Chapter VI

SPECIAL PROBLEMS OF WEST BENGAL: NEED FOR GOING BACK TO THE TRUE FEDERAL SPIRIT AND STRUCTURE

It was not surprising that during British colonial rule the conditions in England, and Europe largely influenced developments in India. Eventually, the transfer of power provided a fascinating study of political history but too many socio-economic facts were overlooked in the bargain. It has been pointed out that there is a "close family resemblance (of the Constitutional articles dealing with Centre-State relations) with the structure laid down in the Government of India Act, 1935. A colonial-imperial framework, set up in the wake of the Simon Commission's visit nearly fifty years ago, continues to govern the financial relationship between the Centre and the States. The concept of development for subjugated peoples was altogether alien to the British way of thinking. By the 1935 Act, the provinces were only offered some crumbs of local self-government, the rest of the political and financial powers were concentrated in Delhi where the Viceroy reigned. Perhaps because of a certain lacuna in realising the implications of the working of the development process in a federal polity at the time our Constitution was finalized, the financial provisions of the 1935 Act were adopted more or less in toto. Inevitably, anomalies of a grave nature have emerged over the years.

"The domain of public economic activities has increased and will continue to increase as long as development with social..."
justice remains the nation's goal and the Government — whether at the Centre or in the States — is enjoined to climb higher and higher the commanding reaches of the economy ..."  

Perhaps the politics of the situation was important because of the economic patterns that followed. India was the launching pad of the industrial revolution in Europe. 3 It furnished capital, raw material and an enormous captive market for Britain, the first industrial Power. But the capitalist penetration of India, far from leading to autonomous capitalistic development, led to de-industrialization, disinvestment and the strengthening of many archaic and repressive social relations, an era in which political independence did not lead to any fundamental (political) change. For the eastern region in general and West Bengal in particular, this has proved to be highly relevant. It has been noted 4 that the community which suffers under economic and social handicaps cannot advance if only the obvious legal or social discriminations against it are eliminated. It has actually to be accorded very strong preferences in opportunities for economic and social advancement in order to overcome the unfavourable initial conditions. The provinces or regions which are economically backward have to receive more than their 'fair share' of public investment in a free enterprise economy because there is a tendency for private investment to flow into more developed regions.
The differences in opportunity between different religious

groups economic classes and provinces in different stages of develop-
ment cannot be eliminated simply by talking about the need for
balanced development of all regions.

STATE'S PROBLEMS

To record some of the State's problems, before embarking on
a brief resume of what has been done within the constitutional
framework (which presents an excellent case of both the workings
and the shortcomings of the structure), there has been a progressive
decline in the State's fortunes from the time of independence.

It has been claimed that in spite of a generally peaceful
law and order situation till 1967 there was a concentrated Central
bid to divert funds from the State. The outlay of West Bengal's
First Plan (Rs. 154 crores) was as big as, if not somewhat bigger
than, Maharashtra's (the share of the then bilingual State of
Bombay comprising Maharashtra and Gujarat was Rs. 224 crores).
In the Second Plan West Bengal's investments came down to Rs. 145
crores whereas Maharashtra's increased to Rs. 207 crores and
Gujarat's to Rs. 143 crores. The Third Plan maintained this trend.
In the Fourth, West Bengal secured a pathetic Rs. 332 crores,
compared with Maharashtra's Rs. 898 crores and Gujarat's Rs. 454
crores. While Maharashtra and Gujarat together had a Plan outlay
which was about one-third bigger than West Bengal's it can be seen
how they eventually secured allocations four times bigger than West Bengal's.

Another factor, often minimized in discussions on purely socio-economic or historical terms of reference, is that of culture. It has been pointed out that political integration of a cultural region has posed certain problems. Bengal, which until 1874 included East and West Bengal, Orissa, Bihar and Assam, was the most populous region in South Asia. In 1947 it was reduced to one-seventh the size of greater Bengal. It was noted that the fact that Calcutta was the capital of British India until 1911 and that Bengalis held most of the privileged positions under imperialism explained historically the reason for "the 20th century image of crises, agitation and rebellion".

Though not bereft of some truth, this conclusion cannot be accepted wholly without reservation. Another interesting probe indicated that a conflict of issues between the Centre and the State included lack of consensus on matters like irrigation, land reform and party government. There was (and still exists) a clash of interests in national policy decisions and the reality of local conditions.

On the highest level of Centre-State interaction, as for example, with the appointment of the States Reorganization Committees in 1953, the national policy veered around a compromise between coercion and complete surrender to provincial sentiments. In the
clash between local cultivators and the Centre during the Damodar Valley Corporation controversy, it was argued that local improvement was more crucial than completing the second stage of the project. Even during one-party rule it was pointed out that "the West Bengal Congress Party has a reputation for being susceptible to pressures from people who are considered key men and for being capable of resisting ideological orientations, and it is on this basis that it has effectively organized the State."

Among most of the conclusions, several of which are open to dispute, possibly the most significant was that the older 'British-subject-overlord relationship' had been replaced by the 'Bengal-politician-Indian-national perspective'.

This again is probably an over-simplification but the conflict of interests raised by the D.V.C. episode could be re-examined in the cases of the agreement with Bangladesh on the sharing of Ganga waters, the States' reaction to the Central decision on free trade in foodgrain and several others. 10

A non-conformist Government has been returned to the State, possibly signifying a welcome return to reality in the sense that differences do exist in the set-ups at Delhi and Calcutta, but a re-examination of fundamental issues is likely to emphasize that the dissimilarities are more than purely ideological.
To revert to the issues just mentioned a brief resume will help reflect some of the typical dissensions which crop up.

**FARAKKA ACCORD**

On the Farakka issue\textsuperscript{11} there were several questions. Firstly, the amount of water allocated to flush out the Hooghly was not considered sufficient by the State Government; secondly, the State Assembly resolution was clearly by-passed without any attempt at 'co-operation' as the definition of federalism seems to indicate; and thirdly, almost characteristically, the solution probably lies on the Indian side of the border because the Ganga Waters are probably exploited along the upper reaches before it reaches the east.

Siltation of the Hooghly river bed is causing West Bengal concern because it jeopardizes the future of Calcutta Port. In the crucial ten-day 'lean period' it has been estimated that 40,000 cusecs would be required to flush the Hooghly. The Centre apparently went back on its word by allocating 20,000 cusecs after the Delhi Agreement with Bangladesh.

The State Assembly passed a resolution demanding the release of 40,000 cusecs during the lean period. The suggestion that the agreement be reviewed on an annual basis was also overlooked. The Centre seemed to emphasize that a State Assembly resolution did not merit consideration.
Thirdly, out of the Ganges' summer flow of 65,000 cusecs, 25,000 comprises 'regenerated discharge'. The upper Ganga Canal, the Lower Ganga Canal, the Dalmau, Bhoupi and Zamania pumped canals, Kanpur, Allahabad and Barauni and irrigation networks in Bihar and Uttar Pradesh use up much of the water. Nobody at the Delhi talks apparently could convincingly establish that West Bengal could manage with less water. Very obviously the Farakka accord was important for New Delhi. The State, arguably, might have struck a deal with the Centre. But the Chief Minister's comment ('We can neither secede nor can we go to war') clearly belied any such hope. The understanding was clearly made without the knowledge of the State leaders. This was obviously not a case of co-operative federalism at work.

On the question of return to the free market in foodgrain, the Centre's case was ostensibly simple. There was bumper harvest and the restrictions on the movement of rice were to be lifted. West Bengal, along with Bihar, Assam, Orissa and Tamil Nadu, were of the opinion that free movement would not only be harmful; it would bring their public distribution systems to a standstill. There was a clear spurt in prices in certain areas of the State.

The State's average minimum price of rice was below Rs.2/- a kilogram before the restriction was withdrawn but it rose up to Rs. 2.09 a kilogram during the first week of October. The point was that an uneven distribution of land for jute cultivation at the...
expense of paddy had led to the State's deficiency in food. West Bengal produced jute and tea on one million acres to help the country earn foreign exchange. Assam also produced 60% of the country's tea crop and Bihar raised a sizable quantity of jute. The State's Finance Minister was quick to suggest that if the Centre refused to revoke its decision, the State Government would ask the Centre to meet its shortage of rice or provide it with necessary foreign exchange for importing rice. The crisis was averted by a massive despatch of rice from the Central pool to meet the State's deficit. But the anomalies remained and it is not unlikely the problem will arise again.

There again when the Centre fixed the price of mustard oil at Rs. 10 a kilogram stocks disappeared in the State. Instead of fixing controls right from the production stage the Centre chose to make a decision without a second look at the all-India marketing pattern. The Centre again agreed to rush rapeseed oil to West Bengal with promises of more to come. It might be repeated that the manner in which the price was fixed by the Centre precipitated the crisis in the first place.

These instances go to prove that not all federal problems can be solved from Delhi and greater de-centralization of political institutions is required.
If one runs through the State's memoranda to the Finance Commission's since independence it will become clear that the demands are not wholly motivated by any particular brand of ideology and that several of the State's problems have been allowed to foster. In several instances what we have today is a virtual piling up of past omissions.

The memorandum to the First Finance Commission 1951, pointed out that "there is no uniformity, no principle and no equity in the past or present patterns of (income-tax) distribution." West Bengal was then receiving the minimum percentage of the proceeds attributable to a State and had been giving away the highest percentage to the Centre. Uttar Pradesh and Bihar were not required to share the proceeds with the Centre, they were allowed to retain the entire proceeds and received more than was raised in those States. Madras was allowed to retain the bulk of the proceeds, contributing only a small share to the Centre. (See Appendix I)

West Bengal submitted that the anachronisms were allowed to continue only because the position had not been correctly analyzed and was not therefore correctly known.

Even in 1951 the State had urged the Finance Commission to carry out a correct and comprehensive analysis and work out new
The memorandum pointed out that the purpose of a uniform income-tax in a federation was not to deprive any State of revenue it would have derived by levying the tax separately but the augmentation of the revenues of both the State and the Centre, besides administrative advantages and the minimisation of inconveniences to the economy. It felt that to treat the unification of a tax in a federation as an instrument of diverting revenue from one State to another cut at the root of the federal principle and that the task of the Commission was to determine the proceeds of income tax attributable to a State. The State's share should be fixed at 60%. Whichever method was adopted the task of the commission was merely to return the sum to the States from where it had been raised after deducting the Central share. It would be wrong to treat the sum as grant as the money did not belong to the Centre. It would be equally wrong if in the process of returning the money, the sum raised in one State was diverted to another.

It was clearly stated that while the principles governing the distribution of grants under Article 275 should be those followed by the Australian Grants Commission — viz. the principle of relative financial needs — the methods of the Commonwealth Commission would need adaptation to local conditions.16

Therefore, relative financial need was the only condition of a grant and was to be measured by the relative financial position...
appearing in the State budgets, adjusted to secure comparability in the pattern of accounting. The grants were to be fixed in such a way that they were not utilized to finance "reckless expenditure greater than in other States or to support lack of effort in raising revenue". 17

The memorandum noted that the effort in raising revenue in West Bengal was the highest among the States; the level of expenditure on security and social services were on the low side; a grant of at least Rs. 8 crores was required annually to wipe out existing debts, which meant that the State had to maintain its existing level of expenditure. And out of the Rs. 8 crore deficit, the State of Cooch Behar had contributed about Rs. 50 lakhs.

Regarding the grant in lieu of a share in jute export duty and jute goods exports, West Bengal submitted that Shri G.D. Deshmukh "had committed the fallacy known in logic as petitio principi in determining the grant on the amount paid by the Government of India after partition to West Bengal, as it was the latter amount which was the subject matter of the dispute". 18 The Finance Commission was urged to decide the question by re-fixing the grant. It was submitted that the share of the Centre should not have been increased on account of partition. The correct principle regarding distribution of the proceeds should have been the determination of the share of the States according to the production of raw jute and the proceeds of the duty on jute goods exports.
West Bengal felt that the grant should not be fixed in relation to one particular year's revenue but should be related to the revenue drawn each year. If the Finance Commission decided to fix the grant in relation to one particular year's revenue, the State felt that it should be fixed in relation to the revenue of the year of determination.

The memorandum went on to add that though industrially the State was relatively advanced it had a decadent agricultural sector. Even regarding the industrial sector, West Bengal had been "rendered vulnerable" because of the existing pattern of transferring federal resources to the States. Per capita Plan outlay, which in the ultimate analysis meant new investment, was practically the lowest; per capita revenue expenditure on nation-building activities was almost at the bottom of the table; spending on education was the lowest; if Calcutta and certain areas adjoining the city were included, per capita income of the rest of the State was comparable to the most backward areas of other States.

Wealth generated in West Bengal resulted in increased Corporation tax which went entirely to the Centre and the proceeds of income-tax and excise duties collected in West Bengal were transferred to other States on the basis of per capita equity. 19

[Special Burdens]

Logically then, the special burdens imposed on the region should also have been borne by the rest of India on the principle
of equalization of burden. Other States with a large agricultural sector had got the best of both worlds. They did not have to bear the burden on social services on industrial areas and at the same time derived the maximum benefit from income generated in such industrial areas. The common man in West Bengal lived in poverty in the midst of plenty. In agriculture, though there was scope for intensive cultivation, it called for large investments in the form of agricultural inputs. In industry, West Bengal had been hit hardest by recession. This had resulted in idle capacity and under-utilization of installed capacity, which could only be remedied by larger investments. There were high levels of unemployment and underemployment remediable only by stimulation of economic growth.

The Greater Calcutta area was the regional growth centre of eastern India and it was in the interest of overall national economic growth to revive the State. Patterns of transfer of federal finance had also to be revised.

Appendix 1: Calculations to show how the amount received by each State as share of net proceeds of income-tax compared with the amount of net proceeds attributable to the State (i.e. West Bengal).
In 1950-51 Part A States received the following grants from the Centre as their share in the proceeds of income-tax:

<table>
<thead>
<tr>
<th>State</th>
<th>Total (In crores of rupees, 1950-51)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bombay</td>
<td>9.95</td>
</tr>
<tr>
<td>Uttar Pradesh</td>
<td>8.53</td>
</tr>
<tr>
<td>Madras</td>
<td>8.29</td>
</tr>
<tr>
<td>West Bengal</td>
<td>6.40</td>
</tr>
<tr>
<td>Bihar</td>
<td>5.92</td>
</tr>
<tr>
<td>Madhya Pradesh</td>
<td>2.84</td>
</tr>
<tr>
<td>Punjab</td>
<td>2.61</td>
</tr>
<tr>
<td>Assam</td>
<td>1.42</td>
</tr>
<tr>
<td>Orissa</td>
<td>1.42</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>47.38</strong></td>
</tr>
</tbody>
</table>

Thus all the Part A States received Rs. 47.38 crores. This represented 50% of the divisible pool. The total was 94.76. After receipt of income-tax collection figures for 1950-51 the memorandum assumed that the ratio in which the divisible pool was raised from the different States in 1950-51 remained the same as in 1948-49.

If the total divisible pool of 94.76 were to be distributed among the nine Part A States in the ratio of collection in 1948-49 the contribution of each State to the divisible pool could be found out. By this process the following table emerged:
<table>
<thead>
<tr>
<th>State</th>
<th>Contribution to divisible pool (in lakhs of rupees)</th>
<th>Receipt from divisible pool (in lakhs of rupees)</th>
<th>% of col. 3 to col. 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bombay</td>
<td>11.60</td>
<td>9.35</td>
<td>23.92</td>
</tr>
<tr>
<td>Uttar Pradesh</td>
<td>4.79</td>
<td>8.53</td>
<td>178.08</td>
</tr>
<tr>
<td>Madras</td>
<td>8.30</td>
<td>8.29</td>
<td>93.15</td>
</tr>
<tr>
<td>West Bengal</td>
<td>30.72</td>
<td>6.40</td>
<td>20.85</td>
</tr>
<tr>
<td>Bihar</td>
<td>1.84</td>
<td>5.92</td>
<td>321.74</td>
</tr>
<tr>
<td>Madhya Pradesh</td>
<td>1.32</td>
<td>2.84</td>
<td>215.15</td>
</tr>
<tr>
<td>Punjab</td>
<td>3.67</td>
<td>2.61</td>
<td>71.12</td>
</tr>
<tr>
<td>Assam</td>
<td>1.89</td>
<td>1.42</td>
<td>84.02</td>
</tr>
<tr>
<td>Orissa</td>
<td>0.23</td>
<td>1.42</td>
<td>617.39</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>94.76</strong></td>
<td><strong>47.38</strong></td>
<td></td>
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</tbody>
</table>

MEMORANDUM TO THE SECOND FINANCE COMMISSION

West Bengal reacted sharply to the population basis of the distribution of the net proceeds of income-tax to States recommended by the Second Finance Commission. The Chief Minister, Dr. B.C. Roy, said that the population basis which had also been suggested by the First Finance Commission was wholly unsatisfactory for West Bengal.* 22

In its memorandum to the Second Finance Commission, the State Government made a strong plea for rectification of the "grave injustice" done to West Bengal in the matter of distribution of the

* The Statesman, November 16, 1957 (Distribution of Income-Tax among the States).
net proceeds of income-tax and in fixing the grant in lieu of its share in the proceeds of the export duty on jute and jute products. The State's greatest grievance about the last commission's recommendations was that, in distributing the proceeds of income-tax, contribution or derivation was given as low a percentage as one to four.

Discussing State finances, the commission, in its report, stated that for four years ending 1955-56, West Bengal had a cumulative deficit of Rs. 265.5 million, the heaviest among all the States. The deficits of nine States, including West Bengal, reflected the impact of the development Plan on their revenues and, except in the case of Assam, also their failure to raise the additional revenue expected of them. The revenue raised in West Bengal through additional taxation fell far short of the target fixed. Out of the target of Rs. 369 million, West Bengal raised only Rs. 45 million, representing 12.20% of the expected total. Its position was second lowest, better only than that of Patiala and the East Punjab States Union.

Compared with 1951-52 the State's revenue yield under principal heads had improved to the extent of Rs. 52.7 million, the figures for the two years being Rs. 238.6 million and Rs. 291.3 million. A disturbing feature in the revenue position of most States was deterioration in the net receipts from irrigation and electricity.
undertakings. West Bengal had deficits for all five years, the figures being Rs. 2.113 million in 1951-52, Rs. 2.269 million in 1952-53, Rs. 1.175 million in 1953-54, Rs. 2.917 million in 1954-55, and Rs. 1.9 million in 1955-56. There was noticeable delay in the utilisation of major irrigation works and tubewells. The returns from electricity undertakings in West Bengal in three years ended March, 1955, was Rs. 800,000.

Five main points were brought out by the review of the States' revenue and expenditure. The scale of devolution recommended by the First Finance Commission was generally adequate for the normal expenditure of most States and left for many of them a sizable surplus to meet their Plan expenditure. The tax effort of many States during that period fell far short of the Planning Commission's expectations. If they had raised the resources expected of them, some of the States, which ran into deficits, might not have done so.

In examining the States' claims, the commission's main objective was to ensure that the States should have sufficient revenue to meet normal expenditure and their commitments in respect of the Plan expenditure on revenue account. No provision had been made by the commission for payments from revenue towards the capital cost of the abolition of zamindari. The cost of compensation for zamindari abolition should have been met from outside the revenue account, the State felt. In the scheme of devolution, the commission sought to close the revenue gap for each State as nearly as possible.
With reasonable prudence on their part all the 14 States ought to have been able to balance their revenue budgets.

Discussing the principle of distribution of income-tax, the report said that there was a wide divergence of opinion among the States. In West Bengal's view, the only method consistent with the language of Article 270 of the Constitution was for the prescribed percentage of the net proceeds to be distributed among the States on the basis of attributability (by which was meant collection) adjusted to provide for payments by assessees of one State into the treasuries of another and for any element of rent or royalty arising in one State and included in the profits assessed in another.

The commission did not find any legal basis for West Bengal's claim that the Union was in some way required to return to the States the income-tax attributable to them after retaining its share. The growth of revenue from sales taxes, motor vehicles taxes and other taxes like electricity duties and entertainment and passenger taxes, to which the urban population made a proportionately larger contribution, had created a situation in which the States were more urbanised and industrially developed were at a distinct advantage compared with those which were not so well developed or urbanised. The main justification for giving a larger
share of income-tax to the industrial States had, therefore, ceased to exist.

GRANTS-IN-AID

In the recommendations relating to grants-in-aid under Article 275 of the Constitution, the Commission had taken note of West Bengal's difficulties arising from the influx of refugees.

West Bengal, with some other States, suggested inclusion of all excise duties in the scheme of division of Union excises and the percentage it asked for was 50. As to the States' share of these duties, the commission considered that it should be 25%. The reduction in the share allocated to the States out of the duties on tobacco, vegetable products and matches would be more than made good by the widening of the range of divisible duties and each State would receive a larger sum from that source. Regarding distribution of the States' share of the divisible excises, the commission felt that it was preferable to continue population as the sole basis for distribution. But the practical effect of such distribution would be to place a few States in a more advantageous position in relation to the rest. In the prevalent circumstances, a small corrective in favour of the latter States would be justified. It had accordingly decided that 90% of the States' share of the divisible Union excise duties be distributed on the population basis, the balance, 10%, being used for adjustments.
Regarding grants-in-aid in lieu of jute export duty, the West Bengal and Bihar Governments desired that the existing grants be permanently secured to them as grants under Article 275 of the Constitution. The Assam Government suggested that the amount of the grant be recalculated with reference to the increase in raw jute production since 1949-50 as the First Finance Commission took into account that year's production to arrive at the amounts of the grants-in-aid recommended by it. The commission was to make recommendations regarding the sums to be prescribed as grants-in-aid for three years from 1957-58. These grants-in-aid would have had no relation to the actual revenue of the Union Government from the export duty on jute and jute products. There was, therefore, no question of relating them in any way to the production of jute. It was recommended that the amounts mentioned in their interim report, which were equal to the sums prescribed by the First Finance Commission, be subsequently readjusted on account of the transfer of certain areas from Bihar to West Bengal. These were to continue till the grants automatically ceased at the end of the financial year 1959-60.

Discussing the problem of determining the States in need of assistance and the amounts of grants to be recommended for them under grants-in-aid of revenues, the commission emphasised that the States would also have to help themselves by raising at least the additional revenues expected of them towards the execution of current
Plan by ensuring all possible economies in administrative expenditure and by maximising their revenues through tightening the machinery for collection and by the recovery of overdue arrears.

West Bengal was in a difficult position; its economy and administration were being strained by refugee influx from East Pakistan and it needed substantial assistance. A grant-in-aid of Rs.32.5 million a year was recommended. The State Government felt that West Bengal's revenue for the past two years would be seriously dislocated by the disappearance of the grant-in-aid under Article 273.

Memorandum to Third Finance Commission

The main thrust of the memorandum to the Third Commission (1961) was that while the State's resources were limited the functions it was called upon to perform were inelastic. It pointed out that the Constitution had laid down the respective functions of the States and the Centre as well as their powers to levy taxes. These powers were mutually exclusive. The functions allotted to the Centre included Defence, External Affairs, Railways and Shipping and during peace time the discharge of these functions in an efficient manner. The Railways and the Posts and Telegraphs also contributed to the general revenues of the Centre. In contrast, the functions allotted to the States included nation-building activities such as education, health, communications, agriculture, development of water resources and power. All these functions called for heavy expenditure even during peace time; neither did the schemes produce corresponding receipts.
These thwarted general economic development in the States; the maintenance of law and order was also a State responsibility. It was pointed out that any deterioration in the situation caused business men and potential investors to panic.

Expanding Sources

The memorandum once again decided to point out that while allocating the taxing powers the Constitution empowered the Centre to levy and collect taxes and duties such as income-tax, Corporation tax, Central Excise duties and customs duties. These taxes again were the main expanding sources of revenue. The State did not think it was incorrect to assign these to the Centre. However it took pains to explain that the taxes which remained on luxuries and entertainments were relatively inelastic sources of revenue. Furthermore, with the abolition of zamindars, land revenue was no longer a source of net revenue as costs of collection and payment of compensation and settlement operations had a negative balance.

The single really expanding source of revenue, sales tax, was held in check because of the inclination to replace the tax by additional Central duties of excise. In 1957 three articles of mass consumption, i.e. textiles, tobacco and sugar, were exempted from sales tax and in lieu thereof an additional excise duty was levied. As a result the States were no longer in a position to vary the rates of tax on these commodities and increase their resources where necessary. They had to be content with the guaranteed
sum representing the sales taxes they were receiving from the commodities prior to replacement by the additional excise duty plus a small marginal excess which might become available. Nor could the excess grow because the additional excises were fixed to replace the amount formally collected as sales tax. The Centre was not keen to increase additional excise duties as it derived the benefit.

As a consequence there was an imbalance between resources and functions in both the Central and State spheres. In the former, the resources available left a surplus for diversion to the States. In the State sphere the resources were exiguous, while requirements were progressively increasing. Thus the Centre's resources for the Third Plan at the draft outline stage were placed at Rs. 6,050 crores while the outlay in the Central Sector was Rs. 3,650 crores. The outlay in the State's sector was placed at Rs. 3,650 crores though the resources amounted to only Rs. 1,200 crores. In the Second Plan the aggregate of the State Plans amounted to Rs. 2,102 crores while the States' resources were estimated at only Rs. 823 crores.

The Constitution-makers were fully aware that such an imbalance was inherent in the Constitutional provisions. Accordingly, provision was made for: (a) divisible taxes, which, although levied and collected by the Centre, could be assigned to the States; and (b) grants-in-aid under Article 275 of the Constitution.
The State was entitled to its share of the divisible pool as of right, the precise quantum transferred depending upon the rise or fall in the collections made and the cost of collections. The State Government thus received a fluctuating amount which should have been computed according to some automatic and simple formula. The grants-in-aid were given to a State which was in need of assistance. While the requirements of a State should have been met from the State's own resources — taxes together with its share of the divisible taxes — it might happen that these did not suffice. The State felt that the legitimate use of grant-in-aid was to fill that gap. Grants-in-aid might also be given for special needs or broad specific purposes, the memorandum pointed out.

The following break-up was given to show the amount of income-tax collected in each State during 1958-59 (excluding Central surcharge) the share of the income-tax received by the State and percentage of such receipts from collections. It will be seen that for every Rs. 100 collected in the States, Andhra had received Rs. 132.3, Assam Rs. 133.1, Bihar Rs. 182.8, Bombay Rs. 19.4, Kerala Rs. 89.8, Madhya Pradesh Rs. 187.6, Madras Rs. 49.6, Mysore Rs. 86.9, Orissa Rs. 393.1, Punjab Rs. 103.9, Rajasthan Rs. 122.5, Uttar Pradesh Rs. 216.4, West Bengal Rs. 18.2 and Jammu and Kashmir Rs. 373.8.

West Bengal therefore received the least on the basis of the system of distribution recommended by the Second Finance
Commission. It's share of the amount collected within its territory was less than what Bombay received. Certain States received more than what was collected within their territories. Thus Orissa received almost three times what was collected. Uttar Pradesh received more than twice the amount collected within its territory. The Centre received 40% of the net proceeds. It followed that there was considerable "transference" of income-tax collected in West Bengal and Bombay and Madras while the beneficiaries were the other States.

[STATE'S SHARE OF DIVISIBLE POOL]

The memorandum then examined the recommendations of the First and Second Finance Commissions with regard to the criteria adopted for distributing the State's share of the divisible pool. The Second Finance Commission stated: "In all previous schemes of distribution some weight has been given to collection but this has been reduced in favour of population. In our opinion this has been a move in the right direction". (Para 105) The First Finance Commission wrote: "In so far as needs in our view form the main criterion of distribution, we consider that only a broad measure of need such as is given by the respective populations of the States is suitable for application in the distribution of the proceeds of a shared tax". Assuming that "needs" were relevant for the purpose of Article 270, the findings of the First Finance Commission were based on an assumption which was not warranted by
facts. The First Finance Commission, after introducing the question of need and making it the main criterion for distribution, made the assumption that the broad measure of needs of the various States was related to the respective populations of the States. The assumption was that needs varied directly and proportionately with the population.

The assumption completely overlooked the fact that the needs of certain States where there were heavy concentration of population in vast cities and their environs were much greater per capita than those of other States where the population was evenly distributed over a wide area and was predominantly rural in character. In West Bengal there was the added complication of a high degree of population. The memorandum sought to draw attention to the defective reasoning of the First and Second Finance Commissions which had overlooked that the per capita cost of social overheads and services were much higher in concentrated centres of population and in densely populated States than in predominantly rural and low-density areas.

When considering the principles according to which income-tax should be distributed among various States, the Second Finance Commission concluded that the main justification for giving larger share of income-tax to the industrial States had ceased to exist. Their argument was that when income-tax first came to be distributed,
agricultural States had a substantial and expanding source of income from land revenue and that source had to be balanced by giving a larger share of the income-tax to the industrial and commercial centres.

FOURTH FINANCE COMMISSION

The memorandum to the Fourth Finance Commission pointed out that West Bengal's indebtedness to the Centre at the end of the Third Plan would exceed Rs. 500 crores if the pattern of Central assistance was maintained. The State's outstanding debts had risen from Rs. 44 crores in 1952 to Rs. 472 crores by the end of 1964-65. Complaining against the pattern of allocation, the State Government also pointed out that the per capita devolution in all the States had improved between the awards of the successive Finance Commissions but in West Bengal it had suffered a deterioration. Even in terms of population West Bengal should have got much more than what it had received out of total Central taxes and grants-in-aid.

West Bengal emphasized that the pattern of allocation was fashioned to maintain excessive control over the States to implement a Centrally agreed Plan of economic development. It argued that a change in the pattern would help West Bengal without curtailing Central supervision.

West Bengal appealed to the Finance Commission not to confine itself to its terms of reference only but to consider the
needs of the State during the Fourth Plan. The State also wanted to do away with the disparities in pay scales and dearness allowance of West Bengal and Central Government employees. It pleaded for Central help for rehabilitation of refugees.

Earlier, the Chief Minister, Mr. P. C. Sen, urged the commission to consider the needs of the State which he said was heavily deficit in food. Mr. Sen explained how the State's food and other large problems arose largely as a consequence of partition. He emphasized that West Bengal had, in the interests of India as a whole diverted, 1.1 million acres of paddy land to jute cultivation.

The Chief Minister pointed out that per capita incidence of taxation in West Bengal was the highest in India. As the scope for more taxation was limited the State had no alternative but to approach the Central Government to meet its special problems caused by natural calamities and the refugee influx. Border security arrangements, including strengthening of the West Bengal Police, meant increased strain on the State's resources.

The State was of the view that the existing method of determining the State's share of income-tax was unsatisfactory. It wanted the divisible pool to be raised from nearly 67% to a minimum of 80%.

State-wise consumption of commodities should be the basis of the distribution of Union excise duties. It held that the fixation of a definite amount as a grant in lieu of tax on
railway fares would deprive the State of the benefit of increased railway fares. It was also opposed to the ceiling on sales tax.

The commission was told of the Centre's refusal to take advantage of Article 269 which required the Centre to levy certain taxes for the benefit of the States.

AWARD 'NEITHER GOOD NOR BAD'

However, judging by newspaper reports, the Fourth Finance Commission's award was "neither good nor bad" for West Bengal. It was stated to have put the State in a "shoe-string position". The receipts under the award were stated to be the "absolutely essential minimum West Bengal will need to meet the deficit in non-Plan expenditure during the Fourth Plan period." It was argued that even to ensure reasonable flexibility in non-planned expenditure the State would have to make special efforts to earn more revenue from internal sources, the scope for which would continue to be very limited.

Under the Third Commission the State was awarded Rs. 112 crores. Additional revenue expenditure on account of the maintenance of Third Plan schemes was expected to be about Rs. 100 crores. As against the Rs. 222 crores asked for by the State, the Fourth Commission gave West Bengal Rs. 197 crores, leaving a deficit of Rs. 25 crores. The gap was found to widen because the rate of economic growth would rise progressively,
resulting in larger non-Plan expenditure commitments to the State. Originally, West Bengal estimated its unplanned expenditure deficit during the Fifth Plan period at Rs. 300 crores which included Rs. 39 crores to cover the Government's commitments under dearness allowance. The figure was subsequently reduced to what was considered the absolute minimum of Rs. 275 crores.

**PERSONAL NOTE**

In personal note appended to the Fourth Finance Commission report, Mr. P. V. Rajamannar, pointed to the risk of an important matter like the determination of the resources available to each State becoming "a gamble on the personal views of five persons or a majority of them". Determination of available resources in the different States was, of course, vital for decisions on grants to be made (under Article 275) to supplement the resources of individual States. The recommendations of the Commission as well as those of the three earlier ones, might have created the impression that the commission had placed a premium on fiscal prudence. While the total amount of the annual grants under this Article had been doubled, six States, including West Bengal, Punjab and Uttar Pradesh were made ineligible for the grants; three-fourths of the annual total of these grants recommended (Rs. 122 crores) would go to five States: Assam (Rs. 16.82 crores), Kerala (Rs. 12.2 crores), Nagaland (Rs. 7.07 crores), Mysore (Rs. 18.24 crores) and Orissa (Rs. 29.18 crores). Of these, the
first three might have deserved the bounty in view of the special reasons applicable to conditions in those States; Rajasthan and Madhya Pradesh fared badly even if it was conceded that their problems were much less complex. "Most States", observed the commission, "produced successive revised forecasts either revising the original figures on the basis of further information or including fresh items of expenditure not included in the original forecasts". It added: "The number of States coming forward with fresh schemes appeared to be unending".

Besides the grant under Article 275 further transfer of resources from the Centre to the States had been effected by placing the entire revenue from Central excises into the divisible pool, instead of only 35 items as under the Third Finance Commission. Distributed on the criteria of economic and social backwardness adopted by the commission, the percentage share of West Bengal, Maharashtra, Madras and Uttar Pradesh would decline. They would however, receive larger amounts than they had. There was little scope for the scheme of distribution of income-tax; the commission recommended only a slight increase in the State's share from \( \frac{66}{3} \% \) to 75%. But here again the reduction of West Bengal's share from a little over 12% to 11% showed that the special problems of industrial States providing for urban services and other facilities required for industry had not been fully taken into account in
The memorandum to the Fifth Finance Commission (1969), after making the familiar protests against the allocation of resources not commensurate with the allocation of functions, the elasticity of revenue sources with the Centre and the "pressing needs" of the State, pointed out that the Constitution had provided for rectification of imbalances by transfer of federal resources to the State through the recommendations of the Finance Commissions.$^{31}$

It reiterated that the States had complained before to the Finance Commissions that there was a perceptible trend towards centralization of resources in addition to centralization of Central functions. It pointed out that a glaring instance was the amendment of the Income-Tax Act which had removed from the definition of income-tax and tax paid by companies and had thereby caused an appreciable shrinkage of the divisible pool to which the States were entitled. Similarly special duties of excise on certain goods levied since 1963 in the form of surcharge on basic duties did not form part of the divisible pool. The memorandum was bold enough to point out that if adequate resources could not be made available to the states under the provisions of the Constitution "it would request the Finance Commission to recommend an amendment of
the Constitution in a way that allocation of resources among the States could correspond to the allocation of functions entrusted to the States.

MORE RESOURCES FOR CENTRE

Under the awards of the successive Finance Commissions the Centre had been left with more resources. In 1960-61 the State's share of Central resources amounted to Rs. 165 crores which rose to Rs. 423 crores in 1968-69 whereas Central resources rose from Rs. 532 crores in 1960-61 to Rs. 1464 crores in 1968-69.

The Chief Minister Mr. Ajoy Mukherji, and the Deputy Chief Minister, Mr. Jyoti Basu, told the Finance Commission that the revenue deficit for the State was calculated to be Rs. 581 crores during the next five years; they thought that the deficit should be met by the Centre. The deficit included Rs. 90 crores of additional expenditure, Rs. 45 crores each for dearness allowances to the State Government employees at Central rates and revision of pay scales.

Mr. Mukherji and Mr. Basu suggested some changes in the system of distributing the Centre's divisible pool. Regarding income-tax, for example, their suggestion was that the weightage should be 35% on collection and 65% on population, against 20% and 80%. In excise duties, the basis should be 75% on population and 25% on the degree of urbanization. The respective percentages
then were 80 and 20.

They demanded relief of debt charge burdens. They argued that Central assistance for the State's Fourth Plan would be more than taken away by the State's repayment of Central loans. Central assistance according to indications available would be \( \text{Rs. 230 crores} \) and repayment would amount to \( \text{Rs. 234 crores} \).

Presenting the case of West Bengal before the Sixth Finance Commission, the Chief Minister, Mr. Siddhartha Roy, analysed the Directive Principles and relevant provision of the Constitution to establish that the State was entitled to "a larger and its due share" of income-taxes, excise duties and resources of the divisible pool. In his memorandum to the commission, the Chief Minister pleaded for integration of the surcharges on income-tax for Union purposes with the basic rates of income-tax and enhancement of the States' share from 75% to 90% of the divisible pool. The basis of distribution should be substantially modified to raise the weightage of contribution to not less than 40%.

On excise duties, he submitted that the distribution of the proceeds should be on the basis of consumption, and, that, if reliable figures of consumption in different States were not available, the distribution of the States' share inter se should be effected on the basis of 40% for urban population and 60% for rural population.
He pointed out that large sums were collected from West Bengal and unless a "reasonable portion" was ploughed back to the State, it would not be able to maintain the infrastructure for industrial development which would retard the economic progress of India as a whole. It would not be proper to assume in this connection that West Bengal was an industrially-developed State, he pointed out.

Referring to the Constitutional provisions, he stressed that proper weightage should be given to collection while deciding on the devolution of taxes and duties.

Apart from the constitutional questions, Mr. Ray said, the special problems of West Bengal should also be considered. According to him, the extent of unemployment which was "most acute" in the State, the severe inadequacy of primary education facilities and the percentage of Scheduled Castes and Tribes who were economically backward were the most relevant factors. The Planning Commission had declared that apart from Calcutta, Howrah and 24-Parganas, all other areas of West Bengal were backward.

Mr. Ray referred to the districts of Bankura and Purulia and North Bengal and said it was for the development of all these areas that the State should get more from the divisible pool. West Bengal, he said, needed help to wipe out its large revenue deficit and to prepare in a big way for the Fifth Plan.
The Chairman of the Commission, Mr. Brahmananda Reddy,* assured the Ministers that his commission would "try to assist West Bengal to improve its economic condition to the extent possible within the resources available". He said the State's case had been made out "lucidly" and that major problems, like the decline in industrial production, stagnation in agriculture, problems of displaced persons and problems of Calcutta, including the port, had been dealt with comprehensively in the memorandum placed by the Chief Minister.

That the chairman and members of the commission viewed West Bengal's case sympathetically was evident from certain remarks and observations made by them during discussions, it was understood.

In his statement, the Chief Minister remarked that industrial development in West Bengal, instead of being a source of wealth to the State Government had become a liability according to the pattern of transfer of Central resources to the States. Wealth generated in West Bengal was transferred to other States on the principle of per capita equality, but the entire liability for maintaining law and order, social overheads, transport facilities and other components of infrastructure of industrial growth developed on the State Government.

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He said that the Fifth Finance Commission had stated that the practice of distribution of a part of the divisible pool relating to income tax on the basis of contribution by each State could be regarded as the counterpart in the non-agricultural sector of the taxes on agricultural income which could be levied by the States themselves. If the agriculturally prosperous States had a right to retain the entire revenues from agricultural income there should be no objection to allowing the so-called industrial States to retain at least a substantial part of revenue earned by them from non-agricultural income. It was only just that the principle of devolution of income-tax proceeds should be such as to enable each State to get back "a reasonable part of the contribution made to the divisible pool by incomes originating within its territory".

Regarding excise duties, Mr. Ray said that although the Fifth Finance Commission put emphasis on per capita income this should not be the criterion in assessing the relative backwardness of States for different reasons. Neither should "special needs or backwardness be taken into account in determining the share of a tax, although if assessed on the basis of the Directive Principles of the Constitution, West Bengal's needs would be very great."
In the new context, the practice of calling a State backward or advanced by the degree of concentration of industries in some parts of it, to the exclusion of other factors had become outdated, he added.

**Loan Repayments**

Regarding loan repayments the Chief Minister pointed out that the development schemes taken up by the States brought benefits to the Centre as well. He said Central loans included shares of small savings collections loans utilised by States for relending to their parties and loans given for specific or developmental purposes. Mr. Ray felt that State Governments should not be asked to repay the small savings loans because "our shares are given from collections exclusive of withdrawals of principals and interest" and that "in no year has there been a net loss due to withdrawals exceeding collections".*

**PECULIAR PROBLEMS**

The Chairman of the Sixth Finance Commission, Mr. Brahmananda Reddy, said after conclusion of the commission's hearing that West Bengal had some "peculiar problems which merit consideration by the Government of India, the Planning Commission and the Finance Commission".*

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On the controversial question whether population or collection of States should be the criterion for determining their shares of the income-tax and excise duties, the chairman said he would have to cover some more States to come to a conclusion.

The West Bengal Government had emphasized that more weightage be given to collection than in the past; three of the five previous commissions gave 80% weightage to population and two others gave 90%. The commission had been urged by some other States to consider urbanisation, problems of Scheduled Castes and some other factors in this regard, Mr. Reddy said.

The Finance Minister, Mr. Sankar Ghose,* strongly pleaded for a "realistic assessment" of receipts and expenditures to ascertain the non-Plan gap. He pointed out that an "unrealistic assessment of these by the Fifth Finance Commission had caused grave economic problems" in West Bengal. Eventually, the Planning Commission had to make a fresh assessment and give non-Plan assistance to some States, including West Bengal, to reduce the gap and ensure that Plan funds were not eroded to meet the gap. This step by the Planning Commission was a "clear proof" of the mistake made by the Fifth Commission, Mr. Ghose said.

He told the Commission about the revenues and expenditure of the State Electricity Board, Calcutta Transport authorities, the

Milk Supply Scheme and some other projects and also the extra expenditure necessary for the Education Department. The Minister later told reporters that the commission had to be given the details of such projects because the Fifth Commission had assumed that large profits would be earned by these to help to reduce the non-Plan gap.

The Third Finance Commission, in its report observed: "It has been held before us by the industrial and urban States, in whose territory large amounts are collected by way of income-tax, that they should have an incentive and wherewithall to maintain the environments which would preserve and promote industrial and trade activities ... Large concentrations of population, more particularly of industrial labour, creates problems of law and order and give rise to an increased demand for administrative and social services".

"NEED" AS CRITERION

It was pointed out to the commission that while determining the States' share of the taxes, the "need" and "backwardness" of the States should be no consideration. "Need" had been mentioned in Article 275 under which States "in need of assistance" got grants-in-aid. But regarding the taxes, the relevant provisions were Articles 270 and 272 where there is no mention of "need".

The commission also received a memorandum submitted jointly

1 Ibid.
by the Chambers of Commerce and heard the views of their representatives. They pointed out that West Bengal's debts to the Centre had piled up to Rs. 700 crores, excluding the overdrafts to the Reserve Bank of India. This was bound to be heavier by the end of the Fifth Plan period. Regarding the devolution of taxes and duties, they said the high weightage given to the population factor by the previous Finance Commissions did not take into account the high density of population in urban areas. They pleaded, in common with the State Government, that collection of income-tax should be given higher weightage because the State had to maintain the necessary environment and infrastructure needed for generation of incomes.

Regarding excise duties, the Chambers said consumption should be the criterion. For the lack of relevant data, previous commission did not apply this criterion and accepted population as the basis. The present basis of giving 80% weightage to population called for a revision because the urban population comprised the major consumers of the exciseable articles in comparison with the rural population.

Referring to grants-in-aid, the Chambers felt that the commission should consider the fact that industrially advanced States, like West Bengal, had extensive backward regions. Special problems like the presence of refugees should be taken into account along with the extent of unemployment, percentage of scheduled castes and tribes and growth of primary education.
Regarding loans, the Chambers stated that the commission should consider whether certain loans which would not yield immediate financial returns should be converted into grants, whether the time of repayment of certain loans should be deferred and whether the rate of interest on such loans should be reduced.

CALCUTTA'S PROBLEMS

The Chambers dealt separately with the problems of Calcutta and said these could not be tackled by the State Government alone without special financial assistance from the Centre. States like West Bengal, which have a large industrial base, raw material and technical manpower should not suffer on account of inadequate resources for sustenance and further growth, the Chambers said.

The Sixth Finance Commission recommended debt relief amounting to Rs. 1970 crores to the States during the Fifth Plan. Such financial relief for West Bengal, as suggested by the commission, exceeded Rs. 100 crores.

The commission recommended significant changes in the terms of repayment of Central loans with a view to providing relief to the States. In some cases it deferred such repayment by 20 to 30 years.

It was stated that towards the end of March, 1972, West Bengal's debt to the Centre was Rs. 660 crores. Since then it had gone up. According to the Finance Minister, the State had to pay
to the Centre about Rs. 90 crores a year in repayment of loans. This he said was a great burden on the State because a major portion of its receipts had to be diverted every year to ensure repayment of such loans.

SETALVAD COMMITTEE

The Setalvad Committee, in its recommendations on the Centre-State relations, had observed that sometimes the States had to borrow money from the Centre to repay Central loans and that this added an air of unreality to the whole transaction. To provide further relief to the States, the Sixth Finance Commission had recommended that some items of debt, which appeared irrecoverable, be written off.

West Bengal and several other States had put pressure on the Centre to include debt relief in the terms of reference of the Sixth Finance Commission to enable it to give relief to the States in respect of repayment of debts or, in other words, to deal with their non-Plan capital gap. The previous Commissions had been empowered to deal only with the non-Plan revenue gaps of the States but the Sixth Finance Commission was given power to also deal with the non-Plan capital gaps of the States.

West Bengal Government circles were happy over the allotments made by the Sixth Finance Commission. They pointed out that the State had received a grant of Rs. 253 crores, the largest amount given to it as a grant.
The Fifth Finance Commission had recommended a grant of Rs. 72 crores. The Sixth Finance Commission appreciated the special needs of West Bengal and increased the grant by more than three times. Another reason for satisfaction was the amount of debt relief provided to the State by the Sixth Finance Commission — Rs. 153 crores.

The Fifth Finance Commission had recommended a total allotment of Rs. 369 crores. The Reddy Commission increased it by more than 100% to Rs. 823 crores. If the debt relief was added to it, the total allotment to the State would be about Rs. 1000 crores.

While expressing satisfaction over the award, it was stressed that West Bengal's problems were too many. West Bengal spokesmen hoped that the Sixth Finance Commission's award would not be used as a ground for not giving the State substantial Central assistance in the Plan sector.

The Chief Minister and the Finance Minister, who were the main spokesmen for the State during the hearing by the Sixth Finance Commission in Calcutta, appeared satisfied with the award but reserved their comments.

The Left Front of the Memorandum

In his Budget speech, the present State Finance Minister, Dr. Ashoke Mitra said that the Centre had been steadily raising the surcharge on income-tax (instead of income tax rates) and
incidence of additional excise levies (instead of the basic excise duty rates) as these were not shareable with the States.

He claimed that the proceeds of some of the newer taxes like gift tax, wealth tax on urban immovable property and the tax on interest earnings of banks had been eaten up by the Centre.

Similarly, since the merging of Railway passenger tax with the price of rail tickets in 1961, the States had lost another source of revenue as they were previously entitled to the proceeds of the levy. The Centre had pegged the State's share out of the tax's collection at Rs. 16 crores whereas at the existing rates, it ought to have been Rs. 100 crores.

The position was that the States under the existing constitutional framework had to bear the responsibility of development in a big way (such as education, health services, construction of roads, bridges and irrigation schemes) but were being denied commensurate fiscal powers.

Mr. Mitra said: "Of the total revenue raised in the country, not more than 25% were under the command of the States; the deployment of the other 75% was the prerogative of the Central Government".

The West Bengal memorandum to the Finance Commission made a "passionate plea to lift federal finances from a futile exercise of robbing Peter and paying Paul" and make it instead development-oriented."
The Six Finance Commissions, which had gone into the issues, had tended to confine their role to that of a gap-filling agency. "A time has come when this approach should be changed and the labour of the Commission be oriented towards devising a system that would help the process of development of the country as whole. For this the basic necessity was to enlarge the size of the divisible pool and allow larger transfer of resources from the Centre to the States".

SPECIFIC SUGGESTIONS

The memorandum made four specific suggestions on sharing of tax proceeds: 1) the surcharge on income tax be brought under the divisible pool or merged with income tax, 2) 100% of the proceeds of the income-tax together with the surcharge be in the divisible pool, 3) at least 50% of the proceeds of the Corporation tax be included in the pool and 4) the size of the divisible pool of the Central Excise duties be raised from 20% to 60% and all types of excise, special and regulatory duties and cesses be brought within the divisible pool.

The Left Front which returned to power in Assembly elections, was CPI-M dominated and had certain economic and political ideas. Some had strong reservations about the ideological undertones in its formulations. The criticism was however not always substantiated by facts. It was conceded that the Left Front's autonomy move was intelligently conceived, though in its anxiety to get on with its
programmes it had betrayed a smack of opportunism. In that context the Front's memorandum on Centre-State relations and the one to the Seventh Finance Commission had been welcomed as important landmarks in a rapidly changing political landscape.

The State Finance Minister, who had the distinction of appearing in his role as an economist before at least one previous commission presented his Budget speech as an introduction to the Government's economic policy. These documents were held in high esteem.

Earlier, a comprehensive note had been prepared on the virtues of a less integrated economy to reduce diseconomies of scale and denudation of the political and economic autonomy of the States.

To begin chronologically with what was described as "growth and diseconomies", it was pointed out that even with the advent of planning, national per capita income had risen little. The official reasons for the low growth rate were the occurrence of natural calamities and hostilities with external Powers. However, another point of view was that savings having shrunk or not having grown satisfactorily, capital formation was less than optimal, leading to income inequalities. These applied as much to regions as to individuals. Therefore, in the absence of adequate growth what little took place was unjustly distributed. Cumbrous regulatory instruments had fouled up market signals and rendered cooperative advantages infructuous; market rigidities had arisen which had led to the rise of oligopolies. This issue
was raised to emphasize that though oligopolists maximized profits they placed restraints on output. Neither did they plough back enough resources to usher in high growth productive activities. Public savings were shrinking with extensive outlays on public undertakings generally yielding poor rates of return. The economic process could not be divorced from developments in the polity and that of Centre-State relations was held to be of major relevance to the problems of growth and redistribution. Though the constitutional structure was supposedly federal with legally even responsibilities between the Union and the States, it has been seen how partition and other developments since the commencement of the Constitution have placed severe constraints on the powers of the States.

MONETARY RESERVES

Though the Finance Commissions were set up to devolve financial powers to the States and Part XII of the Constitution was quite clear about how income-tax proceeds should be distributed between the Union and the States, control over monetary reserves remained the exclusive preserve of the Centre which exercised control over the Reserve Bank, currency, coinage, legal tender and foreign exchange. With the exception of taxes on agricultural income and property, the rest of the major sources of income, including credit taxation, belonged to the Centre. Moreover, the Finance Commission had been eclipsed by the Planning Commission; loans and grants for development purposes out of the consolidated
funds of the Centre were the prerogatives of the Planning Commission. The latter therefore determined the pace and pattern of growth all over the country. The nature of the Planning Commission being what it was the Centre had become the dispenser of monetary and fiscal bounty to the States who were expected to queue up for benediction. Professor Gadgil had supported the plea for a decentralized framework for planning.

But, he pointed out quite clearly that the need for a substantial degree of uniformity in tax structures and burdens in the interests of optimum allocation of resources, effective tax administration and tax compliance conflicted directly with the need for fiscal autonomy of the State Governments. The result was inevitably a compromise and might have led, as it has in some older federations, to frequent reviews of the system. Inter-governmental finances in India had been marked from the very outset by a growing gap between the requirements of the States and what they are able to raise on their own. The successive Finance Commissions had made modest contributions to reduce that gap but had not called for a review of the system.

Professor Gadgil had said that the problem of Centre-State relations was a general one found in all Constitutions. The essence of a federal Constitution was an attempt to divide responsibilities between the Central Government and the other Governments, which were semi-autonomous, the degree of autonomy being defined by the Constitution. In order to vest this autonomy with reality, it was necessary
that the resources required to finance the responsibilities placed on these autonomous units — the State — be made fully available. The States should not be made dependent on the Central Government for finances.

The Administrative Reforms Commission had pointed out that the Centre had imposed Central thinking for dispensing financial favours. This variety of centralization had caused the country dearly. Indivisibilities have been imagined to exist where there have been none. With the result that State Governments had been more prone to cash in on political conformism than efforts at resource mobilization. The memorandum to the Seventh Finance Commission firstly brings us up to date with the economic realistics in West Bengal. Secondly, and more importantly, it is an interesting the attempt to reorient the fiscal structure, though/(memorandum to the) Fifth Finance Commission, under the aegis of the United Front Government, made a similar effort.

The memorandum makes the first point very clear in its recommendations. "There should be far-reaching changes in the pattern and scheme of Centre-State relationships". To this end it refers to its memorandum on Centre-State relations submitted to New Delhi and circulated among State Chief Ministers. The basic approach of the State Government to the terms of reference before the Seventh Finance Commission was that the States had a rightful claim to a reasonably large share of the Centre's elastic revenues — large enough to cover current as well as developmental requirements, keeping in view the role enjoined on the States by the Constitution.
The State Government felt that the Finance Commission could fulfill a historically significant role if through its deliberations and recommendations it could ensure that three quarters of national revenue were earmarked for the purposes of the State Governments. The suggested earmarking of a quarter of the aggregate revenue from the Centre would not constrict it in the fulfilment of its constitutional obligations. The commission, however, would be fully justified in suggesting the changes necessary in the Constitution and the States.

It claimed that the forecasts of expenditure and receipts of the Centre were not subjected to the same kind of scrutiny as the forecasts of the State Governments. If the "asymmetry" was ended, further resources would be available for transfer to the States and the estimates of resources available for transfer would be more realistic.

The memorandum made its most significant recommendation in suggesting that the commission not recommend itself to a mere gap-filling role. As a corollary it added that the normal requirements for administration, including development administration, on the part of the States had to be met, as far as possible, from out of the proceeds of taxes and duties irrespective of whether these were formally collected by the Centre or the States. The grant-in-aid element had to be treated as a residuary support to fill the gap left uncovered after the distribution of Central taxes and duties. The tendency in the past had been to let the size of the divisible pool stagnate in relative terms. The size of the pool had been
restricted by changes in tax laws and during successive forecast periods principal items of revenue had been distributed almost on the same basis of percentage as the total proceeds. The memorandum wanted the practice to be reviewed.

On the surcharge levied on income-tax the memorandum wanted suitable legislative changes to include the extra levy in the divisible pool, or the absorption of the surcharge in the basic income-tax. It wanted the entire proceeds of the income-tax, together with the surcharge, to constitute the divisible pool. The memorandum urged that at least 50% of Corporation tax proceeds be included in the Divisible pool after suitable legislative changes. It also wanted the size of the divisible pool of Central Excise duties to be stepped up from 20% to 60% of the net proceeds. The memorandum suggested that the divisible pool be similarly enlarged to include excise, special and regulatory duties and cesses.

It pointed out that additional excise duties should be reviewed and the right to levy sales tax on goods subject to such duties be restored to the States; this right should not be circumscribed by a ceiling rate applicable to declared goods. The grant in lieu of railway passenger tax should not be a fixed grant but be determined as proportion of the total railway passenger earnings every year, excluding suburban passenger earnings. The States' right to railway passenger tax under Article 269 should be restored, failing the Centre's willingness to grant the demand.
Another important suggestion made was in regard to the non-Plan capital gap. Drawing on the Seventh Finance Commission's wider terms of reference "appropriate measures" to deal with the non-Plan capital gap were recommended by the Memorandum.
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