**

Reference may be made to paragraph 16 *supra* for our comments and recommendations upon matters which will arise in connection with the taking-over of the staff and the administration of these Departments by the Central Government.

### (4) National Highways

According to information furnished by the Ministry of Transport (Roads Organisation) a stretch of 66 miles of roadway in Baroda is classifiable *at present* as National Highways. An amount of Rs. 1·98 lakhs, representing the estimated cost of maintenance of, including "current" improvements to, this road at Rs. 3,000 per mile per annum, has accordingly been included in Statement II. Any roads which may *hereafter* become eligible for declaration as "National Highways" would be roads of the Bombay Province (*including* Baroda territories) and would be dealt with as such in the ordinary way.

### (5) Defence (Indian State Forces)

The "provision" for raising and training new units, and the cost of *non*-I.S.F. units and establishments, including their pensions, have been excluded. The latter are irregular forces which, if continued after the merger, would be a charge on "provincial" revenues. On the merger, the Central Government must take over all I.S.F. units as a "going concern", together with all establishments, installations and equipment, including all "unproductive" assets, outstanding liabilities and funds, connected with them [*vide* paras. 11(1) and 12 *supra*]. The treatment of certain military Funds, including a military Pedhi (a sort of loan institution), etc., should be as indicated below (in Section V) under Assets and Liabilities.

In our discussions on the subject of Defence expenditure, the Dewan of Baroda objected to its being taken at Rs. 45 lakhs (as shown in Statement II). His contention was based chiefly on two grounds:—

(i) that such expenditure was considerably lower both in 1948-49 and in the two years 1945-46 and 1946-47;

(ii) that it was inflated in 1947-48 due mainly to the Ruler's decision to provide for raising and training new units.

We have given the matter our most anxious consideration, but are unable to accept these contentions quite to the extent the Dewan Saheb would desire. In the first place, we are clear that having decided to take 1947-48 as the "base" year for our computations, the figures relating to *earlier* years could not be accepted as relevant at all. In fact, in all the other cases we have so far examined, the trend of expenditure on Defence was also in the same direction as in Baroda; and in those cases, too, we have decided not to modify our computations merely because of lower expenditure in earlier years. Secondly we are quite unable to accept the 1948-49 (revised) estimate of Defence expenditure as a proper guide for our present purposes, as the circumstances in that year have been (and continue to be) exceptional in Baroda. Proceeding, therefore, on the basis of 1947-48 figures alone, we have arrived at the sum of Rs. 45 lakhs as follows:—

| | Rs. (in lakhs) |
|---|---|
| *Total* actual military expenditure in 1947-48 . . . | 72·68 |
| *Less* provision for raising and training new units . . | 7·00 |
| Balance . | 65·68 |
| I.S.F. Defence expenditure at 60% thereof . . . . | 39·41 |
| *Add* Maintenance of buildings (charged to P.W.D.) . . | ·80 |
| Dearness and other Allowances (charged to Civil Estimates) | 5·48 |
| | 45·69 |

In one of his communications to us on this subject, the Dewan of Baroda suggested that the normal expenditure of the State on Defence (I. S. F.) should not be taken at more than Rs. 36 lakhs per annum. Adding to this the expenditure charged to Civil estimates in 1947-48, the amount would be Rs. 42 lakhs approximately. This is only Rs. 3 lakhs less than the figure adopted by us. Nevertheless, we regret we are unable to accept the suggestion.

**(6) Aviation and Archaeology**

These departments, together with their staff and all the unproductive assets etc. [*vide* para. 11(1) *supra*] connected with them will have to be entirely taken over by the Central Government.



**(7) Broadcasting**

*Broadcasting* has been already taken over by the Central Government, on *payment* for the value of the assets taken over. As this was a pre-merger transaction, perhaps nothing can be done about the payment. We are unable, however, to accept the suggestion made by the Dewan of Baroda, that the expenditure incurred on this Department in 1947-48 (the "base" year) should be ignored in computing "Central" expenditure (Statement II). The contention that there was no such expenditure incurred *by the State* in 1948-49 seems to us altogether irrelevant; for the fact remains that Broadcasting as such continued in Baroda, though operated by and at the expense of, the Government of India. We have accordingly included the expenditure in Statement II.

**(8) Meteorology**

There is no separate State Department, as such, concerned with this subject; the present arrangement is that meteorological work is done for the State by a section of the staff of the Baroda College, at a cost of approximately Rs. 0·07 lakhs per annum to the State. It will be for the Government of India to decide whether they should continue this arrangement in future or establish their own independent meteorological Department: in the latter event they may have to take over such of the Baroda College staff as may be wholly or mainly engaged on this work, if the College authorities should so insist.

(9) (a) **Patents, Copyrights and Trade Marks;**

(b) **Joint Stock Companies.**

These departments will have to be taken over by the Government of India, together with such staff as may be wholly or substantially engaged on these duties. Of them, (a) may be merged with the corresponding Department of the Government of India at Bombay; and (b) may be merged with the office of the Registrar of Joint Stock Companies and Firms at Bombay, (working for sometime, however, as a separate wing located at Baroda itself). As regards the taking over of the dead-stock, assets and liabilities of these departments, reference is invited to para. 11(1) *supra*.

(10) **Pensions**

The pension liability in respect of I. S. F. Military personnel and "Central" Civil departments personnel who may have retired before the merger will be that of the Central Government. All these will be payable at one or other of the treasuries in Baroda. From a *practical* point of view it will serve no useful purpose to disturb these arrangements. We, therefore, recommend that these payments (of which a *complete* list should be compiled on the date of the merger) should continue to be paid at various Baroda Treasuries as at present *on account of the Government of India* (*i.e.*, to the debit of their account annually) by the Government of Bombay. Pensions in respect of retirements occurring *after* the merger will be payable in the ordinary way directly by the Government of India.

(11) **The Accounts and Audit Department** of the Baroda Government will, upon merger, devolve *entirely* upon the Central Government. The only exception will be—

(a) The section dealing with non-I.S.F. Military Audit;

(b) The section dealing with Investments;

(c) The sections dealing with compilation and Budget, Savings Bank, Contingency and Dead Stock.

Of the above, (c) will have to go entirely to the Provincial Government to be merged into its Secretariat (Finance Department); and sections (a) and (b) will have to be taken over by the Central Government and wound up. [Actually, the staff concerned need not necessarily be discharged but may be absorbed in the vacancies already existing in the various sections of the office of the Accountant-General, Bombay].

The rest of this Department will have to be wholly taken over, together with all its staff and unproductive assets (*e.g.*, buildings, dead-stock etc.), outstandings and liabilities etc. [*vide* para. 11(1) above] by the Central Government. We suggest that it may be found useful to continue the whole organisation, for sometime at any rate, at Baroda and to absorb it gradually into that of the Accountant-General, Bombay.

(12) In connection with some, if not all, of the Departments referred to in sub-paragraphs (1) to (11) above, "transitional" provisions will be necessary to ensure legal validity and "continuity", after the merger, of proceedings taken or pending under the relevant Baroda Acts.

## Financial (Revenue) Adjustments required between the Central Government and the Government of Bombay

19. We now come to the financial adjustments which, in our opinion, will be necessary on revenue account between the Central Government and the Government of Bombay (as successors to the Government of Baroda in the field of "provincial" administration and finance). As we have pointed out earlier these adjustments take no account of the wider financial problems arising out of the merger as such, but are concerned with only the results of integrating the "federal" or "central" finances and expenditure of Baroda with those of the Central Government. The objective, therefore, is the strictly limited one of ensuring that the finances of *Baroda* (regarded as a continuing State) should not be adversely affected by the fact that its "Central" revenues, functions and assets will be taken over by the Central Government.

20. The gross revenue-gap in the finances of Baroda, in consequence of the loss of "central" revenues and taxes as a result of federal financial integration will amount to Rs. 186* lakhs per annum in round figures; (*vide* Statement I and paragraph 15 *supra*). As against this, the Central Government will assume responsibility for all "Central" expenditure in Baroda, which, for this purpose, may be taken to amount to Rs. 60 lakhs per annum; (*vide* Statement II and paragraph 17 *supra*).

Our recommendations for making good the resultant net "revenue-gap" *viz.*, Rs. 126 lakhs per annum, are as follows:—

(i) The Bombay Government (as successors to the Baroda Government in the "provincial" field) must, *with effect from* 1950-51,

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*NOTE :—To this must be *added* the interest receivable in future by the Government of India on the *current* assets to be assigned to them *less* the interest payable by them in future on the *current* liabilities to be assigned to them, in accordance with the procedure indicated in paragraphs 26-28 of Section V of this Report. The net amount to be so added is not readily ascertainable and will not be known precisely until after the merger; accordingly it has been ignored for the purposes of the subsequent calculations in this and later paragraphs assume responsibility for 40 per cent. thereof, *i.e.*, Rs. 50 lakhs *per annum* (in round figures).

(ii) The Central Government must guarantee to make good to the Bombay Government the entire net revenue-gap of Rs. 126 lakhs (per annum from the date of the merger) in 1949-50, and Rs. 76 lakhs (per annum) for the next ten years. This they should do in the shape of—

(a) The incraesed amount which Bombay will receive on account of divisible income-tax and other federal taxes (such as they may be from time to time) on account of the addition of Baroda territories to the Province; *and*

(b) an *ad hoc* revenue-subsidy to the extent that (a) should fall short of the guaranteed amount.

It should be noted that all other subsidies (including food subsidies), all grants-in-aid, and all other forms of central assistance which Bombay may be accorded as a result of the accretion to its area, population and needs, in consequence of the merger would be entirely outside (*i.e.* in addition to) the above payments.

**Comments**

(1) As regards proposal (i) above, the figure of Rs. 50 lakhs represents a considerable improvement on a somewhat higher figure (*viz.*, Rs. 60 lakhs) which was agreed to, after discussion with the representatives of the Bombay and Baroda Governments, as the burden which might reasonably be borne by the State, regarded as a continuing entity, when integrating with the Central Government on federal finance. In our considered opinion there would be no difficulty at all in the way of the Baroda State undertaking this burden a year after federal financial integration. The main sources from which it could make good the whole of this amount in 1950-51 would be:—

| | Rs. (Lakhs) |
|---|---|
| Saving in Privy Purse (Civil List) | 23·50 |
| Raising the "Provincial" taxes to the Bombay level (1948-1949) | 25-00 |
| Requiring Municipalities to raise their taxes sufficiently to become self supporting. | (more than 1·50) |

(2) We fully recognise that this method of dealing with the matter has the effect of isolating the problem, resulting from the integration of federal finances of Baroda with those of the Central Government, from the wider financial and other issues arising out of the merger of the State into the Bombay Province. But, as we have already stated, this method of approach has been deliberately chosen by us as being the only one strictly within our terms of

reference. We also recognise that the merger of this State as such will raise many difficult financial issues which will have to be urgently tackled as part of the over-all problem of "merger finance" embracing the finances of the Bombay Province *as a whole* in relation not only to Baroda but also to the numerous other States which may have been merged into or integrated with it since 15th August, 1947. Finally, even in regard to the merger of Baroda, considered by itself, several factors will have to be taken into account, besides those considered by us. Some of these factors are:—

(a) **On the "Credit side":**

The savings and increases in resources already referred to above, *viz.*, saving in Privy Purse; increased "provincial" revenues of Baroda at Bombay (1948-49) rates; and decreased municipal subsidies;

The "central" (guaranteed) subvention as above of Rs. 126 lakhs (per annum) in the first year of merger, and Rs. 76 lakhs per annum thereafter; (or Bombay's increased share of divisible "federal" taxes, if that should be higher than the guaranteed sum in any year);

Increased food-subsidies (from 50 per cent. to 75 per cent.) in respect of losses on the sale of imported foodgrains; and procurement and export "bonus" on foodgrains;

Increase in "provincial" revenues of Baroda at Bombay (1949-50) rates;

Savings in "Headquarters" expenditure of Baroda (executive, judicial, legislative, administrative and secretariat);

Savings in Baroda District Administration (from consolidation of scattered territories);

Savings of some considerable part of the non-I.S.F. Defence expenditure;

Savings in miscellaneous "Khangi" and official expenditure of the Ruler (other than Privy Purse strictly so called);

(b) **On the "Debit side":**

Higher salaries at Bombay rates, to such staff as may be retained after the merger;

Other additional expenditure, *e.g.*, to deal with increased work, at the Headquarters of the Bombay Government.

The net revenue-gap of Rs. 126 lakhs per annum by reason of "Central" revenues and expenditure being taken up by the Central Government.

Fresh recurring commitments entered into by the Baroda administration during 1948-49. (We assume, though we should not be understood as recommending, that all these commitments would be binding on the Bombay Government).

A complete survey of Baroda post-merger finances on the lines indicated above would, we conceive, be necessary, as constituting an important part of any over-all survey of the problem of "merger finance" of the Bombay Province as a whole. But such a task would be clearly outside our terms of reference; and we do not propose, accordingly, to embark on it.

### Ruler's Privy Purse

21. It remains for us to deal with the question of Privy Purse of His Highness the Gaekwar of Baroda. This presents a difficult problem, because "Privy Purse" is not at present a "Central" liability; and it is also not so under the Draft Constitution of India. The financial adjustments consequent on the merger, as proposed by us, have, therefore, been evolved on the basis, and on the presumption, that the Privy Purse will be a charge on the revenue accruing to Bombay. We accordingly recommend that *if* it should subsequently be decided that Privy Purse should be made payable out of "Central" revenues, the sum involved (Rs. 26.5 lakhs) should be added in Statement II as expenditure to be borne by the Central Government as a result of federal financial integration consequent upon the merger. In that event—

(i) The net "Central" revenue-gap of Baroda would be reduced to Rs. 100 lakhs (in round figures);

(ii) The burden to be borne by Baroda from 1950-51 onwards would be reduced to Rs. 40 lakhs; and

(iii) The Central Government's guaranteed subvention would be reduced to the amount by which Bombay's increased share of income-tax (and other divisible federal taxes, if any) should fall short of Rs. 100 lakhs (per annum) in 1949-50 and Rs. 60 lakhs per annum thereafter.

(iv) Our other proposals would remain unaffected.

In this way our scheme of financial adjustments, which is based upon a certain appropriatness or "balance" in the distribution of the burden resulting from the federal financial integration will be preserved.

We would observe, however, that any proposal to "centralise" Privy Purse payments should not be considered with reference to the conditions of Baroda alone; because whatever decision is taken in that case will naturally apply not only to all other "merging" States but also to all continuing States and Unions which may agree to integrate with the rest of India on "federal" financial matters. The point is, therefore, one which, we suggest, the Government should decide as a question of general policy.

## V.—ALLOCATION OF ASSETS AND LIABILITIES

### Capital Assets and Liabilities

22. As regards the allocation of *Capital* Assets, both productive and non-productive, together with the *connected* liabilities, we have little to add to what we have already stated by way of governing principles in paragraph 11 *supra*. Their practical application will have results as illustrated below by reference to the position as it was on 31st July 1948, *i.e.*, at the end of the State's financial year 1947-48.

23. All *unproductive* specific Capital Assets connected with the various "Central" functions and departments dealt with in Section IV of this Report should be taken over by the Central Government. These assets will consist mainly of lands, buildings, aerodromes, aviation works, laboratories, apparatus, appliances, furniture, office equipment and appliances, stocks of stationery and forms, etc. in use on the date of the merger in the various "Central" departments. There are unlikely to exist any comprehensive lists of such assets, except perhaps some departmental lists, with book values noted in some cases only. These assets must be taken over by the Central Government as they are, in each Department, by inventory. No valuation need be attempted as it will serve no useful purpose.

All running, or "continuing" liabilities and outstandings in each "Central" Department must similarly be taken over. On the "cash" system of accounting (followed by all Governments) these items will not have been "accounted" for at the time of account closing. They will consist of pending bills for supplies, stores, contracts, services and contingencies; pending assessments; arrears of revenues and refunds; outstanding claims for and against Government, etc., etc. No "account" need be rendered of these also; but an immediate inventory at the time of taking over would be desirable.

24. Similarly, the Central Government must take over all the *productive* specific Capital assets connected with "Central" functions together with any specific debts connected with them. Depreciation Funds connected with them not having been specifically invested separately, will be taken over as deductions from the book values of these assets, *except to the extent* of any excess of current or liquid assets that may be available after meeting the current and "funded" liabilities of the State.

The "Central" Productive Capital Assets. on 31st July 1948, two, as follows:—

**Productive Capital Assets—Central :**

| | (Lakhs) |
|---|---|
| (1) Telephones—(Book Value) . . . . . . | 12·27 |
| *Add* Expenditure out of Post-War Reconstruction Fund . | 0·51 |
| | 12·78 |
| *Less* Depreciation Fund (not invested) | * |
| | 12·78 |
| (2) Railways—(Book Value of Baroda State Railway *plus* the State's financial interest in the Tapti Vally Railway ; *vide* "Note" below). . . . . . . | 653·47 |
| *Less* Depreciation Fund (not invested) | * |
| | 653·47 |

*These Funds, though not separately invested, are *not* deducted here from Book Values because, on 31-7-48, there was a surplus of liquid or current assets over current liabilities sufficient to cover these Depreciation funds [*vide* paragraph 28 (ii) below].

**Specific Debt :—**

| | |
|---|---|
| (1) Telephones . . . . . . . . | *Nil* |
| (2) Railways (Loan from "Khangi" for Vijapur-Kalol Bailway) | 3·00 |
| Loan from "Khangi" for the Tapti Valley Railway . | 39·08 |
| | 42·08 |



The *net* value of productive Capital assets to be taken over by the Central Government would thus, be Rs. 624.17 lakhs on 31st July 1948.

NOTE.—(i) The total amount paid by the Baroda State for their interest in the Tapti Valley Railway was Rs. 51·47 lakhs (inclusive of a "premium" of Rs. 8·50 lakhs). Of this only Rs. 12·39 lakhs was actually paid out of State Funds, and the balance (Rs. 39·08 lakhs) was paid out of "Khangi" Reserve. This did not matter so long as H.H. The Gaekwar continued to be the *de facto* Ruler of the State; but now that the State is to merge into the Dominion, the entire interest must pass to the Government of India. It follows that the amount paid out of "Khangi Reserve" must be reimbursed to it, to be subsequently dealt with in the same manner as other assets held against that Fund. This is provided for in the above computation by taking the book value of this Railway at Rs. 51·47 lakhs and showing the payment originally made out of "Khangi" as a specific railway *Debt* to be made good to "Khangi" by the Government of India.

(ii) Subsequent to the merger, the Government of India will have to write off the "premium" amount of Rs. 8·50 lakhs included in the book value of the Tapti Valley Railway.

25. The Provincial Government should take over all the remaining unproductive and productive *Capital* assets. While no inventory is possible (or need necessarily be taken) of the former, assets of the latter category on 31st July 1948 were as follows:—

**Productive Capital Assets Provincial:**

| | Rs. (Lakhs) | Rs. (Lakhs) |
|---|---|---|
| (1) Electric Schemes (Book Value) . . . | 46·22 | |
| *Add* Expenditure out of Post-War Reconstruction Fund. | 0·05 | |
| | 46·27 | |
| *Less* Depreciation Fund (not invested) | * | 46·27 |
| (2) Port Okha—Minor Port—(Book Value) . . | 63·00 | |
| *Add* Further Expenditure as above . . . | 26·33 | |
| | 89·33 | |
| *Less* Depreciation . . . . . . | * | 89·33 |
| (3) Productive Irrigation Works & Vijapur Tube Wells (Book Value) . . | 31·43<br>20·49 | 51·83 |
| (4) Govt. Printing Press (Book Value) . | 4·60 | |
| *Less* Depreciation . . . . | * | 4·60 |
| (5) State Furniture Factory (Book Value) . . | | 0·30 |
| | | 192·33 |

There was no specific debt outstanding against the above Assets.

*These Funds, though not separately invested, are *not* deducted here from Book values because, on 31st July 1948, there was a surplus of liquid or current assets over current liabilitie sufficient to cover these Depreciation Funds [*Vide* paragraph 28 (ii) below].

**Current or Banking Assets and Liabilities:**

26. We now turn to the allocation of the State's current or "banking" assets and liabilities. As already stated in paragraph 12, "the proper procedure here is first to allocate the current and funded *liabilities* of the State between the two successor Governments..............upon the *functional* basis, coupled with the principle of public convenience". Statement III attached hereto shows what these liabilities were on 31st July 1948, arranged in their

"order of priority"—beginning with liabilities due to "outsiders" and ending with non-specific Development Funds and Reserves,—and showing how they should be allocated between the two Governments on the basis stated.

Apart from certain purely "computational" notes concerning certain items embodied in Statement III, the following important points arise in connection with some of them:—

**(1) State Savings Bank (Item 1 of Section A of Statement III).**

This is *not a* "Postal" Savings Bank, but a State concern like the Savings Bank Department of any ordinary Commercial Bank. It is not, therefore, a "Central" subject.

This Savings Bank scheme in the State is *additional* to the ordinary Postal Savings Bank run by the Government of India through the Posts and Telegraphs Department. The State's Savings Bank accounts are maintained at the various State Treasuries; and the Depositors are free to maintain a Savings Bank account either with the Government of India (at Post Offices) or with the Government of Baroda (at their Treasuries). Functionally, as well as on grounds of public convenience, it will be best for these State Savings Bank accounts to be carried in future by the Bombay Government; any other decision would, moreover, have adverse consequences on the "Ways and Means" position of Bombay, which must be avoided. We recommend accordingly.

The question whether, besides continuing the existing State Savings Bank accounts, the Bombay Government should accept any *new* accounts or any further deposits from the existing depositors, stands on a different footing. In our opinion, the answer must be in the negative (especially as regards opening *new* accounts), unless Bombay is already conducting a Savings Bank Department through its own treasuries.

We would add that the recommendations which we have made on this subject are designed, on the one hand, to avoid any immediate inconvenience to existing depositors or any immediate disturbance in Bombay's Ways and Means position and, on the other, to provide for the gradual "voluntary" liquidation of this Department over a period of years by not permitting any fresh deposits and allowing only withdrawals.

**(2) State Life Assurance Fund (Item 3 of Section A of Statement III)**

This, again, is not a "postal" insurance scheme, but an ordinary "Life Assurance" scheme run by the State (confined to Government Servants) in the same way as by any Insurance Company. Functionally, as well as on grounds of public convenience, there is no need to allocate the Fund to the

Central Government. We recommend that the Bombay Government may take it over and decide subsequently whether it should be transferred (together with corresponding investments), at its actuarial valuation to the Indian Posts and Telegraphs Department. In any arrangement finally adopted, the interests of the assured (quite irrespective of whether their services are transferred to the Bombay Government or to the Central Government, as a result of the merger) must be fully safeguarded, and the facility which they now enjoy, of having their premia deducted from their pay bills, must be continued.

Should the Bombay Government decide to continue the Department themselves, they should not, of course, issue any *new* policies, since the existing Postal Insurance scheme of the Government of India *already* provides the necessary facility for all Government servants in India.

**(3) Accident Insurance Fund (Item 4 of Section A of Statement III)**

The position here is the same, *mutatis mutandis*, as stated above in connection with the State's Life Assurance Fund, except that there need be no objection to the Bombay Government's continuing to carry on the Accident Insurance Fund by further annual contributions to it.

**(4) Provident Fund (Item 5 of Section A of Statement III)**

The Provident Funds relating to the staff employed in Railways, Broadcasting and Telephones will have to be wholly taken over by the Central Government.

So much of the Provident Fund balances of the "Other Departments" (Statement III) as may relate to the staff to be taken over by the Central Government will also have to be taken up by the Central Government. As the ascertainment of this staff is not likely to be delayed beyond a month after the date of the merger, all the required particulars will be readily available at the time of account-closing as at the date of the merger.

The rest of the Provident Fund Balances must be taken over by the Bombay Government.

It is *most important* that there should be an account-closing as at the date of the merger, and that it should be complete in all respects, including the interest (and Government contributions, if any), creditable to various Provident Fund Accounts—in detail (*i.e.*, for each subscriber) as well as for the funds as a whole.

**(5) Departmental and other Deposits (Item 7 of Section A of Statement III)**

(a) *Military Pedhi.*—This is a small loan bank of military personnel. This must be taken over by the Central Government.

(b) *Railways*
(c) *Broadcasting*
(d) *Telephones*

} The deposit balances of these three departments must be wholly taken over by the Central Government.

(e) *"Central Revenues" in suspense deposits.*—This represents the collections made by the State by way of "Central" excise Duties (on Tobacco, Matches and Vegetable products), but kept in deposit, pending division with the Central Government under the "pooling" arrangements now in force. Strictly speaking, the division of this between the two successor Governments must be made in accordance with what *would* have been the position had the division been *determined and finalised*, on the date of the merger itself, in accordance with the "pooling" formulae between the Government of India and the Government of *Baroda*. The share payable to the Central Government must, therefore, go *wholly* to them and the balance, which would have gone wholly to the Baroda Government must remain over as part of the *current assets* of the State to be divided (in the event of there being a surplus of current assets over current liabilities) between the two successor Governments as part of such surplus, on the lines indicated in sub-paras. 28(ii) and (iii) below.

A contrary set of adjustments would be necessary in regard to Customs Revenue which, though divisible through a "pooling" arrangement with the Government of India is in fact credited by the State direct to its revenues; so that here, Baroda's share has already been received by it, credited to revenue and included in assets, whereas the amount payable to the Government of India remains *wholly* as an outstanding liability *not* shown in the State's accounts at the account-closing date but treated as payable out of next year's revenues.

A broad consideration of the figures relating to Central Excise and Customs Duties indicates however that the *net* amount likely to fall to the share of Bombay, after making appropriate adjustments and calculations as above, would be comparatively trifling. Accordingly, we recommend that the *entire* joint "Central" revenues held in deposit, should go wholly to the Central Government, and no further adjustments need be made. We may mention, however, that there would, of course, be no objection, in principle, to dealing with the matter on the more meticulous lines already indicated, if that should be preferred.

**(6) Remittance Account (Item 9 of Section A of Statement III)**

It is obviously impossible to allocate this balance until "cleared" by entries to appropriate accounts on the receipt of advices from the remitting departments. When so "cleared", the sorting between "Provincial" and "Central" categories will be automatically achieved on a functional basis. For the present, however, it is assumed that the entire balance is "Provincial".

**(7) Suspense (Item 10 of Section A of Statement III)**

We have the same comments to offer here as under (6) above.

**(8) Army (Military) Funds (Item 10 of Section B of Statement III)**

These are partly Regimental Funds, and partly Reserve Funds for Military Establishments, Training, Building, Installation and Equipment. These are clearly "Central" functions; and the funds must, therefore, be taken over by the Central Government. We were given to understand, however, that during the current year substantial sums have been re-appropriated for the benefit of current revenues of the State. In our opinion, such re-appropriation to the extent that it represents a re-appropriation of funds intended for *non*-I. S. F. units or for raising and training new units, need not be objected to.

**(9) Railway Betterments Fund (Item 11 of Section B of Statement III)**

This is clearly a "Central" function and the Fund must, therefore, be taken over by the Central Government. The present Baroda administration is anxious not only that these funds should be expended, for the purposes intended, exclusively on the Baroda State Railway system, but also that as corresponding liquid assets are readily available, such expenditure should not (subject to the usual canons of financial propriety), be unduly delayed. Their concern in this respect is both understandable and proper; we, therefore, recommend that the Central Government should deal with this Fund in the sense desired by the present Baroda Administration.

**(10) Railway Capital Reserve Fund (Item 3 of Section C of Statement III)**

This is in addition to the Railway Depreciation Fund; since "Railways" is clearly a "Central" function, the Reserve Fund must be wholly taken over by the Central Government. As in the case of the Railway "Betterments Fund" referred to above, the present Baroda administration is naturally anxious, —and we support them in that respect—that this Fund should be utilised for Capital Improvements, Extension and Development of the Baroda Railway system *alone*, and that, subject to considerations of financial propriety, such expenditure should not be unduly delayed.

*One important matter* to which we must especially invite attention in this connection is that for a number of years up to 1947-48, the State's policy, as regards the "appropriation" of net Railway revenues (after charging depreciation), was to take to general revenues an amount equal to 4 per cent. of the capital at charge and to credit the balance to the Railway Capital Reserve Account. During the current year (in December 1948), however, it was decided to change this policy. The details of the new formula, as also its effect on the current year's contribution by the Railways to the general revenues of the State, are for our present purposes irrelevant. But it has been sought to give *retrospective* effect to the new formulae by directing that any short-contributions found (according to the new formula) to have been made in the past (from 1942-43 onwards) should be made good in the current year by a re-appropriation from the Railway *Capital* Reserve; (the amount involved is Rs. 58.30 lakhs). We were inclined to regard this procedure as altogether irregular: but it was pointed out to us that—

(i) for some years the Railways had not contributed to general revenues even according to the old formula;

(ii) during the years in which that formula had effectively operated the Railways had contributed far less to general revenues and far more to the Reserves than they should or need have done in accordance with the principles followed by the Government of India in regard to their Railway earnings; and

(iii) during 1948-49 the need for a special contribution to general revenues,—even from the Railway Capital Reserves, if need be,—was most urgent in view of the prevailing famine and foodgrains scarcity.

We have examined these arguments, particularly that set out in (i) above, sympathetically; and we consider that, in the circumstances, the re-appropriation need not be objected to. We recommend accordingly.

**(11) Post-War Reconstruction Fund (Item 1 of Section E of Statement III)**

This has been *provisionally* classified in Statement III as "provincial".

On 31st July 1948 this was the only Reserve Fund with *non-specific* objectives. It has been built up out of revenue surpluses during war years. The expenditure already incurred out of it (up to 31st July 1948) was as follows:—

*On "Central" Capital Assets.*

| | Rs. (in Lakhs) |
|---|---|
| Telephones . . . | 0·51 |

*On "Provincial" Capital Assets.*

| | |
|---|---|
| Electric Schemes . . . | 0·05 |
| Okha Port . . . | 26·33 |
| TOTAL . | 26·89 |

The balance of the Fund on 31st July 1948 was, therefore, Rs. (216·61—26·89) lakhs = Rs. 189·72 lakhs, represented by (unspecified) assets included among current "banking" assets.

We have anxiously considered whether the whole of this should go to the Bombay Government for expenditure in the "provincial" field in Baroda territories, or whether any part should equitably be taken by the Central

Government for expenditure on "Central" objectives *in those territories.* It is not easy to decide this issue on any *a priori* grounds. For while it is true, that having been built up out of the conjoint "central" and "provincial" revenues of Baroda in the past, the Central Government can appropriately insist upon taking over a not unsubstantial part of this fund, on the basis perhaps of the *pro-rata* "central" and "provincial" revenues of years during which the Fund was accumulated, one must also have regard to the "needs" in the two fields of expenditure in Baroda, which are now to be separated. On that basis, it must be conceded that the Railway and Defence Capital requirements of the future have been fairly adequately provided for by the separate Capital Reserves existing specifically for those purposes and that only the Telephone and "National Highways" requirements of the future remain principally to be considered so far as "Central" functions in Baroda territories are concerned.

The "upper" limit to the Central Government's claim is thus furnished by the "*pro-rata* revenue" test, according to which the maximum they could claim would be almost exactly one-third of the gross amount at the credit of the fund *less* the expenditure already incurred on telephones. On that basis, and by reference to the position as at 31st July 1948 the Centre should get one-third of Rs. 216·61 lakhs, *less* Rs. 0·51 lakhs, *i.e.* Rs. 71·70 lakhs of this Fund. On the other hand, the "lower" limit is furnished, in general terms, by the "needs" in the Central field, as indicated above. And it is important in this connection to keep two circumstances in mind—

first, that the Trunk Telephone system in Baroda is still very much incomplete; and

second, that there is only a very small mileage of trunk roads in the state which is *now* eligible for classification as "National Highways" and that an important road which will eventually qualify as "National Highway" is now at the "alignment" stage and will require considerable expenditure.

These needs are urgent, and their satisfaction will be both expensive and for the lasting benefit of the people of the State. We would, accordingly, recommend that the portion of the fund which should go to the Central Government should be 12 per cent. of the gross amount at credit, *less* the expenditure already incurred on "Central" objectives. The result (at 31st July 1948) would be—

| | Rs. (in Lakhs) |
|---|---|
| One-tenth of Rs. 216·61 lakhs. . . . | 21·66 |
| *Less* Expenditure on telephones. . . | 0·51 |
| | 21·15 |

The balance of the *net* amount at credit of the fund, *i.e.*, (Rs. 189·72—21·15) lakhs = Rs. 168·57 lakhs should go to the Bombay Government.

27. The result of the foregoing discussion and recommendations may be summarised in the following form showing the proposed allocation of current and funded liabilities shown in Statement III, between the two Governments :—

| *Section.* | Particulars. | "Provincial" (Rs. in Lakhs) | "Central" (Rs. in Lakhs) | "Total" (Rs. in Lakhs) |
|---|---|---|---|---|
| A. | Banking or Cur ent Liabilities (subject to re-allocation of "other" Provident Funds) . | 732·14 | 393·77 | 1125·91 |
| B. | Specific "Functional" Funds. | 39·32 | 60 10 | 99·42 |
| C. | Specific Capital Reserve . | 24·73 | 177·54 | 202·27 |
| D. | Land Revenue Equalisation Fund | 107·03 | ... | 107·03 |
| E. | Post-War Reconstruction Fund | 194·95 | 21·66 | 216·61 |
| | *Less* Amount already spent thereout-of on Productive Capital Assets | —26·38 | —0·51 | —26·89 |
| | TOTAL . | 1071·79 | 652·56 | 1724·35 |

NOTE.—The above summary does not include the liability on account of Depreciation Funds which have *not been specifically invested* (Rs. 27·93 lakhs "Provincial" and Rs. 54·67 lakhs "Central"—Total Rs. 82·60 lakhs); as already stated, these amounts should be taken in reduction of the book-values of the assets concerned, except to the extent that investments in the shape of "current" or liquid assets are actually available *after* providing for *all* current liabilities and Funded obligations.

28. Turning now to the current or liquid Assets of the State, Statement V attached hereto shows what these assets were as at 31st July 1948. [Items 13 and 14 in that Statement are, for the present, assumed to be of "provincial" character for the same reasons as those stated against the corresponding liability items of Statement III,—*vide* sub-paras. (6) and (7) of para. 26.]

The *primary* basis for apportioning and allocating these current assets should, in our opinion, be that each successor Government must be given sufficient assets to meet the *liabilities* or Funds allocated to it—*vide* paras. 22, 26 and 27 *supra*, and that within this over-all primary limit, each Government must, so far as possible, first take up those specific assets which are appropriate to the liabilities allocated to it and/or to its functions. Finally, any surplus of current assets over liabilities must first be allocated against Depreciation Funds (*vide* note under para. 27) and the balance, if any, divided between the two Governments on some equitable basis. (The *income* arising from 'current' assets must be classified as 'Central' or 'Provincial' according to the allocation of the assets themselves as between the two Governments).

(i) The result of this recommendation can be readily appreciated by a reference to the "remarks" column in Statement IV. It shows that items ., 8 and 12 (a) totalling Rs. 47·61 lakhs must be taken up by the Central

Government, and that items 1, 7, 9, 10, 11, 12(b), 13 and 14 totalling Rs. 737·80 lakhs, must be taken up by the Provincial Government. The position will then be as follows:—

| | "Provincial" (Rs. in Lakhs) | "Central" (Rs. in Lakhs) | "Total" (Rs. in Lakhs |
|---|---|---|---|
| Allocation of Liabilities and Funds (paragraph 27 *supra*) | 1071·79 | 652·56 | 1724·35 |
| Allocation of Current Assets as above . . | 737·80 | 47·61 | 785·41 |
| Balance (uncovered Liabilities) | 333·99 | 604·95 | 938·94 |

(ii) The balance of available current assets would then be items 2, 3, 5 and 6 of Statement IV namely,

| | Rs. (Lakhs). |
|---|---|
| Government Securities . . . . | 63·826 |
| Bonus and Debentures . . . . | 18 00 |
| Industrial & Commercial Sahres . . | 248.61 |
| Fixed Deposits . . . . . | 513·64 |
| TOTAL . | 1418·51 |

This amount is sufficient to provide:—

Firstly, assets to the *full* extent of the uncovered balance of the liabilities (Rs. 938·94 lakhs) assigned to the two Governments—Sub-para (i) above;

Secondly, assets to the *full* extent of the Depreciation Funds (Rs. 82.60 lakhs), which would otherwise have to be taken in deduction of the book-value of the assets concerned (*vide* para. 24 and Note under paragraph 27).

There will then remain an over-all net surplus of assets over liabilities (Rs. 396·97) lakhs) to be divided between the two Governments on some equitable basis. Theoretically there are two alternative ways of sharing this over-all surplus:—

*either* in proportion to the "Central" and "Provincial" revenues of the State, from which, obviously, this surplus was built up.

*or* in proportion to the "Central" and "Provincial" *expenditure*, upon which this surplus would have been spent by the State.

The former alternative favours the Central Government: this is particularly so in this case, because a glance at the relative amounts already spent on "central" and "provincial" productive *capital* assets (paragraphs 24 and 2 *supra*) will show that the expenditure in the past on assets of the former category has been relatively heavy. For these reasons, the expenditure-basis would, we consider, be more equitable. We recommend accordingly. The result will be that the Centre will be entitled to only *one-tenth* of the surplus assets.

(iii) The final division of the residual assets, enumerated at the commencement of sub-para. (ii) above, which we recommend, in accordance with the principles there enunciated, is accordingly as follows:—

| | Against Uncovered Liabilities. | Against Depreciation Funds. | Out of net over-all surplus. | TOTAL |
|---|---|---|---|---|
| | Rs. in lakhs | Rs. in lakhs | Rs. in lakhs | Rs. in lakhs |
| To the Central Govt. | 604·95 | 54·67 | 39·70 | 699·32(x) |
| To the "Provincial" Govt. | 333·99 | 27·93 | 357·27 | 719·19(y) |
| TOTAL | 938·94 | 82·60 | 396·97 | 1418·51(z) |

We further recommend that *each component item* of the liquid assets as at (z) above should be divided between the Central Government and the Provincial Government, so far as possible, in the ratio (x): (y).

29. There remains the question of indicating the *modus operandi* in the event of there being an excess of liabilities over assets on the date of the merger.

In such a contingency, there can, of course, be no question of providing any liquid assets against Depreciation Funds. These should, in such circumstances, be taken in reduction of the book value of the assets concerned.

As regards the remaining liabilities and Funds, a careful consideration of the summary, set out in paragraph 27 above, itself furnishes the answer. Those liabilities have been arranged in descending order of priority; and of them those grouped under Sections A and B are either "outside" or earmarked liabilities which *must* be met, whereas those under Sections C to E are in the nature of "surpluses" credited to Funds or Reserves.

It follows that any excess of liabilities, as there grouped, over current assets must *first* be utilised to "extinguish" the funds grouped under Section E, next the Reserves under Section D, and finally the Reserves under Section C. In so extinguishing these Funds and Reserves, the "Central" portion of each Fund or Reserve may, as a matter of justifiable concession, be extinguished *before* the "Provincial" portion. We recommend accordingly.

## VI.—SUMMARY OF RECOMMENDATIONS

30. **Our principal conclusions and recommendations are summarised below:—**

### (1) Terms of Reference

In the case of Baroda, we are in effect concerned only with terms of reference (4) and (6), *viz.*, the integration of the Federal Finances of Baroda with the finances of the Central Government, and the consequential financial adjustments and relations which should subsist between the Government of Bombay on the one hand and the Government of India on the other, in respect of the merged territory. (Para. 5).

### (2) Constitutional Position

The Constitutional position is that after the necessary Order under Section 290-A of the Government of India Act, 1935, is issued by the Governor-General in respect of Baroda, the Bombay Government and Legislature will exercise in the area newly added to that Province *only* those powers they are now exercising in the Bombay Province under the Act; while, in the same area, the Dominion Government and Legislature will exercise powers in respect of "Dominion" subjects precisely as they are now doing in Bombay Province as at present constituted. (Para. 7).

### (3) Consequential Basis of Approach

Assets, liabilities, functions and sources of revenue of the former Baroda Government which are classifiable as "Central" will accordingly vest in the Dominion Government, while "Provincial" assets, liabilities, functions and sources of revenue will vest in the Bombay Government. Any special arrangements at present subsisting between the Government of India and the Baroda State in respect of "Central" functions and revenues will terminate. (Para. 8).

### (4) Allocation of Departments, Assets, Liabilities, etc.

As from the date of the merger the Central Government will take over all "Central" sources of revenue and the administration of all Departments concerned with "Central" functions, together with all connected unproductive capital assets, current liabilities, outstandings, refunds etc. (Para. 10).

Similarly, all specific productive capital assets connected with "Central" functions (*e.g.*, railways and telephones), together with any debt, cash balances, liabilities and outstandings specifically relating to them, should also be taken over by the Government of India. (Para. 11).

"*Current*" liabilities and Funded obligations of the State must be allocated between the Central Government and the Bombay Government on a "functional" basis, coupled with the principle of public convenience. The allocation of such liabilities should be accompanied, so far as may be possible, by an equivalent allocation of current (liquid) assets. There will then remain a *net* surplus of liquid assets or of *current* liabilities, to be apportioned between the two successor Governments. (Paras. 12-13).

**(5) "Central" Revenue**

The average annual revenue realised by Baroda from "Central" sources was Rs. 186 lakhs, on the basis of the average of the last three completed accounting years of the State. (Para. 15).

**(6) "Central" Expenditure**

The expenditure classifiable as "Central" incurred by Baroda during the last completed financial year (1947-48) amounted to Rs. 60 lakhs. (Para. 17).

**(7) Financial (Revenue) adjustments required between the Central Government and the Government of Bombay**

We recommend that the net revenue-gap in the finances of Baroda (*viz.*, Rs. 126 lakhs per annum), arising from the loss of "Central" revenues and taxes, as reduced by the savings in respect of "Central" expenditure, after Federal Financial Integration, should be made good as follows:—

(a) by the Bombay Government assuming responsibility, *with effect from* 1950-51, for Rs. 50 lakhs per annum, *i.e.*, 40 per cent. of Rs. 126 lakhs;

(b) by the Central Government assuming responsibility for, and guaranteeing to pay to the Bombay Government as from the date of the merger, a sum of Rs. 126 lakhs per annum up to 31st March 1950, and thereafter a sum of Rs. 76 lakhs per annum for a period of 10 years, in the shape of—

(i) the share of divisible income-tax and other divisible federal taxes, if any, which will accrue to the Bombay Government on account of the addition of the Baroda territory to the Province; and

(ii) and *ad hoc* revenue subsidy to the extent to which (i) should fall short of the guaranteed amount.

In our considered opinion, the Bombay Government should have no difficulty in bearing a share of the net revenue-gap as suggested above. (Para. 20).

**(8) Specific matters connected with Revenue and Expenditure**

We have made several detailed recommendations concerning certain specific matters relating to items of "Central" revenues and expenditure, and concerning the taking over of the respective departments and staff by the Government of India; those relating to Income Tax are of special importance. (Paras. 16 and 18).

**(9) Ruler's Immunities and Privy Purse**

Steps should be taken to secure, by necessary executive orders, statutory notifications and/or amendments (as may be appropriate), the continuance of the personal immunities of the Ruler in the matter of taxation etc.

With regard to the Privy Purse, our proposals have been evolved on the basis that it will not be a "Central" liability. If, however, the Privy Purse should, for any reason, be made payable out of Central revenues. the net "Central" revenue-gap of Baroda will be reduced by that amount; we have suggested consequential changes in the amount thereof to be borne by Bombay and the amount to be guaranteed by the Central Government, respectively, (Para. 21).

**(10) Assets and Liabilities**

(i) "Unproductive" specific Capital assets pertaining to "Central" functions will be taken over by the Government of India without valuation; the rest of such assets will go to the Government of Bombay.

(ii) "Productive" capital assets of a "Central" nature will similarly be taken over by the Government of India; their book value, *less* specific debt attached to the assets, amounted to Rs. 624·17 lakhs on 31st July 1948.

"Productive" capital assets of a "Provincial" nature will vest in Bombay Government; these were valued in the books at Rs. 192·33 lakhs on the same date. (Paras. 24 and 25).

(iii) We have made several detailed recommendations regarding the allocation of certain specific items of current or banking liabilities to the Central Government or the Bombay Government and also about the apportionment of certain Funds and Reserves. [Paras. 26(1) to (8)].

(iv) We have recommended that the Railway Betterments Fund and the Railway Capital Reserve Fund should be utilised for the purposes of the Baroda State Railway system only and without undue delay. [Para. 26(9) and (10)].

(v) We have recommended that the portion of the Post-war Reconstruction Fund which should accrue to the Centre should be 10 per cent. of the gross amount at credit *less* expenditure already incurred on "Central" objectives: the amount so allocated to the Centre should be ear-marked for expenditure upon "Central" objectives in Baroda territories. [Para. 26(11)].

(vi) We have drawn up a scheme under which the Bombay Government and the Government of India will each receive sufficient current or liquid assets to meet the liabilities or Funds (including Depreciation Funds) assigned to them. We have further recommended that the Central Government should receive one-tenth of the over-all surplus of current assets over liabilities; the amount so allocated to the Centre should be ear-marked for expenditure upon "Central" objectives in Baroda territories. (Para. 28).

(vii) Should there be a surplus of current liabilities over liquid assets on the actual date of the merger, we have indicated in what respects, the plan suggested will have to be modified. (Para. 29).

31. In view of the complexities and importance of the issues arising out of the merger, and the large amount of detail to be attended to purely from the accountancy and financial points of view, it would be desirable, if possible, to invite the Auditor-General of India to appoint an officer on special duty to assist in the implementation of the decisions which may be taken on the various suggestions and recommendations made by us. The officer should be required to work locally in the office of the present Accountant-General, Baroda, for about six months after the merger but under the control and directions of the Accountant-General, Bombay. It will be a great advantage if such an officer could be appointed as soon as orders of Government are passed on this report. The Officer will have to verify carefully, the accuracy of the figures finally to be adopted in the computations of Assets and Liabilities as on the date of the merger; and we ourselves would, of course, be glad to offer such assistance as may be necessary, in clarifying any points of principle arising out of the report.

32. This report is not signed by Mr. Patil, as he is out of India at present. But all the important issues have been discussed with him and the conclusions reached have his full concurrence.

V. T. KRISHNAMACHARI,

(*Chairman*).

N. DANDEKER.

(*Member*).

G. SWAMINATHAN,

(*Secretary*).

*New Delhi, the 1st June*, 1949.

# ANNEXURES

# BARODA

## STATEMENT I.

PARTICULARS OF "CENTRAL" REVENUES WHICH WILL MERGE WITH THE REVENUES OF THE CENTRAL GOVERNMENT UPON "MERGER" OF THE STATE INTO BOMBAY PROVINCE

| S. No. | Particulars | Actual Receipts 1945-46 | Actual Receipts 1946-47 | Actual Receipts 1947-48 | Average for three years | Reference to Foot-notes |
|---|---|---|---|---|---|---|
| | | Rs. (Lakhs) | Rs. (Lakhs) | Rs. (Lakhs) | Rs. (Lakhs) | |
| 1 | Customs Duties on *Foreign* Trade :— | | | | | |
| | Import Duties . | 31·98 | 31·42 | 31·78 | 31·73 | Note (1) |
| | Export Duties . | 0·26 | 0·18 | 0·39 | 0·28 | .. |
| 2 | Corporation Tax (other than Agricultural Corporation Tax). | 6·48 | 4·10 | 2·60 | 4·39 | Note (2) |
| 3 | Opium Receipts (Recovery of cost of cultivation and manufacture). | 4·35 | 1·21 | 1·50 | 2·35 | Note (3) |
| 4 | Income-Tax and Super-Tax (other than Corporation Tax and Agricultural Income-Tax). | 73·60 | 94·75 | 119·60 | 95·98 | Note (4) |
| 5 | "Central" Excise Duties. | 23·21 | 34·68 | 20·74 | 26·21 | Note (5) |
| 6 | Salt . . . . | | .. | .. | .. | Note (6) |
| 7 | Customs Duties on *Internal* Trade. | .. | .. | .. | .. | Note (7) |
| 8 | Railways . . | 23·31 | 23·52 | 21·72 | 22·85 (net) | Note (8) |
| 9 | Postal "Immunity" . | 1·25 | 1·25 | 1·25 | 1·25 (net) | Note (9) |
| 10 | Telephones . . | 0·55 | 0·54 | 0·94 | 0·68 (net) | .. |
| 11 | Miscelluaneous (Interest on "Central" investments.) | .. | .. | .. | .. | Note (10) |
| | TOTAL . | 164·99 | 191·65 | 200·52 | 185·72 | |

## Baroda

### NOTES RELATING TO STATEMENT I

(1) This represents Baroda's share of the total Customs Revenue "appropriate" to each year, according to the sharing arrangements with the Government of India.

(2) As Corporation Tax is not separately levied in Baroda 2/3rds of Super-Tax is taken under this head.

(3) This is an estimate of receipts from cultivation and manufacture of opium. The entire opium cultivated and manufactured in the State is internally consumed. In accordance with the practice of the Government of India, receipts from "cultivation and manufacture" of opium are equated to the estimated departmental *cost* for cultivation and manufacture of opium. The balance of the income under the head 'Opium' is excluded as "Provincial" revenue which will continue to accrue to the benefit of the Provincial Government.

(4) These are Income-Tax receipts *plus* 1/3rd Super-Tax receipts *less* proportionate Refunds relative to Income Tax as distinct from Sales-Tax. There is no Agricultural Income-Tax levied in the State.

(5) "Appropriate" figures for each year are taken for "pooled" items (actuals for 1945-46 and estimates for the other two years).

(6) Refunds have been granted to Baroda by the Government of India for surrendering their rights for manufacturing Salt and levying duties on it. These are, however, omitted as Salt Revenue has entirely ceased from 1947-48 and is *not*, therefore, a loss arising from the merger.

(7) The "protective" Internal Customs Duties are already being abolished owing to :—

(*i*) the expenditure being much more than the revenues.

(*ii*) no protective measures of this kind being necessary for Port Okha, and

(*iii*) the changed political circumstances through the formation of Saurashtra Union.

The amounts are, therefore, omitted being loss *not* resulting from merger.

(8) These are the net contributions to general revenues in the form of 4% interest on the capital advanced by the State, in accordance with the normal practice of the State in the years in question.

(9) This represents cost of Service Stamps supplied free by the Government of India to the Baroda State.

Free carriage of State Mails within the State, which used to benefit the State by Rs. 0·25 lakhs or so, has already been stopped ; it is *not*, therefore, a loss resulting from merger.

(10) As "Federal" funds are not separately invested, no figures can be worked out. The amount to be finally shown here will be the interest *receivable* (in future) by the Government of India upon current assets and investments allocated to them, *less* the interest *payable* by them upon current liabilities and funds allocated to them upon merger.

# BARODA

## STATEMENT II

PARTICULARS OF "CENTRAL" EXPENDITURE WHICH WILL MERGE WITH THE EXPENDITURE OF THE CENTRAL GOVERNMENT UPON "MERGER" OF THE STATE

| S. No. | Particulars | Amount (Rs. in lakhs) 1947-48 | Reference to Foot notes |
|---|---|---|---|
| 1. | Cost of collection of Customs Duties on Foreign Trade | 0·25 | Note (1) |
| 2. | Cost of collection of Central Excise Duties | .. | Note (2) |
| 2A | Cultivation and Manufacture of Opium | 1·50 | Note (2A) |
| 3. | Cost of collection of Income-Tax | 2·69 | Note (3) |
| 4. | National Highways | 1·98 | Note (4) |
| 5. | Defence (excluding cost of non-I. S. F. Units) | 45·00 | Note (5) |
| 6. | Aviation | 0·30 | Note (6) |
| 7. | Broadcasting | 2·09 | Note (7) |
| 8. | Meteorology | 0·07 | .. |
| 9. | Archaeology | 0·35 | .. |
| 10. | Geology (Survey) | .. | .. |
| 11. | (a) Patents, Copyrights, Trade-Marks | 0·07 | .. |
| | (b) Joint Stock Companies | —0·10 | Note (8) |
| 12. | *Ad hoc* (Federal Civil Works) etc. (other than Military) | 0·25 | Note (9) |
| 13. | Pensions—of Military and "Federal" Personnel (unless already included under preceding items). | 1·35<br>0·40 | Note (10)<br>Note (10A) |
| 14. | Accounts and Audit | 3·66 | Note (11) |
| | TOTAL | 59·86 | Note (12) |

### NOTES RELATING TO STATEMENT II

(1) This represents the expenditure on collection of Customs Duties at Ports other than Port Okha. Expenditure for the latter is deducted from Customs revenues as shown in Statement I.

(2) The expenditure is deducted from the receipts from Central Excise as shown in Statement I.

(2A) Estimated at 70% of the total cost of "opium" department.

(3) 70 per cent of the Establishment cost of the combined Sales and Income-Tax Department has been taken in arriving at this figure.

(4) Represents Estimated expenditure on maintenance of "National Highway" (66 miles) at Rs. 3,000 per mile per annum.

(5) The expenditure on non-I. S. F. Units has been excluded at 40% of the total expenditure, *after* first deducting therefrom the "provision" for raising and training new units. Sundry receipts from Defence are deducted in proportion of 60% of the total receipts. Similarly charges for maintenance of buildings, and dearness and other allowances, charged to the Civil Budget, have been *added* in proportion to the expenditure on I. S. F. and non-I. S. F. Personnel.

(6) This is the maintenance charge for Baroda Aerodrome.

(7) The Baroda Broadcasting Station was sold to the Government of India on the 16th December 1948.

(8) (*a*) The figures for Patents and Trade-Marks are "*less* receipts". The Establishment charges are being incurred from 1st January 1947.

(*b*) The receipts from Joint Stock Companies exceed the expenditure. The net figure of —0·10 is arrived at as below :—

| | Rs. |
|---|---|
| Expenditure during 1947-48 . . | 15,729 |
| *Deduct*—Receipts during 1947-48 . | 25,953 |
| | —10,224 or say Rs.—0·10 lakhs. |

(9) This represents the cost of compensation for land in Aerodrome works paid by Baroda.

(10) Pensions of I.S.F. Personnel are grouped here on an approximate basis. A sum of Rs. 0·10 lakhs is added each year to show the additional expenditure on new pensioners. The actual amounts spent on pensions in the Military Department in lakhs of Rupees (including I.S.F.) were :—

| 1945-46 | 1946-47 | 1947-48 |
|---|---|---|
| Rs. | Rs. | Rs. |
| 1·77 | 2·01 | 2·22 |

(10A) Pensions of other "Central" personnel estimated at Rs. 0·40 lakhs.

(11) The distribution of Audit charges is made on the following computation :—

| | | Rs. (Lakhs) |
|---|---|---|
| Total Accounts and Audit Expenditure . . | | 3·26 |
| *Add* Expenditure on dearness allowance and house-rent, etc. . . . . . . . . | | 1·21 |
| | | 4·47 |
| *Less* Non-I.S.F. Military Audit . . | 0·07 | |
| Investment Mahal (Provincial) . . | ·13 | |
| Chitnishi Branch including supervision of Accountant-General and his principal Assistants (50% Provincial) . | ·25 | |
| Compilation and Budget (Provincial) . | ·24 | |
| Savings Bank (Provincial) . . . | ·08 | |
| Contingency and Dead Stock . . | ·04 | |
| | | 0·81 |
| Balance "Central" . . . . | | 3·66 |

(12) Expenditure in respect of dearness allowance, house-rent allowance and other allowances is *included* under each Department.

# BARODA

## STATEMENT III

### ANALYSIS OF LIABILITIES AS AT 31ST JULY, 1948.

| S. No. | Particulars | "Provincial" | "Central" | Total | Reference to Foot-notes |
|---|---|---|---|---|---|
| | | Rs. (Lakhs) | Rs. (Lakhs) | Rs. (Lakhs) | |
| | *(A) Banking or current liabilities.* | | | | |
| 1. | State (Treasury) Savings Bank Deposits . . . . | 79·62 | .. | 79·62 | .. |
| 2. | Local Cess . . . . | 23·85 | .. | 23·85 | |
| 3. | State Life Insurance Fund (not Postal). | 7·44 | .. | 7·44 | .. |
| 4. | Accident Insurance Fund (Museum and Port). | 0·29 | .. | 0·29 | .. |
| 5. | Provident Funds : | | | | |
| | (a) Railways, Broadcasting and Telephones. | .. | 24·26 | 26·22 | Note (1) |
| | (b) Other Departments . | 1·96 | .. | | |
| 6. | Probationary Fund (?) . | 0·31 | .. | 0·31 | Note (2) |
| 7. | Departmental and other Deposits— | | | | |
| | (a) Military (Pedhi) . . | .. | 3·36 | 484·53 | Note (3) |
| | (b) Railways . . .. | .. | 68·77 | | |
| | (c) Broadcasting . . . | .. | 0·52 | | |
| | (d) Telephones . . | .. | 0·89 | | |
| | (e) "Central" Revenues (Tobacco, Matches and Vegetable Products Excise Duties). | .. | 295·97 | | |
| | (f) Others ("Provincial") . | 115·02 | .. | | |
| 8. | Endowments and Memorial Funds | 23·38 | .. | 23·38 | .. |
| 9. | "Remittance" Account Balance (?) | 416·16 | .. | 416·16 | .. |
| 10. | Suspense (?) . . . | 18·42 | .. | 18·42 | .. |
| 11. | Village Uplift Trust Funds . | 23·03 | .. | 23·03 | . |
| 12. | Shanta Devi Trust Fund (and Interest) | 22·66 | .. | 22·66 | .. |
| | TOTAL OF (A) . | 732·14 | 393·77 | 1125·91 | .. |

# BARODA

## STATEMENT III—*contd.*

### ANALYSIS OF LIABILITIES AS AT 31ST JULY, 1948—*contd.*

| S. No. | Particulars | "Provincial" | "Central" | Total | Reference to Foot-notes |
|---|---|---|---|---|---|
| | (*B*) *Specific "Functional" Funds.* | Rs. (Lakhs) | Rs. (Lakhs) | Rs. (Lakhs) | |
| 1. | Child Marriage Insurance Fund. | 1·11 | .. | 1·11 | .. |
| 2. | City Improvement Fund . | 0·27 | .. | 0·27 | .. |
| 3. | Text Books Fund . . | 0·37 | .. | 0·37 | .. |
| 4. | H. H. "Coronation Book" Series Fund. | 0·21 | .. | 0·21 | .. |
| 5. | Secondary Education (Laboratories, Buildings and Equipment) Fund. | 4·75 | .. | 4·75 | .. |
| 6. | Attached Area Development Fund. | 10·16 | .. | 10·16 | .. |
| 7. | Miscellaneous Funds (Mal Vera, Shiledari and attached area). | 7·55 | .. | 7·55 | .. |
| 8. | Distress Relief Fund . . | 4·93 | .. | 4·93 | .. |
| 9. | Police, Jail, and Political Funds. | 9·97 | .. | 9·97 | .. |
| 10. | Army (Military) Funds . | .. | 49·99 | 49·99 | .. |
| 11. | Railway Betterments Funds | .. | 8·82 | 8·82 | .. |
| 12. | Cotton Cloth and Yarn Cess Fund. | .. | 1·29 | 1·29 | (Note (4) |
| | TOTAL of (*B*) . | 39·32 | 60·10 | 99·42 | |
| | (*C*) *Specific Capital Reserve Funds.* | | | | |
| 1. | Local Boards Reserve Fund. | 1·54 | .. | 1·54 | .. |
| 2. | Electric Schemes Reserve Fund | 23·19 | .. | 23·19 | .. |
| 3. | Railway Reserve Fund . | .. | 170·40 | 170·40 | .. |
| 4. | Telephones Reserve Fund . | .. | 7·14 | 7·14 | .. |
| | TOTAL of (*C*) . . | 24·73 | 177·54 | 202·27 | |
| | (*D*) *Specific Revenue Reserves* | | | | |
| 1. | Land Revenue Equalisation Fund. | 107·03 | .. | 107·03 | .. |
| | (*E*) *Non-Specific Development Funds.* | | | | |
| 1. | Post-war Reconstruction Fund | 216·61(?) | .. | 216·61 | Note (5) |
| | GRAND TOTAL (*A* TO *E*) | 1119·83 | 631·41 | 1751·24 | Note (6) |

## BARODA

### NOTES RELATING TO STATEMENT III

(1) So much of this as relates to personnel who may be transferred to the Central Government will have to be taken over by that Government.

(2) The nature of this item is not clear ; it is assumed to relate to "Provincial" functions.

(3) Represents undivided collections of " Central " Excise Duties.

(4) It is assumed that this relates to " Central " functions.

(5) Provisionally assumed to be *wholly* " provincial ". Of this, a certain amount has been already spent on certain productive capital assets as follows :—

| | | |
|---|---|---|
| Telephones . . . . . | Rs. 0·51 lakhs | " Central " |
| Electric Schemes . . . . | Rs. 0·05 lakhs | " Provincial" |
| Okha Port . . . . . | Rs. 26·33 lakhs | " Provincial " |

(6) *General.*—The analysis in Statement III does not include Depreciation Funds which have *not been specifically invested* (Rs. 27·93 lakhs " Provincial " and Rs. 54·67 lakhs "Central "—Total Rs. 82·60 lakhs) ; these will be taken in reduction of the Book values of the assets concerned, *unless* investments or other liquid assets are actually available *after* providing for *all* current liabilities and funded obligations.

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## STATEMENT IV

### Analysis of Current or Liquid Assets as at 31st July 1948.

| S. No. | Particulars | Amount (Rs. in lakhs) | Remarks |
|---|---|---|---|
| 1. | Cash and Bank Balances . | 86·80 | To be taken up by the Provincial Government (for "Ways and Means" reasons). |
| 2. | Government Securities . | 638·26 | |
| 3. | Bonds and Debentures . | 18·00 | |
| 4. | Railway Shares . . | 7·68* | To be taken up by the Central Government. |
| 5. | Industrial and Commercial Shares | 248·61 | |
| 6. | Fixed Deposits in Banks . | 513·64 | |
| 7. | Cash in Police "Pedhi" . | 0·36 | To be taken up by the Provincial Government. |
| 8. | Cash in Military "Pedhi" . | 3·36 | To be taken up by the Central Government. |
| 9. | Insurance Fund Investments | 7·23 | To be taken up by the Provincial Government. |
| 10. | Trust Fund Investments . | 50·10 | Ditto. |
| 11. | Attached Area Fund Investments | 3·47 | Ditto. |
| 12. | Current Loans and Advances— | | |
| | (*a*) "Central" Departments *or* for "Central" Functions. | 36·57 | To be taken up by the Central Government. |
| | (*b*) Others—"Provincial" . | 219·53† | To be taken up by the Provincial Government. |
| 13. | Positive Balance on "Remittance" accounts. | 362·65 | Ditto. |
| 14. | Suspense (including 0·03 on "rounding"). | 7·66 | Ditto. |
| | Total . | 2203·92 | |

**Railway Shares*.—The amount shown against this item in the published Budget Memorandum of the State is Rs. 20·07 lakhs. This figure includes a sum of Rs. 12·39 lakhs which represents investment in a fixed *capital* asset, namely, the Tapti Valley Railway and has been classified accordingly, *vide* para. 24 of the Report. The amount to be taken as representing liquid or current assets, is therefore, only Rs. (20·07—12·39) lakhs or Rs. 7·68 lakhs.

†*Advances for purchase of food-grains* will be included in this. The amount of such advances will be represented *actually* by—

(*i*) Cost of stocks of food-grains on hand; and

(*ii*) Accumulated losses :

(*a*) State's share,

(*b*) Government of India's share (subsidy).

The figure for such "Advances" should be substituted, when preparing the Statement of Assets on the date of the 'merger' by (*i*) and (*ii*) (*b*) above ; and (*ii*) (as should be written off against the revenues of the State up to the date preceding the merger'.