CHAPTER - IV
CHAPTER IV

THE EVOLUTION OF PROVINCIAL FINANCE IN BRITISH INDIA

4.4.1 Introduction

Dr. Ambedkar as part of his doctoral thesis to the Columbia University submitted the present book under the title *The Evolution of Provincial Finance in British India: A study in the Provincial Decentralisation of Imperial Finance* under the guidance of Prof. Edwin R. A. Seligman.

This book, besides the introduction, is divided into four parts and each part consists of three chapters. Four parts are namely (i) Provincial Finance: its origin, (ii) Provincial Finance: its development, (iii) Provincial Finance: its mechanism, and (iv) Provincial Finance under the Government of India Act of 1919.

In the introductory part, Dr. Ambedkar gives the plan of the book and an explanation towards the title and the sub-title of the book. He stated that the meaning of the phrase “decentralisation of finance” meant differently at different times. In 1855, the decentralisation of finance resulted in the separation of the Local from the Imperial finance, whereas the decentralisation of 1870 to 1882 resulted in the separation of Local from Provincial finance. Hence ‘decentralisation of finance’ could not be indicative of Provincial finance and is a general name for variegated and multifarious process of decentralisation. Hence the title and the sub-title of the book were purposely chosen to give a definite shape to the subject matter of the book and the title and contents could be the same.
PART I

4A.4.1 PROVINCIAL FINANCE : ITS ORIGIN

CHAPTER I

4A.4.1.1 The Imperial System: Its Growth And Its Breakdown

Dr. Ambedkar presents a picture of the system of Finance as it existed before the inauguration of the Provincial Finance and to states the causes that called for a change in its organisation.

As pointed out in the beginning itself to replace the existing multiplicity in the systems of justice and police by a uniform system with its varieties classified and systematised, the Imperial system of Government in 1833 was essentially established in India. However, under the existing system then prevailing such multiplicity was inevitable, and now to the codes of law promulgated by these authorities had to be added the whole body of English Statute law introduced in India. All this work of administering such a diverse body of laws proved so embarrassing that the Supreme Court of Calcutta stated (as quoted in Herbert Cowell’s The History of the Constitution of Courts and Legislative Authorities in India, Calcutta): “no one person can pronounce an opinion or form a judgment... upon any disputed right of persons, respecting which doubt and confusion may not be raised by those who may choose to call it in question; for very few of the public or persons in office at home, not even the Law Officers, can be expected to have so comprehensive and clear a view of the Indian system of law, as to know readily and familiarly the bearings of each part of it on the rest.” (Moon 1989)
Another “motive was to create a strong central government to deal effectively with the European settlers in the country. It is to be noted that if the native population suffered under the uncertainties of law, the British population lived under the most galling restrictions. The revelations of oppressions by Englishmen practiced, in the early days of British Rule, were followed by very stringent laws governing the entry and residence of private British subjects in India. No British subject of European birth was allowed to reside in India beyond 10 miles from any one of the principal settlements without having previously obtained a special license from the Company or the Governor-General of India or the Governor of the principal settlement in question. Unlicensed British subjects were made liable to be deported and such as were licensed were required to register themselves in the court of the district in which they resided. Subjected as they were to the regulations of the Local Government they were made amenable to justice in India as well as in Great Britain for all illegal acts done in British India, or in Native States” (Moon 1989).

The ruling race had long chafed at these restrictions, under which it was placed, without much avail. But as time went on, and as the Indian Empire was consolidated by successive victories over the native princes, many raised their voice against these restrictions stating that they had now outlived their purpose. The British Parliament too was susceptible to these sentiments. It realised that a harmonious treatment of the immigrants and an effective control over them was absolutely essential. Also apart from the necessity of a harmonious treatment based on uniform principles, as Dr. Ambedkar puts it, “the fears of Parliament that the ingress of British immigrants would result in the revival of oppression on the natives were not completely allayed.” (Moon 1989)
The Parliament too desired to subject them to a strong and uniform central control, so that the offender in one jurisdiction might not be able to find an asylum in another. Therefore, considering these aspects about the uniformity of laws or securing stringency of control over elements subversive of order, the prevalent system of government with its divided jurisdiction was ill-suited for the purpose held in view. Hence an all-powerful Central Government legislating for and controlling the affairs of India as a whole was considered to be the only solution in such an emergency.

A Central government was thus created by vesting the legislative power exclusively in the Governor-General of India in council. Being responsible for peace, order and good government, the Presidencies of Madras and Bombay could have refused to govern according to laws made by the Central government, and all the gain expected to arise from the institution of a central and strong government would have been lost. To eliminate this element of weakness in the Indian politics newly established, Parliament proceeded to divest the presidencies of Bombay and Madras of the high status that they hitherto occupied as responsible governments. And so the Executive Government of each of the several Presidencies was to be administered by (not vested in as heretofore) a Governor and three Councilors, which were to be in turn under the direct control of a Governor General and councilors styled the Governor-General of India in Council.

This Imperial system of government as established in the aforementioned manner was necessarily accompanied by the Imperial system of Finance. Before the inauguration of the Imperial system of Administration the several Presidencies were like separate clocks each with its own mainspring in itself. Each possessed the powers of sovereignty, such as the legislative, the penal, and the taxing powers. And were independent in their finance. However, for their ways and
means they often drew upon the resources of one another, not, because their exchequers were not distinct, but because they were parts of a common exchequer belonging to the East India Company. All this was changed by the Act of 1833, which vested the revenues and the government of the different territories in the Governor-general of India in council. British India in fact was subdivided into Presidencies under separate locally controlled governments only for the sake of convenience. In reality, however, it was one sole grand Power in dependence on Great Britain, having undivided interests, a single exchequer, and controlled in all essential and general principles by one Government—the Governor-General in Council. So when the Crown took over from the Company the government of India in 1858 it was found that no province had any separate power of legislation, any separate financial resources, or practically any power of creating or modifying any appointments in the public service. The Imperial system of Government, however, from its very start it suffered from the fatal disease of financial inadequacy, and it was only occasionally that the efforts of the Finance Ministers were successful in restoring an equilibrium and slaving off the hour of crisis. In this context, Dr. Ambedkar, here, quotes Disraeli who remarked in the House of Commons—"...the state of the finances of India has always been involved in perplexity, and India that has produced so many great men, seems never to have produced a Chancellor of the Exchequer." (Moon 1989).

The inadequacy of Indian Finances is mainly to be ascribed to an unsound fiscal policy. The policy was unsound for various reasons. In matters of state economy it is usual to argue that the expenditure to be incurred should determine the magnitude of revenue to be raised. But it must be remembered that the mode of raising the revenue is an aspect of the question that is fraught with tremendous consequences for the stability and productivity of the nation. It is important for those who are entrusted with the financial management of the State to look beyond the
more immediate object of raising and spending of money, as the “hows” of finance are very important, and can be seldom neglected in practice with impunity. As Dr. Ambedkar puts it, “The wealth of society is the only patrimony on which the State can draw, and the State that damages it cannot but end in damning itself. History is abound with instances of States wrecked by the unwise neglect of these evident truths, but if an illustration be wanted in further proof thereof, the system of Imperial Finance established in India is matchless for the purpose.” (Moon 1989)

“The land tax was the heaviest impost of the Imperial revenue system in operation. The underlying doctrine of the tax in India has been that it is of the nature of rent paid by the cultivator to the State in virtue of the theory that the land in India has from immemorial times been regarded as the property owned by the State. The cultivator is not the proprietor, but is the occupier of the land. The land is let to him and the State is therefore justified in claiming the whole of the economic rent arising from the land. On this assumption the land tax has been imposed irrespective of the question of necessity or justice” (Moon 1989).

Whatever may have been the reasons for augmenting the land tax, few can deny that a heavy consolidated impost on the first exertions of any species of industry absorbing the whole or nearly the whole of its profits in ruinous and impolitic. It becomes an effectual bar to the creation of that produce on which the future exertions might be profitably employed and through the medium of which individual wealth and public revenue may be increased to an almost inconceivable extent. A land tax of this nature was sure to blast the very production of that wealth which industry would have otherwise brought into being. Dr. Ambedkar points out to the fact of the land tax being so heavy that the system of tax prevailing in India might well have been called a near approach to the single tax system.
While on one hand, "The land tax prevented the prosperity of the agricultural industry, the customs taxes, on the other hand, hampered the manufactures of the country. There were internal customs and external customs, and both were equally injurious to trade and industry. The internal customs were made up of transit and town duties. For the purposes of transit duties the country was artificially divided into a number of small customs areas. Goods may be manufactured and consumed within each customs area, but the moment they left their own division they became liable to duty. The injurious effects of this regulation, though concealed, were none the less real. The transit duties held up trade, which in its turn reacted adversely on the manufacturers of the country. The adverse effect on the transit duties was also felt in another way. There existed also a territorial division of labour, otherwise called localisation of industry that formed a prominent feature of Indian economy. Under it each locality in India specialised in a particular art or industry; for instance, cotton was grown in one locality, woven in another, and bleached in a third place. But it often happened that these localities were situated in different customs areas, and a raw good might have had to pay the transit duty many a time before it reached its finished stage. To avoid this each locality was obliged to waste its energies along unprofitable lines in order to escape the transit duties" (Moon 1989).

As Ambedkar clearly explains- "The town duties, which formed a part of the internal customs, also worked in their effects towards deurbanisation. Commercial entry points are admittedly vast instruments of the trade of a country. The opportunity of ready purchase and sale of almost every kind of commodity in any quantity, accumulated capital, extended credit, general information all meet here as in a centre. They support, encourage and give lift to commerce and to the trade of a country. The direct effect of the town duty was to distract and drive away trade. Under the system, every article apart from being subject to the
payment of transit duty, also had to pay the town duty on the entry to the town. If there was any change of form due to manufacture within the town of entry, it could move to another neighbouring town only with a further duty being paid under the transit duty system in accordance to the increase of value it might have acquired from the labour and the skill bestowed upon it." (Moon 1989) And so all this led to the towns dwindling both in trade and industry owing to the fact that merchants stopped frequenting them and that no manufactures of articles subject to the transit duty were capable of being established in them except for their own supply.

"It was in this depressed condition that the Indian industries were called upon to meet foreign competitors. But the external customs cannot be said to have protected, much less fostered them. Dr. Ambedkar points out that the tariff was based on political rather than economic considerations. The Indian Import Tariff varied not with the nature of the imports but with the origin of the imports and the bottom on which they were shipped. Being political in character it was preferential in design and in its framework. It is to be regretted all the more that the preference involved an unmitigated loss to the people and to the government. It was excusable to have admitted into India. It must be noted that where goods of English origin were admitted into India and shipped on English bottoms at a rate half of what goods of foreign origin and shipped on foreign bottoms were charged with. However at the same time, British goods were let in India at lower rates than what the Indian goods had to pay under the internal customs; and this was done when England was prohibiting by high tariff the entry of India-made goods and India-built ships. Thus the customs laws internal and external blockaded trade and smothered industry. The comparatively paltry revenues derived from them are the best proof of their ruinous effects" (Moon 1989).
And when these resources failed the Government resorted to some very questionable means of raising revenue. "Justice in taxation was conspicuous by its absence and so the dagger was directed not where the blood was thickest but to that part of the body politic which on account of its weakness and poverty most meekly bore the pang. The landlords who lived their lives on the earnings of the poor tenants, or the European civil servants were supremely exempted from any contribution towards the maintenance of the Government. On the other hand the revenue was collected from the poor and continued to be a tool to harass the industrious poor. Though many of the petty and vexatious taxes prevalent under the native rule were abolished, the land tax continued to be consolidated and increased concurrently with, if not consequently upon, the abolition of such other taxes as being raised from the poor cost the Government more than their yield" (Moon 1989).

This injurious revenue system led to the decaying of the taxing capacity of the people so that notwithstanding its numerous resources from which it derived its revenues the Imperial Government was unable to make both ends meet. Dr. Ambedkar points out that when their revenue laws are harmful to the resources of the people the financiers must blame none but themselves for their empty treasury.

However, the expenditure on the other hand it must be noted has been that of the military expenditure The table shown by Dr. Ambedkar in his paper points out to the unparalleled fact of a country wasting between 52 to 80 per cent. of its precious little money on war services. So this expenditure, whether from the standpoint of public utility or private employment, did not benefit the population which contributed to the revenues of the State.
“The civil and political charges which absorbed nearly 10 per cent. of the revenue can hardly be said to be recuperative in their effect. This part of the expenditure again was not shared by the native population which bore its burden” (Moon 1989). Conquered and distrusted the natives since the commencement of British rule had come to be excluded from the higher administrative posts of the country. It was to remove this injustice that Parliament in the Act of 1833 provided that no native nor any natural-born subject of His Majesty, could by reason only of his religion, place of birth, descent, colour or any of them be disabled from holding any place, office, or employment under the said Company. But, as a matter of fact, till after the Mutiny not one of the natives was appointed to any office except such as they were eligible for as advised by the Court of Directors.

Thus the bulk of the money raised by injurious taxes was spent in unproductive ways. The agencies of war were cultivated in the name of peace, and they absorbed so much of the total funds that nothing practically was left for the agencies of progress. Education formed no part of the expenditure incurred and useful public works were lamentably few. Railways, canals for navigation or irrigation and other aids to the development of commerce and industry for a long time found no corner in the Imperial budget. As Dr. Ambedkar aptly comments, “There is a principle well known to farmers that constant cropping without manuring ends in the exhaustion of the soil. It is, however, capable of wider application, and had it been observed in the State economy of India the taxing capacity of the country would have grown to the benefit of the treasury and the people. Unfortunately it was lost upon the financiers of India to the detriment of both.” (Moon 1989).
As might be supposed, a strong Central Government of the kind established in 1833 was capable of effecting economy wherever possible. As a matter of fact, the centralisation was of the weakest kind. However, it was only de jure there was an Imperial system of administration. The de facto administration was conducted as though the primary units of executive government were the Provinces and that the Government of India was only a co-ordinating authority. This was obvious from a variety of circumstances. Though the laws that were passed by the Government of India were passed for the different provinces, the initiative in legislation still lay in the Provinces and that the Government of India was only a sanctioning authority. Each Province had its own customs, internal as well as external, a survival of their sovereign status and each Province continued to have its own Army. Notwithstanding centralisation, the account system still remained provincial, sustaining the sense of their financial independence. The work of administration and collection of revenue being still conducted by them, the provinces behaved as though they were the lawful authorities charged with the responsibilities of Government. This spirit of independence bred insubordination, and some especially Bombay and Madras provinces, resisted the attempts of the Government of India to tax the people under their jurisdiction when the cost of the mutiny compelled it to levy fresh burdens. Dr. Ambedkar points out that the Act of 1833 made an unfortunate divorce between the legal and administrative responsibility. The Imperial Government was responsible in law but did not administer the country. The converse was true for the provinces—the Provincial Governments administered the country but had no responsibility in law. This had a fatal effect on the economy in the finances of the country. Earlier before the Imperial system came into place, the Provincial Government was obliged to raise money for the charges included in their budgets and hence as a consequence they had to be economical. This was not the case now.
This led to the Provincial Governments making extravagant demands which the Government of India had often to yield; for, till very late, it did not possess the machinery to appraise the demands and to control the expenditure on them. There were many reasons to this. To begin with, the Imperial system in India was without its executive machinery of control. The Act which created it let there be a common Secretariat charged with the work of the two Governments of Bengal and India, thus leading to inefficiency creeping in. It was only in 1843 that a separate Secretariat was set up. Also, notwithstanding the establishment of the Imperial system of finance, the officers of audit and account remained attached to the Secretariats of the various Provincial Governments. They were not accountable to the supreme Government on whom the responsibility for the ordering and the management of the revenues of India had by law devolved. Secondly, the budget system, though good enough for the purposes of mercantile accounts, that is, record, was useless for the first and elementary purpose of all good State accounts, namely, check. The distribution of public money on the different services was not held to mean appropriation. “It was only treated as cash requirements. Owing to this fact the grants were never carefully prepared nor was the limit set on them observed in practice. It is evident that in the absence of an appropriation budget the primary object of all State accounts and audit, namely check on the spending authority to abide by the sanction, was never achieved. The Provincial Governments, extravagant in their demands, were also careless in the matter of expenditure. So long as the Government of India remained without an appropriation budget and a centralised system of audit and account, it continued to be only a titular authority in the matter of financial control. The provinces though by law being the weakest of authorities in financial matters, were really the masters of the situation”(Moon 1989).
"Under such a system nobody was a Chancellor of the Exchequer to urge economy, because everybody was supposed to be one. This led to finance in “being everybody’s business suffered from being nobody’s business”, so that funds were distributed not according to the genuine needs of the services, but according to the relative claims and persistency of the clamour made for them" (Moon 1989).

Dr. Ambedkar points out that though “The collapse of the Imperial system was due to a faulty fiscal system marked by injurious taxes and unproductive and extravagant expenditure, it must not, however, be supposed that this faulty fiscal policy commenced with the inauguration of the Imperial system. On the other hand, it was a heritage which descended to the Imperial system from the past. Non the less it is obvious that, a timely revision of the fiscal policy and the strengthening of central control would have solidified the foundation of the Imperial system. But a much too long continuance thereof undermined its financial foundations, and as it could get no more money to meet its rising expenditure from a people, whom it had beggared. The Imperial system succumbed to the shock of the Mutiny, never to rise again in its original grab(Moon 1989).

CHAPTER II
4A.4.1.2 Imperialism Vs. Federalism

The Mutiny of 1857 led to the collapse of the system, but the blame was put on the irresponsible extravagance it engendered in the Provincial Governments. This led to the substitution of the Imperial system for a Federal system so that the financial position of the Central authority in India be assimilated to that of the Central authority in the United States. The new plan was that each province could keep its revenues and meet its charges from them. The problem of responsibility was sought to be
solved here. Thus the Federal plan the consolidated Imperial Budget instead of its mere formal division between Imperial and Provincial was to be replaced by creating two distinct separate budgets, Central and Provincial, based on an actual and genuine division of services and allocation of revenues. This therefore actually helped set bounds to the extravagant expenditure of the Local Governments (by limiting the funds on which they were to draw), and also as a measure for setting bounds to the growing expenditure of the Central Government. Many federalists thought that by the vesting or the re-vesting of the powers of taxation to the Provincial Governments, they being regional players would be able to tap sources of revenue which have remained untapped by the Imperial government so far.

Thus the outlay on public works was in Bengal 1 3/4 per cent.; in North-Western Provinces, 2 1/2 per cent.; and in Madras a little over 1/2 per cent/of their respective revenues. However, this led to a favoured treatment of some provinces as against the others, which was justified by the Imperial Government, on the ground that the favoured provinces showed surpluses in their accounts. But many pointed that these deficits and surpluses ascribed to the different provinces were grossly fictitious as they were the result of a bad system of accounts. The system of accounting was continued to be the same as it was before 1833 when there was no common system of finance. Dr. Ambedkar gives an example of the Bombay Presidency here where he states that the reason for the presidency to show a deficit time and again was because the accounts system kept on charging the Presidency with the cost of the Indian Navy.

However, despite the merits of the Federal Plan shown by the federalists, when proposed, this Plan gave rise to a determined opposition by the supporters of the Imperial system who essentially were mostly military men in civil employ. Their arguments were based on that of practicability and expediency.
The question as asked by the Imperialists was whether to localise the revenues and charges of India as belonging distinctively to one particular province. Arguing in the same strain as the resources of British India should be considered in the aggregate and not with reference to the particular province in which it is raised. The Imperialists' arguments and the emphasis laid upon the difficulty of separating the revenues and charges into Imperial and Provincial, it must be conceded that the task was by no means so insuperable as the Imperialists made it out to be. In fact Dr. Ambedkar quotes Colonel Chesney who in response to the challenge thrown out by the Imperialists makes a notable attempt to distinguish the existing heads of charges into Imperial and Provincial in his book Indian Polity: “The items of Imperial expenditure for which contributions would be required consist apparently of: (1) the Home Establishment and charges disbursed by the Secretary of State; (2) interest on Indian debt; (3) Establishments of the Government of India; (4) Diplomatic establishment; (5) Army; (6) Imperial Services—Post Office and Telegraph Department; (7) interest guaranteed on railway capital; to which must be added (8) grants in aid to some of the poorer provinces (which do not at present pay their expenses).” (Moon 1989)

This made the Imperialists to shift their emphasis from the argument from practicability to that from expediency. Expediency furnished a better ground for attacking the Federal plan. They argued that it was the Imperial system with a strong power of control that had saved the country to the British from the hands of the mutineers of 1857. They did not fail to point that because the Imperial system of finance had given into the hands of the Imperial Government the control over the management of the revenues and disbursements of the Empire. This led to the Imperial Government be able to stimulate every source of income, in an emergency like the Mutiny, and close every avenue of outlet, and concentrate all its expenditure on the capital object at stake—
energetic prosecution of hostilities. It was also argued that the Central Government could not be able to maintain its prestige without centralisation in finance. It was this system of Imperial Finance which, having collected the leading strings in political and administrative matters into the hands of the Imperial Government, enabled that Government to dictate a policy and have it executed to its own satisfaction. Otherwise the Central Government would be nothing but a pensioner of the Local Governments subordinate to it.

It must be remembered at this point that Federalism was itself in its infancy. People sided with the Imperialist essentially because of the events and circumstances of that time. However Dr. Ambedkar notes that the Federalists lost a cause that was bound to succeed. "The Imperial Government had to be extricated from the state of chronic penury in which it had fallen, and if statesmanship did not favour the system of Federal Finance as a means, financiers soon learnt that the system of Imperial Finance was doubtful as an end." (Moon 1989)

CHAPTER III

4A.4.1.3 The Compromise: Imperial Finance without Imperial Management

However, the Federalists' cause was not lost as a whole. Their arguments led to the revising of the revenue laws and improving the machinery of control so that more revenues be obtained and less wastefully spent. Serious attempts were made to do away with the oppressive taxes which had so long retarded the prosperity of the people and consequently of the Government. As pointed out, "The internal custom duties were done away with, and the country was freed from all restrictions which hampered the growth of trade and industry. Positive encouragement was also given to them by introducing the element of
protection in the import tariff and trade was facilitated by equalising the 
duties on English and foreign shipping. Articles of export were relieved 
from the handicap of export duties and efforts were made to improve the 
cultivation and pressing of cotton, tea and other staples which 
commanded a great market in Europe and elsewhere." (Moon 1989)

The administrative machinery was next subjected to revision. The 
Indian Councils Act of 1861 led to the creation of a post of Chancellor of 
the Exchequer wherein a reputed financier, Mr. James Wilson was 
appointed. Mr. Wilson first directed all his attention to the improvements 
in the machinery of fiscal administration. Dr. Ambedkar gives the credit 
of establishing in India a uniform system of accounts, centralisation of 
civil and military audit, and the introduction of an appropriation budget 
to him. However, this did not lead to much change in the financial 
condition of India as the needs for expenditure were growing, and the 
economy in expenditure became difficult of achievement. The growing 
needs of improvements, till now neglected, and the contracting scope for 
economy, both together to demand an ever-increasing scale of taxation. 
The dangers of increased taxation were well known to all.

The Local Governments could be made to be economical in their 
ways only by giving them the power and responsibility of managing their 
own affairs. The financiers too found out as a matter of administrative 
experience that while some of the branches of revenue and expenditure 
were truly imperial, there was a wide field of both of them which was 
properly local in character, and ought to have been entrusted to Local 
Governments. As Dr. Ambedkar points out- "They were convinced that 
there could be no standard of economy until the requirements of the 
Local Government were made absolutely dependent upon known means, 
and nothing they thought would serve to make known to the Local 
Governments the means available for their outlay than to carve out from 
the Imperial purse a separate purse of definite magnitude for the use of
Local Governments and to throw on them the responsibility of meeting their demands and maintaining an equilibrium in their finance." (Moon 1989). The Federalists had concluded the same way too. But considering the opposition by the Imperialists it was necessary that it be made acceptable to them, and hence certain concessions were made without seriously compromising the working of the plan. It must be noted that the Federal plan necessitated a change in the constitution of the system of government in India and also a legal partition of the revenues and charges of India between the Central and the several Provincial Governments. Though everyone knew that the Plan would add responsibility, the concern lay in the fact that it would legally and permanently to divest the Central Government of the resources of India. As Dr. Ambedkar notes the financiers were "practical politicians" (Moon 1989) who found that there was no need to resort to a constitutional change as convention was deemed to be as good as law and, once established, can seldom be altered without disturbance. Separation of charges and revenues between the Central and Provincial Governments was therefore proposed to be made a matter of convention which could be upheld so long as it was profitable for the parties concerned to do so. This compromise between constitutional Imperialism and constitutional Federalism was essentially "Imperial finance without Imperial management."(Moon 1989) Here, the revenues and charges remained Imperial in their status, but their management was to be provincialised, so that each of the Provincial Governments was given to administer a part of the Imperial charges incurred in its territory within the limits of a part of the Imperial revenues collected within its territory. The essence of the Plan was retained. The only difference was in retaining to the Imperial Government the supreme controlling, counseling and regulating authority in all matters pertaining to Indian Finance, without its being actually engaged in the details of its administration.
Mr. Laing, the successor of Mr. Wilson, in order to promote the useful public works, led him to propose to the Provincial Governments a method of supplementing the scanty Imperial grants made to them. As Dr. Ambedkar puts it, his object was to enact local budgets "not merely to meet a temporary difficulty but to inaugurate a permanent improvement," (Moon 1989) to the relief of the Imperial treasury and the benefit of the Provincial Governments. This scheme involving the management of the public works charges by the Local Government with an allotment from the Imperial revenues supplemented by the power to tax had secured a general approval. However, in order to implement the scheme, at that time, the Local Government was without the requisite machinery for carrying into execution the powers of legislation necessary to impose the taxes proposed to be given to them. The postponement of the execution of the scheme pending the enactment of the other legislations led to it being dropped sine die consequently.

Mr. Massey revived the scheme in a much more enlarged form. He proposed that (as quoted by Dr. Ambedkar) (Moon 1989) "...my first object has been to select, for the first series of charges to be transferred to local authorities, those items of expenditure which being least susceptible of control by the Government of India, give as a whole, an amount of such dimensions as will not be difficult to manage, and yet will be of sufficient importance to indicate that the measure is intended to be a reality, and a step towards the more complete transfer of the financial administration to the local government. Taking the civil estimates... it seems to me, plainly, the most convenient method of proceeding to transfer a few entire grants or section of grants, in preference to selecting special items from several grants... By adopting the plan... no change whatever in the system of accounts will be called for; and the only alteration will be, that certain sections of the grants for various purposes, will be provided in a
special manner. The only exception to this rule... is in dealing with a head "Miscellaneous" which... is rather an incongruous collection of charges." (Moon 1989).

Without going into the details of the scheme, it must be noted that though it won the approval of cautious critics the scheme was too large for the Imperialists. And as the two greatest of them, Lord Lawrence, the Viceroy of India, and Lord Napier of Merchistoun, Governor of Madras, disapproved of it, it failed to materialise in consequence of their opposition. To put in Dr. Ambedkar's rather interesting words—"But unfortunately for the Imperialists, throughout this decade during which they were stubbornly objecting to any surgical operation on their patient—the Imperial system of Finance—it did not show any sign of convalescence. On the other hand, the delay in the operation aggravated its ills." (Moon 1989) Notwithstanding the constant enhancement in taxation and the reduction in expenditure, the three Chancellors of the Indian Exchequer sent from England could point to only three years of surplus during the decade between 1860 to 1870. The constant deficits led to the breakdown of the budget system that was in fact created to bring about order and economy in the public finances of the country. Speaking of its merits of expediency, the budget system due to excessive centralisation proved futile. The finances thus were nothing but chaos.

"Lord Mayo was convinced that there was something rotten in the system of Imperial Finance. While anxious not to end it, he courageously sought to mend the system by inaugurating the scheme of Provincial Finance" (Moon 1989).
PART II

4B.4.1 PROVINCIAL FINANCE: ITS DEVELOPMENT

4B.4.1.1 Introduction

In this Part II of the book, Dr. Ambedkar deals with the development of Provincial Finance. The arrangement of this part of the study differs from that of by Justice Ranade, what was adopted by him in his pamphlet published on the subject of Provincial Financial in 1887. To quote Dr. Ambedkar, “As will be seen from a perusal of Part II, one of the features of Provincial Finance was that the revenues and charges incorporated into the Provincial Budgets were revised every fifth year. Justice Ranade in his pamphlet, which simply covers the ground traversed in Part II of this study, and that too up to 1882 only, has taken this feature as a norm by which to mark off the different stages in the growth of Provincial Finance from one to another. Consequently, each quinquennial period to him becomes a stage, and in his hands the history of Provincial Finance falls into as many stages as the quinquenniums into which it can be divided... If we scan the history of Provincial Finance in British India with a view to discover the method of meeting the problem of equilibrium in Provincial Budgets and the changes introduced in it from time to time, we shall find that Provincial Finance has evolved through three different stages, each with its own mode of supply, namely, Assignments, Assigned Revenues and Shared Revenues. Consequently, instead of following the mechanical plan of Justice Ranade, it is believed to be more logical and instructive to divide the stages in the growth of Provincial finance according to the method of supply to the Provincial Governments adopted by the Government of India.” (Moon 1989)
Hence the Part II of this book is divided into three chapters namely: (1) Budget by Assignments- 1871-72 to 1876-77, (2) Budget by Assigned Revenues- 1877-78 to 1881-82, and (3) Budget by Shared Revenues- 1882-83 to 1920-21. It must be noted that this part presents the evidence of the empirical data and original analysis of Dr. Ambedkar. Therefore the original text of this part of Dr. Ambedkar's study has been provided in the appendix. This has been done so in order to provide the reader with a complete and clear picture of the empirical data as collected by Dr. Ambedkar. Moreover, this part of the work has been appreciated by Edwin R.A. Seligman in his foreword to this book.

PART III

4C.4.1 PROVINCIAL FINANCE: ITS MECHANISM

CHAPTER VII

4C.4.1.1 The Limitations Of Provincial Finance

In the start, Dr. Ambedkar points to the fact that it was in 1855 when local Finance dated its origin. There, however, were collections of local revenues such as Ferry Funds, Toll Funds, Cesses, etc., prior to 1855. But the point to be noted is that the balances from such funds were not carried to a separate account but were merged in the general balances of the country (only Bengal and North-Western Provinces were an exception such balances were carried to separate local Fund Accounts). It was by the Financial Resolution of May 11, 1855, that local Funds were completely separated from Imperial Funds thereby being treated as "Deposits". Subsequently by the September, 1863 Resolution, local Finance was established on a separate footing by the institution for each of the different provinces of a distinct local Fund Budget as separate from the Imperial Budget. The absence of local authorities led the
Government of India to entrust the task of the preparation and execution of the local Funds Budget to the respective Provincial Governments as being more in touch with local wants. This accident has led many to falsely believe that this was essentially Provincial Finance. Before 1870, the Local Funds were to be handled by the Provincial Governments as merely in a form of trust. This cannot be interpreted to mean the amount to be at their disposal (which if was the case, could be considered to have been Provincial Finance). It was only the Resolution of December 14, 1870, which instituted actually the scheme of Provincial Finance, though the terminology used was “Resolution on local Finance”.

Dr. Ambedkar then embarks on the study as to whether the system of Provincial Finance thus established in British India was independent in its organisation. For this the test of the freedom of budgeting and everything that is involved in it as an evidence of the existence of these powers is looked into. As he puts it, “Independent budget powers would involve the power to determine the services which, according to the needs of the country, a good government should undertake, and to decide upon the mode of raising either by taxation or loan sufficient money to meet the expenditure upon those services. Alongside these powers the budget system entails the obligation of keeping accounts and submitting them to independent audit.” (Moon 1989)

If you were to apply these tests to the Provincial Budget, it could be seen that the budget system introduced into India with regard to the different Provinces was accompanied by the most stringent limitations. They were given a budget without its powers, and they bore the obligations of accounts and audit just because they were left free within the limits of their budgets. He states that all this was part of the scheme and not without a purpose. Pointing out that complete understanding of
the operation of Provincial Finance in British India was not possible without a thorough knowledge of its rules of government. Dr. Ambedkar then goes on to analyse them.

The Rules of 1877 were essentially the basis of all those that were subsequently issued. With very small addenda or corrigenda they remained in force for a period of fifteen years, when they were superseded by a new series of Rules promulgated in 1892 and then again in 1897 and 1912. The 1912 rules were re-issued in 1916 and could be taken as laying down the final regulations of Provincial Finance.

Dr. Ambedkar points out that the reason for his going into the examination of the Rules is twofold: (1) to know what limitations there were and (2) why they were placed. Though the object was to see what the limitations were, the main reason was to get a proper understanding of the causes of the necessity for these limitations that knowledge of them is to be sought. While analysing the rules, he states that for a successful working of such a scheme, rules would have to be laid down for the purposes of defining the administrative and the financial powers of the Provincial Government. For a clearer understanding a further classification needs to be made. Therefore the Rules relating to Administrative Powers may be further subdivided into those pertaining to (i) Services and (ii) Staff. Similarly the Rules defining the Financial Powers may be conveniently grouped under the following subsidiary categories: Those (i) of a general nature and those pertaining to (ii) Provincial revenues (iii) Provincial Expenditure (iv) Budget Sanction and (v) Audit and Account.
Apart from these specific limitations the Provincial Governments were not altogether the free architects of their own destiny within the sphere allotted to them. The power of supervision and control in any Department continued to be rested in the Governor-General in Council. Furthermore, the Provincial Governments had kept him fully informed of their executive and financial proceedings so as to enable the Governor-General in Council to discharge its obligations for peace, order and good government. The general effect on the financial freedom of the Provinces was essentially to paralyse.

CHAPTER VIII
4C.4.1.2 The Nature of Provincial Finance

Dr. Ambedkar points out that the study of Provincial Finance cannot be said to be complete unless the question as to what was the resulting financial relationship under the old scheme between the Central and Provincial Governments in British India remains unanswered. With this in mind, he goes on to explain the exact nature of the system of Provincial Finance established in British India.

The commonly understood view was that the Indian system was based on a separation of sources between the Provincial and the Central Governments. Along with the fact that there was a separation of services, there also existed a separation of revenues between the Central and Provincial Governments in British India. The collection of most of the taxes in India by the agency of Provincial Governments makes one hold the latter view.
Dr. Ambedkar points out to another fact that must be noted. He says, "...reference must be made to the peculiar mode of presenting Indian Accounts adopted in official Blue Books...to the General Accounts of the Government of India is attached a supplementary account professing to show the distribution of the different heads of receipts and expenditure among the various Provinces into which British India has been divided. This mode of showing the accounts is beyond doubt misleading. It appears as if the aim was to show the financial position of the Provinces. But as a matter of fact the figures given in the columns in which the revenues and charges are shown in their provincial distribution do not represent the respective claims and responsibilities of the different Provinces. Far from showing the financial position of the Provinces, the figures in the columns merely represent the geographical distribution of the different agencies through which the financial business of the Government of India is conducted, and through which the revenues are collected and the expenditure is defrayed." (Moon 1989)

Citing an example of the Bombay Presidency, he states- "The revenue and expenditure, for instance, shown under "Bombay" represent the income and outgo which pass through the books of the Accountant General of the Government of India stationed at Bombay, and the same is true of entries under the heads of other Provincial Governments. The figures really represent the transactions of the Government of India distributed geographically, and there is nothing provincial about them in the least. However, such a system of account bears the impression that the system of finance in India is primarily Federal." (Moon 1989)

Dr. Ambedkar points that the proposals of changing the system of divided heads of revenue into one of complete separation supplemented in favour of the Central Government by contributions from the Provinces in the form of (1) a fixed sum revisable every few years, or (2) a lump percentage on provincial revenues, or (3) a fluctuating contribution from the provinces on their population, revenues or wealth, were all aimed at
reaching some such intelligible basis of distributing the burden of the Imperial exchequer as equality of payment or ability to pay. The Royal Commission on Decentralisation had in fact pointed that that equal contributions were not necessarily equitable contributions. However, Dr. Ambedkar points to the fact that “neither the Royal Commission on Decentralisation nor the Royal Commission on Indian Expenditure challenged the language which spoke of the Provinces as surrendering their revenues to make contributions to the Imperial treasury after paying for their services.” (Moon 1989) and hence it becomes imperative to examine the arguments based for the system was based on the principle of separation of sources and contributions from the yield.

An important question was how could one say that as to what is provincial. The administrative criterion would suggest that anything that a Province administered was provincial. But can this be a final criterion? As Dr. Ambedkar points out, it must be noted that “all regional rights of an administrative polity are in modern times exercised in the main, not in virtue of any social compact or the mere discharge of certain functions, but in virtue of a general law.” (Moon 1989). One can therefore answer the question with reference to the law that defined the status of the Provincial Governments in British India.

Here, he clearly points out that in the eye of the law all revenues including those provincialised still remained the constitutional possession of the Government of India. It is doubtful however whether the Government could have effected a legal separation by investing itself of the revenues of India in favour of the Provinces. This is due to a clause in the Parliamentary enactment, which vests the revenues of India in the Government of India which goes on to limit the legislative powers of the Government of India.
The Government of India had not made any legal separation of the title to the revenues. The Provincial Governments too were not allowed to establish their own treasuries to receive the collections from Provincialised revenues as the rules explicitly disallowed them from doing so. The intention of the Legislature can be clearly seen here wherein the possession of the revenues remained in the hands of the Government of India and the disbursement from the provincial revenues was carried out from the Imperial Treasury by the officers of the Imperial Government.

Dr. Ambedkar further points to the fact that the division of functions between the Central and Provincial Governments in India had no sanction in law and no legal responsibility attached to the provinces for any of the services, not even for those Provincialised. “The entire responsibility by law rested on the shoulders of the Imperial Government and it could not absolve itself of that responsibility by transferring it on to any of the Provinces. That the Provinces accepted the financial responsibility for some of the Imperial services was their choice.” (Moon 1989) Here, he cites the example of Madras which had refused to accept such responsibility in 1877. Hence it was the Government of India which was, by law, responsible for peace, order and good government in the country. All services were therefore essentially imperial in status, which were undertaken by the Government of India while discharging of its constitutional obligations.

It is further pointed that the view which posited that the relationship between the Central and Provincial Governments in British India was one of separation of sources and contributions from the yield was an untenable one. Unlike in the case of Federal Governments where the role of the state is pivotal, the Provincial Governments formed the weakest entities in the group of administrative polities functioning in India. The establishment of the Imperial system by the Act of 1833 led to
the crushing of the sovereignty of the Provinces that no trace of a truly federal element was left for a chance of a Federal structure to happen. Since then the government has entrusted the country to a single authority charged with the sole responsibility for the good government of the country. As no single administration could support the load of governing such a vast country, great powers were delegated to the Provincial Governments. But these were as Dr. Ambedkar points out, the "agents of the Government of India." (Moon 1989) In a-matter-of-factly way, the Provincial Governments had no legal powers or functions which polities designated as Governments have been known to possess. The Indian system of polity was actually just the opposite to the federal system of polity. It was a centralised system with nothing Provincial about it and what appeared Provincial was but the "regional aspect of the Imperial." One therefore cannot say that there existed a financial relationship between the Provincial and Central governments. To put in Dr. Ambedkar's words-"For here the Provinces had no separate resources which they lawfully owned, and could not therefore be spoken of as surrendering their revenues to make contributions to the Central Government after paying for what may be supposed to have been their own services-a supposition rigorously excluded by the law of the constitution."(Moon 1989).

In fact the limitations on the working of Provincial Finance as mentioned earlier in this chapter further showed that everything had remained imperial in status.

Dr. Ambedkar goes on to state that the only theory of financial relationship between the two governments, which accorded with facts and agreed with law, was that of aggregation of the sources and distribution of the yield. For as has been remarked before, all revenues whether assigned or reserved were collected into the Imperial treasury
and were thence paid out on all approved Government transactions. And so, if all the revenues are thrown into a common pool, it cannot be said that what the Provinces were given were revenues. The collections from all sources of revenue being inextricably mixed up, the only proper view is to say that what was given to the Provinces were funds. As Dr. Ambedkar says all the expressions “Budget by Assignments, Budget by Assigned or Shared Revenues are in a certain sense all fictitious phrases...The only proper expression, if it is to be true to facts, would be to say that Provincial Finances simply meant that the Government of India opened a Provincial Services Account in its Treasury books which varied with the yield of the Assigned or Shared Revenues and on which and to its extent only the Provincial Governments were permitted to draw.” (Moon 1989)

From all this it follows that instead of the Provinces contributing from their funds it was the Government of India, which distributed the yield of its taxes among the Provinces. The point to be noted as has been stated earlier consisted in the fact that the administrative and financial responsibility did not rest on one and the same authority, as should have been the case. The Provincial governments not having the obligation to find the money, tended to make extravagant demands, which the Government of India had to consider as it did not have the details, and hence was unable to judge of the true requirements of each service. The question of too much responsibility with too little trust was there. And so to avoid this Provincial Finance system was set up under which the Government of India that distributed its funds among the Provinces, and the Provinces in their turn undertook to manage some of the services which they administered for the Government of India within the sum which came to them severally out of this distribution.
Dr. Ambedkar points out that contributions must be according to ability, but distribution must be according to needs in order to make it equitable. But the distribution was not primarily among the Provinces, but among the various departments, whether controlled by the Government of India or by the Provincial Governments. This could make a considerable difference in the equity of the distribution. The distribution of funds by the Government of India was not based upon the Principle of each Province according to its needs but upon the principle of each department according to its needs. Thus interpreted, the system of Provincial Finance must strike as of the nature of as Dr. Ambedkar puts it Departmental Finance, something quite different from Decentralised Finance or Federal Finance. Here, in the case of Departmental Finance every Department of the State has a certain grant fixed for it in the Budget and it then draws upon the Treasury to the extent of the grant. In the same manner Provincial Governments were given a certain consolidated grant for the departments they managed and for the expense of which they were to draw upon the Imperial Treasury to the extent of the grant. Other than Provincial Finance, nothing was provincial in its status. The revenues, the services, the Civil Service, were as strictly Imperial in status after 1870, when Provincial Finance came into being, as they were before 1870, when there was no such thing as Provincial Finance in existence. Dr. Ambedkar states that "it is therefore no exaggeration to say that Provincial Finance, instead of being an independent system of Finance involving freedom to tax and freedom to spend, was only a matter of accounts, the operations on the debit and credit side of which were subject to stringent control on the part of the Government of India." (Moon 1989)

This shows that there was no change in the nature of the financial relationship between the Central and Provincial Governments as a result of the introduction of the scheme of Provincial Finance. It was a financial
counterpart of the Imperial system then established as the relationship of aggregation of sources and distribution of the yield was not a new one but was as old as 1833. However, Dr. Ambedkar points out to two important changes that were made as a result of the introduction of Provincial Finance:

1. "Before 1870 balances on all services lapsed to the Government of India at the close of the financial year. After 1870 all unspent balances on the services delegated to the management of Provincial Governments remained at their disposal and formed a part of their resources for the ensuing year.

2. Before 1870 Budget estimates on all services had to be sanctioned by the Government of India and the Provinces could not undertake any reappropriations between the different grants for the year, even if it was found necessary, without the previous sanction of the Government of India. After 1870 the Provinces were left to a greater extent free to distribute their expenditure in any way they thought proper among the various services delegated to their management, provided their total expenditure did not exceed the funds lying in the Imperial treasury to their credit respectively. But by the rules they were required to maintain all the services under their management in a state of administrative efficiency. Similarly after 1870 the Provincial Government had complete freedom which they never enjoyed before to carry on re-appropriations between the grants under their management without the sanction of the Government of India, provided their total expenditure did not exceed the amount budgeted for the year" (Moon 1989).
Likening to that of a joint Hindu family system, Dr. Ambedkar points out that “the revenues of India were jointly enjoyed by all the departments whether under Central or Provincial management without metes and bounds being fixed to the shares of any one of them. After 1870 the only change that took place consisted in the cesser of commensality and the fixing of metes and bounds to the shares of each in the common property according to their respective needs. The system remained a joint family system, although separate accounts were opened by the head of the family, namely the Government of India, to guard against any member overdrawning the amount placed to his credit.” (Moon 1989)

In 1870 in fact, the Provinces wanted freedom and the Government of India stability, but as Dr. Ambedkar puts it “none can assert that this compromise between Imperialism and Federalism was tried in vain.” (Moon 1989)

He further adds that “the importance of the large measure of stability derived from it be fully realised unless it is borne in mind how before 1870 the Government of India was left between the devil and the deep sea by having to refuse or to accept the bewildering demands ranging from dustbins for a Department to education for the people made by the Provinces on its not too large resources. The Provincial Governments had been saved the delay and the indignity in having to depend upon the Government of India for sanction of the meanest of their wants. The Imperial Government on the other hand was saved the fumbling task of scrutinising the most trivial of demands and grant or reject it, but always under the apprehension of having done wrong by acting either way. The system not only gave freedom to the Provinces and stability to the Government of India, but also had replaced the irresponsibility and extravagance which had proved the bane of the
Imperial System by economy and responsibility, for by setting bounds to the funds of the Provincial Governments the Government of India had ended in setting bounds to itself. These results, it is true, did not satisfy the critics of Provincial Finance. More in other directions was expected of it, but that could have been possible only if Provincial Finance was a system independent in its organisation. So long as Provincial Finance was a part of Imperial Finance, inseparably linked to it, it could have yielded no greater results than have followed from it, and those that have followed are by no means slight." (Moon 1989).

CHAPTER - IX
4C.4.1.3 The Enlargement of the Scope of Provincial Finance

Being the custodian of the funds, the Government of India did often put the consideration of Imperial Services above that for the Provincialised Services. However, with the shifting of emphasis on the competing needs of the Central and Provincial Governments the complaints on the score of unfair distribution of funds ceased, and no fear of an adverse revision remained when the settlements were declared permanent. There remained another objection to the system of Provincial Finance that the limitations imposed upon it tended to reduce the Provincial Government to a non-entity by restricting the scope of their activity within the field allotted to it.

The restriction on the Provinces with regard to the freedom to tax was particularly resented. Other limitations such as on the spending powers of the Provincial Governments in the matter of staff and establishments, creating new or abolishing old appointments or revising the establishments of their departments, and powers to make needful changes in the agencies which carried out the services managed by the
Provinces, etc were also questioned. Limitations such as the ones on the preparation and execution of the Provincial Budgets were a matter of concern.

In the matter of control over the preparation and execution of Provincial Budgets the Government of India urged that the scrutiny was not motivated by a desire to control an unwelcome policy, but was inevitable because of the three important ties by which the Provincial Budgets were bound up with the Budget of the Government of India. These were (1) the incorporation of the income and expenditure of the Provincial Governments into the Budget and the Annual Accounts of the Government of India as an integral part thereof; (2) the system of divided heads of revenue and expenditure, and (3) a common treasury involving a combined “ways and means” for the transaction of the Central and Provincial Governments. The first two points of inter-relation required that the Government of India should examine the Budget Estimates of the Provincial Governments. It was thought that this power was necessary to make such alterations was rendered as the local Governments had the tendency to over-estimate their expenditure and under-estimate their revenue. There was need, hence, for the Government of India to scrutinise the Provincial Estimates in order to preserve accuracy in the combined accounts. Besides the interests of accuracy, the Government of India had to ascertain by a scrutiny of their estimates that a Province did not impair the stability of its finances by (1) including in its budget expenditure on schemes which had not received due administrative sanction, or was not likely to receive such sanction in time to be incurred during the year; or (2) by entering on an enhanced scale of expenditure a Province was not unduly depleting its balances. Another fact was that in so far as some of the Heads of Accounts were shared, the ultimate result of the Central Budget, whether there was to be a surplus or deficit, depended upon the accuracy of the estimates. The
Government of India, it was urged, was thus directly interested in the Provincial Budgets, and could not have abandoned its right to scrutinise them without exposing its budgetary system to serious derangement. The third point of inter-relationship necessitated that the Provincial Governments should work within the grants as fixed finally by the Government of India. As Dr. Ambedkar points out, to have allowed the Provincial Governments the liberty to exceed the grants because they had ample balances to their credit would have been incompatible with the responsibility of the Imperial Government to provide the ways and means for the whole administration of the country. “A provincial balance, it was pointed out, was not a separate balance locked up in a separate provincial chest. It was a part of the general balances on which the Government of India operated daily. If a sudden demand uncontemplated in the Budget were to be made upon these balances, as would have been the case if the Provincial Governments had exceeded their budget grants, it would have disturbed the ways and means transaction and would have involved the Government into insolvency by causing insufficiency of cash.” (Moon 1989).

It is reasonable to centralise such powers as could not be efficiently exercised otherwise. However, on the other hand it is equally unreasonable to centralise powers where central control or uniformity is not clearly essential or is impracticable. Many a time centralisation in fact makes all progress to be retarded, all initiative liable to be checked and the greatly impairs sense of responsibility of local Authorities. It is further pointed out that “centralisation conflicts with what may be regarded as a cardinal principle of good government, namely, that when administrative business reached an authority fully competent to deal with it, that authority should deal with it finally. Even when there is a higher authority equally competent, to pass the business on to it would at best help to transfer power to the hands of the lower ranks of the official hierarchy, by causing congestion of business in the Central
Department." (Moon 1989). This shows that centralisation may lead to inefficiency. Therefore, considering India with all the various conditions prevailing in the different Provinces, the Central Government became an authority less competent to deal with matters of provincial administration than the Provincial Governments, who would have been more aware of the situation at the ground level.

However, the point put forward by the other side was so long as the Government of India remained the authority solely responsible to Parliament it was reasonable to hold that it should be the controlling authority in all matters pertaining to the administration of the country. But as Dr. Ambedkar points out, "it was equally reasonable to ask whether it would not have been possible in the interests of cordiality between the Central and Provincial Governments to have relaxed such of the restrictions on the financial powers of the Provinces as would not have been incompatible with the due discharge by the former of its own responsibilities." (Moon 1989) To the question as to whether it was possible to enlarge the scope of Provincial Finance by a relaxation of the limitations without injury to the position of the Government of India was evident from the suggestions made by the Provincial Governments:


2. Power of sanctioning expenditure on Staff and Establishments up to a limit higher than that allowed by the Government of India.

3. Separation of Provincial Estimates from the Imperial Budget and Accounts.

4. Abolition of the system of divided heads of revenue and expenditure and the replacement of it by a system of separation of sources and contributions from the yield.

5. Power to spend part of their balances up to a defined amount, without the previous sanction of the Government of India in meeting an excess of expenditure over Budget Estimates" (Moon 1989).
Dr. Ambedkar analyses each of these suggestions. He states that to suggest, as did the Government of India, that the Provincial Governments would abuse these powers to the extent of causing discontent or jeopardising the stability of their financial system, was to believe that such legally recognised polities as the Provincial Governments were run by incompetent administrators unmindful of their obligations.

The second demand could have been granted with greater ease. Each Province has had its own separate “Provincial” and “Subordinate” Services, but while it has a free hand in recruiting for the latter, appointments to the former have been regulated by rules laid down by the Government of India. That being the case it would have been only logical that the Government which had the power of recruiting for an appointment should also have the power of regulating the salary. A local Government knows better the economic value of a local man, and should therefore have been trusted with powers up to a limit covered by the Provincial and Subordinate Services. The suggestion of the Government of India that the grant of such powers would have resulted in heavy additions to the recurring expenditure of a Province should also be accepted.

“The acceptance of the third recommendation could not have affected the responsibility of the Government of India. The only objection which the Government of India urged was that such a separation would have been unwise. To have published accounts or estimates of the Imperial Government which excluded the accounts of the Provincial Governments, when the items excluded covered such a large magnitude, would have misled the public and rendered a wholly incomplete idea of the financial position of the Government of India” (Moon 1989). But as Dr. Ambedkar points out, “the Provincial Budget as framed by the
Accountant General was passed by the Provincial Government and no more reference was required to the Government of India except to inform it that the estimate was a probable one and that it was within the limits of the revenues assigned to the Province. It is therefore obvious that there could not have been any constitutional objection to the granting of the demand for a separation of accounts.” (Moon 1989)

The fourth recommendation with regard to the abolition of the divided heads of revenue would have clearly eliminated the interference of the Government of India in the preparation of the Budget Estimates by the Provinces. The substitution of a system of separation of sources and contributions from the yield for the system of divided heads would have clearly resulted in a greater freedom to the Provincial Governments, without any evil consequence to the Government of India. The objections that the Government of India was able to oppose to this demand were, as Dr. Ambedkar puts it, far from convincing. It was urged that the Provincial Governments under complete separation might cease to take such interest as it took in respect of revenues, which were divided. Dr. Ambedkar clearly points that it is evidently a mistaken view that a Provincial Government could not have been trusted to administer a tax efficiently unless it had a financial interest in the result. Besides it was overlooked that the fact that the divided heads gave a personal interest to the Provincial Governments was indeed a point against the system rather than in favour of it. “A system which created a vested interest in a revenue apart from the interest of the public was a bad system, for such an interest was sure to lead to harshness and rigidity in collection.” (Moon 1989) Dr. Ambedkar further states that “If humanising the Provincial Governments was a desirable end, then the abolition of divided heads was a good means.” (Moon 1989) The other objection of the Government of India was that such a change would have given the share
of the Government of India from the revenues raised in the provinces the character of a tribute, and the Government of India would have appeared to be the pensioner of the Provincial Governments, depending upon them rather than controlling them. Dr. Ambedkar rules out this objection as being sentimental.

The fifth and the last suggestion for the enlargement of the scope of Provincial Finance countered by Dr. Ambedkar by a simple fact that "the demand of the Provincial Governments did not ask for a complete separation of Provincial balances from the balances of the Central Government involving separate treasury system and separate ways and means, probably because they anticipated that as such a proposal meant separate possession of provincial revenues the Government of India would raise a constitutional objection to such a demand. All they asked for was a power to spend part of their balances up to a defined amount without reference to the Government of India." (Moon 1989).

It is, hence, clearly shown that "The scope of Provincial Finance was unduly restricted by a too narrow and too legalistic an interpretation of the constitutional obligations of the Government of India. From the above analysis of the suggestions made by the Provincial Governments it is clear that without making any breach in the constitutional position of the Government of India it would have been possible" (Moon 1989). To effect the changes they desired. Dr. Ambedkar argues that such concessions would, in fact have made Provincial Finance as self-sufficient and as autonomous as it was capable of being made. "The system would no doubt have rested on pure convention: none the less its benefits would have been as real as though it was based on law." (Moon 1989)
But "The time had arrived when the financial arrangements could no longer be looked upon as a matter, which concerned the Central and Provincial Governments. The Indian taxpayer came about as a third party who could not be ignored that it now "compelled the powers that be to alter the system so as to permit him to take the part he claimed to play." (Moon 1989)

PART IV

4D.4.1 Provincial Finance Under The Government of India Act of 1919

CHAPTER X

4D.4.1.1 The Necessity For A Change

Among the two types of governmental systems, the Presidential and Parliamentary the Parliamentary Government demonstrated its supreme virtue in securing orderly progress even though it was originally developed as an accident in the evolution of the British Constitution. And now it has been most eagerly adopted as the most fundamental institution by many countries whose political convulsions have required them to prepare anew or alter the existing framework of their governmental systems.

If the fact of the Executive being a part of the Legislature were a sufficient indication of the Parliamentary type of government, then the system of government in India since 1853 may be said to be analogous to the Parliamentary system. But judged in the light of its de facto consequences the Indian system falls lamentably below the de jure connotation of the class of governmental systems to which it belonged. If in other countries the record of Parliamentary government is one of
submission of the Executive to the Legislature, in India it had been one of the Executive thwarting, often of flouting, the legislature. Many a time in fact the Executive ever paying deference to the wishes of the people. As Dr. Ambedkar puts it, "Reforms have been incessantly, asked for by the legislature only to be denied with equal tenacity by the Executive." (Moon 1989)

The reason for this is that it was a Parliamentary system without a Parliamentary Executive. In other words, the Executive under the system was not responsible to the legislature and was not removable by it. The Indian Legislature could neither make nor unmake the Indian Executive.

"As a matter of fact neither was the Secretary, though all-powerful in Indian affairs, inclined to restrain the Executive in India from doing what the people regarded as evil nor to constrain it to do what he thought to be for the good of the people. Hardly can it be said that the British Parliament, wherein every member has been supposed to be a member for India, has made the acts of the Indian Executive a matter of anxious scrutiny" (Moon 1989).

The salary of the Secretary of State for India being paid out of the revenues of India, the Parliament too, had no occasion, as it had in the case of the Colonial Secretary, to annually review his actions in the full activity of the parliamentary Session. However, later by the provision of the Government of India Act of 1919 the House has a better opportunity to criticise Indian affairs owing to the salary of the Secretary of State having been placed on the British Estimates.

"It is therefore evident that the control of the Secretary of State and of Parliament over the Executive in India was only a nominal control, and the Indian Executive was in reality an uncontrolled body of bureaucrats
in the exclusive charge of Indian affairs. And Dr. Ambedkar aptly sums it up by saying "the Indian Executive has sacrificed progress to order." (Moon 1989) He points out that "so religious has been the regard of the Executive for the preservation of the personal law, notwithstanding the fact that it has disabled millions of its subjects from enjoying the most elementary rights of citizenship, that it has been careful not to allow in cases of conflict the rational provisions of the civil law to override or chasten the irrational rulings of that archaic code. Also, in the matter of securing economic rights its response was of a very halting character, and the legislation it has been persuaded to undertake for giving security or fixity of tenure to the agricultural or ease and comfort to the industrial population sank in comparison to what it refused to undertake for liberating the rest from a species of industrial slavery notwithstanding incessant demands for its abolition."(Moon 1989).

Its financial system was similarly characterized by the desire to preserve peace and order by taxing the masses and exempting the classes. It has been urged that the revenue system be so altered as to give relief to the poorer classes. The damaging character of the salt tax in India was called for as a sufficient ground for its elimination from the revenue system of India. "But not only did the Executive refuse to accept the demand, it actually increased the salt tax whenever a deficit has occurred instead of tapping some other source of revenue, which it could have done with equal ease and greater justice" (Moon 1989).

But the salt tax is not the only instance of inequity under which the masses paid for the classes. The land revenue as it has been levied in India may be cited as another example of inequity in the Indian Tax System. The sources of inequity are various. The system, as Dr. Ambedkar puts it, "in undertaking to tax per unit of land, taxes the poor
peasant with only one acre to cultivate and the landlord owing hundreds of acres at a uniform rate without realising that as the total incomes of the two must be vastly different this uniformity of taxation must produce a glaring inequity of treatment as between the rich and the poor." (Moon 1989). If the revenue thus raised by sacrificing equity to the dictates of order had been spent on services promoting progress there would have been some compensation. But such was not the case.

And to top it all, the revenue that was collected was spent on Services such as Police, Military and Administration and services such as Education, State aid to industries, were no where to be found in the scheme of things.

The point is that an irresponsible government, however sovereign, is incapable of progress, for in the exercise of its sovereign powers it is hampered by two very serious limitations. There is first of all the internal limitation, which arises from the character, motives and interests of those who are in power. Dr. Ambedkar states, “…the Executive in India did not do certain things most conducive to progress it was because by reason of its being impersonal and also by reason of its character, motives and interests it could not sympathise with the living forces operating in the Indian Society, was not charged with its wants, its pains, its cravings and its desires, was inimical to its aspirations, did not advance Education, disfavoured Swadeshi or snapped at anything that smacked of nationalism, it was because all these things went against its grain. But, an irresponsible government is powerless to do even such things, as it may like to do. For its authority is limited by the possibility of external resistance. There are things which it would do but dare not do for the fear of provoking thereby resistance to its authority... For the same reason the Government of India dared not abolish the caste system,
prescribe monogamy, alter the laws of succession, legalise intermarriage or venture to tax the tea planters. Progress involves interference with the existing code of social life and interference is likely to cause resistance.” (Moon 1989)

The gist of the matter as stated by Dr. Ambedkar is that the irresponsible Executive which had been in power in India was paralysed between these two limitations on its authority and much of what went to make life good was held up. Part of the programme it would not undertake and the other part it could not undertake. As a result of this, so far as the moral and social life of the people was concerned, the change of government by the Moghuls to a government by the British was only a change of rulers rather than a change of system.

The Executive had, coupled with the large grants of these discretionary powers to suppress the liberties of the people in order to preserve law and order, the gift of an equally generous measure of immunity to its agents in carrying out those powers. The right of public meeting was suppressed in the same manner and with the same sternness as was the right to personal freedom and the right to freedom of discussion; for, over and above the restrictive provisions contained in the ordinary law of the land, the executive armed itself with discretionary powers under a special enactment to prohibit any public meeting on the excuse of what it regarded as the interest of the public. There is no wonder then if such discretionary powers, exercised extra-judicially, substituted a reign of terror in place of a regime of peace.

A Legislature as distinct from the Executive was first inaugurated in 1853. But in 1861, “The constitution of the Legislature then established was altered. The ground urged was that that Legislature was not a body representative of the Indian people. Its members were drawn
from the official class representing the several Provincial Governments. In order to make the Legislature representative of the people, the Act of 1861 directed that it should be composed of nominated members chosen by the Governor-General from among the public, of course on the advice of the Executive. Again, by the Act of 1892 the Governor-General was directed to nominate such persons to the Legislature as were selected by public bodies in the country. These changes in the constitution of the Legislature appear to be aimed at liberalising it. As the legislature gained in its representative character it lost in its controlling power. The powers exercised by the Legislature under the Act of 1853 were far vaster than anything possessed by the Legislature under the Act of 1861. From 1861 the legislature met only for legislative purposes. As a consequence of this limitation the Legislature was debarred from asking a question, moving a resolution or dividing on the Budget. During the first thirty years of its existence the legislature did not even discuss the annual budget on more than sixteen occasions, and that too because some new tax legislation had been called for, and which the Executive could always carry through with the help of the nominated official block as it did every other kind of legislation it deemed necessary. The right of discussing the annual financial statement and the right of asking questions in regard to matters were first conceded to the legislature by the Rules of Procedure framed under the Indian Councils Act of 1892. But it may be doubted whether these concessions of powers to the Legislature amount to a restoration of the position which it occupied and dominance it exercised under the Act of 1853" (Moon 1989).

Before 1909 whatever conflict there was manifested outside the Legislature. By the reforms of 1909, however, an attempt was made to make the Legislature independent and at the same time to muzzle it. This attempt, ingenious as it was, only served to bring to the surface the deep-seated conflict between the Executive and the forces agitating the minds of the people. Election procedure or business procedure governing a
legislature is, in the words of Prof. Redlich (as quoted by Dr. Ambedkar), as it were a political pressure gauge, indicating the tension in the parliamentary machine and thence in the whole organism of the State. It is possible that this pressure gauge in the first instance may either be badly constructed or may become worn out so as to give a false reading of the actual tension. But so long as the members of the legislature derived their mandates from the Executive, owing to the fact that all of them were nominated members, such an artifice worked well, with the entry of the elected members holding their mandates from the people, the weakness of the artifice became evident.

As a result of the realisation of this fact that the Legislature with its limited powers was found to be an insufficient safety valve those who had given their thoughts to the political reconstruction of the country agreed that a mere reform of the procedure will not do. Only a reform of the constitution will save the state from anarchy. The Congress-League-Scheme which arose from this realisation, was merely increased the Indian element in the Executive and the Legislature, and added provisions aimed at converting advice into control without comprehending what was to happen if the Executive refused to be bound by the wishes of the Legislature. “The essence of the project was an Executive with a divided mandate legally responsible to Parliament, and practically to an elected Legislature. Such a separation of mandates, it was obvious, would have enabled the Legislature to paralyse the Executive without having power to remove it. Being without any constitutional means to change the Legislature in cases of conflict by an appeal to the Electorate it would have been obliged to carry on the Government even where it did not respect the wishes of the Legislature” (Moon 1989). Dr. Ambedkar argues though that “The scheme was unsound, like all previous attempts at the reform of the Indian Constitution, because in it the Executive and the legislature derived their mandates from and were responsible to different powers. It was unsound
because it overlooked the possibility that two mandates may not agree, in which case there would be a conflict. That conflict is inherent in a non-parliamentary executive. Some form of a Parliamentary government with a Parliamentary executive was the only way of avoiding it" (Moon 1989).

The announcement of August 20, 1917 heralds a new chapter altogether, Dr. Ambedkar points out. “Under the new conception the aim was to endow the Legislature with the power to make or unmake the government, so that it would be not only a government of the people and for the people, but by the people. The adoption of such a change of policy in the basis of the political institutions of the country involved far-reaching changes in their relations with one another, administrative, legislative and financial. The changes in the system of Provincial Finance introduced in consequence of the Reforms Act of 1919 were not caused by any inherent defects in the system as it stood at that date. On the other hand, the system was eminently workable. They were effected because the system as a whole was inconsistent with the great revolution which that Act had sought to effect in the governmental system of that country” (Moon 1989).

CHAPTER XI

4D.4.1.2 The Nature of A Change

Dr. Ambedkar analyses the announcement of the August 20, 1917 declaration of which he spoke of the future government of India and of the survey of the Montague-Chelmsford Report regarding it. Dr. Ambedkar observes, “One of the merits of that Report consisted in showing that the Congress-League-Scheme of political reforms did not embody the principle for the recognition of which they were agitating so long. Instead of inaugurating a responsible government in India, the scheme would have saddled the country with a non-parliamentary
executive under a parliamentary system of government. The Congress-League politicians abandoned their scheme in favour of the proposals contained in the Joint Report. But in their turn they demanded the introduction of a more or less complete responsible government in most of the political institutions at one stroke. But the framers of the new constitution pointed out that the emphasis on the word progressive in the announcement was as great if not greater than the emphasis laid on the word responsible.” (Moon 1989).

While dealing with the ‘progressive realisation of responsible government as the goal’, Dr. Ambedkar comments on the then Central and Provincial Governments: “The Provincial Governments in India, like the Central Government, were irresponsible governments. The changes made in the constitution of Provincial Legislatures were of the same nature as the changes in the Central Legislature, in that both were calculated to enable the Executive to consult the Legislature without being amenable to its control.” (Moon 1989)

From these differences in the constitution and procedure of the Central and Provincial Governments, it must not be supposed that the provincial Governments were less irresponsible with regard to their Legislatures than the Central Government was with regard to its own Legislature. The fact that since 1909 there was no majority of official members in the Provincial Legislature as there was in the Central Legislature was a matter of no moment so far as its practical consequences to the Executive were concerned; for it is to be remembered that in practice the difference between nominated members from among the non-officials and the official members was only superficial. Both had their mandate from the government who gave them their seats in the Legislature, and as nominees of the Government they voted for the Government, so that, though not in theory, in practice the Provincial Government had as much a standing majority in Legislatures as the
Central Government had in theory as well as in practice. Nor did the budget procedure of the Provincial Government mark any decided improvement over that adopted in the Central Government in the matter of giving greater control to the Legislature over the Executive. In both cases the aim was to give the members of the Legislature the privilege of discussing beforehand the question of such alteration with reference to the necessities of the Budget, only in the case of the Provincial Budget this privilege was allowed to be exercised at an earlier stage than in the case of the Imperial Budget. But considering that the Resolutions of the Legislature on the Provincial Budget, as those of the Central Legislature on the Imperial, were only recommendations to their respective Executives, this difference between the Budget procedure of the two Governments did not impose any greater control over the one Executive than it did on the other. As Dr. Ambedkar points out, "the Provincial Government could always restrict the scope of this Budget Committee by transferring any head from the class of non-obligatory expenditure to the class of obligatory expenditure. Besides this, the operation of certain other rules of Budget procedure based upon general principles of public finance tended directly to restrict the powers of the committee to put forth schemes of alternative or additional expenditure. It was rightly provided that schemes involving recurring expenditure could only be proposed with due regard to the rate of growth of recurring revenues and recurring expenditure." (Moon 1989) Owing to this rule, the committee had to drop proposals which involved recurring expenditure, but which were desirable from its standpoint. On the other hand, similar proposals made by the Executive could be easily carried through by the device freely adopted of obtaining previous sanction of the Government of India. "The consequence was that in all the Provincial Budgets presented under the new rules the amount of this "unallotted" fund left to the discretion of the committee bore too insignificant a proportion to the total expenditure in the budget to make the Provincial Executive in any real degree amenable to the Provincial legislature." (Moon 1989).
No really responsible government could, however, be introduced in the provinces without first of all making a complete change in the mutual relations between the Central Government and the different Provincial Governments in India. The relation between the Central Government and the different Provincial Governments in India, which existed before the passing of the Act of 1919 was one of complete subordination of provincial Governments to the Central Government. In this bond of subordination Dr. Ambedkar goes on to discern three strands—legislative, financial, and administrative. Of these it has been seen as to how tight was the financial strand was. The Government of India's control over revenues and expenditure was derived from Parliamentary Statutes which treated the revenues of India as one and applied them to the purposes of the Government of India as a whole. It is true that this provision was not so strictly construed as absolutely to prevent the appropriation of particular sources of income to specific purposes all-India or provincial. Or else the development of the provincial system of finance would have been impossible. But it certainly had the effect of denying to Provincial Governments any inherent legal right to the revenues which they raised. The Government of India completely controlled taxation imposed in British India, apart from the local taxes which were raised by local bodies. Taxation could only be levied by law, but the law had forbidden a Provincial Legislature, without the previous sanction of the Government of India, to consider “any law affecting the public debt of India or the customs duties or any other tax or duty for the time being in force and imposed by the authority of the Governor-General in Council for the general purposes of the Government of India.” (Moon 1989)
The law would not inhibit a provincial legislature from exploiting for provincial purposes any new source of taxation which it had the ingenuity to discover. But even in that case the project would, before being translated into action, have to secure the assent of the Finance Department of the Government of India, which would not give its sanction without considering closely if it trespassed on the Central Government's sources of taxation.

As Dr. Ambedkar points out, "Even within the prescribed limits of Provincial Finance the Provincial Governments were not free from the control of the Central Government. Because the provincial settlements were based not on provincial revenues but on provincial needs, a central control was inevitable. The Government of India could not allow a Province to go bankrupt. But if the Government of India were responsible for provincial solvency they must be in a position to control provincial expenditure. Again, as regards revenues, so long as the Government of India took a share in the proceeds they had a strong motive not only in interfering in the Budget estimates of the provinces, but also in interfering in details of administration. To give an example, their interest in land revenue, inevitably led them to close supervision over revenue settlements, and the control tended to become tighter in cases where expansion and development of a source of revenue, such as irrigation, depended on capital outlay" (Moon 1989).

The legislative powers of the Provincial Governments had in the same manner been made subject to statutory restrictions. There was no doubt an extensive field in which, so far as the substantive provisions of the Statute were concerned, the legislative competence of the provincial Legislatures was legally unfettered. Actually, however, the power of the local legislatures was curtailed in two ways. In the first place, considering that the Provincial Legislatures were younger institutions than the Central Legislature of the Governor-General, a great part of the field were
covered by the concurrent power of legislation. But the field remaining open for Provincial Governments in the matter of legislation was further restricted by the fact that the power of the Secretary of State and Parliament to control all-Indian legislation was made operative by means of executive directions” (Moon 1989). This necessitated the Provincial Governments to submit for the previous sanction of the Government of India and the Secretary of State all their projects for legislation before introduction. Furthermore, the Government of India by directions to the Provincial Governments was in a position to control all private provincial legislation almost as effectively as the Provincial Government’s Bills.

With regard to administrative matters too, every Provincial Government was by law required to obey the orders of the Government of India and keep that Government constantly and diligently informed of its proceedings and of all matters which ought, to be reported to that Government. Apart from this, the provincial Governments were not free to initiate any new policy too. It was the Government of India that regarded itself as distinctly charged with the duty of framing policy and inspiring reforms for the whole of India by issuing new orders. Cleverly enough, to see to it that these orders were effective, they were often accompanied by handsome grants to Provincial Governments strictly earmarked for the purpose of pushing on some particular feature of the new policy.

This led to no responsible government being there in the Provinces as “no government can be made to serve two masters at one and the same time.” (Moon 1989) Dr. Ambedkar gives an example of an occasion during the currency of the Morley-Minto Reforms when the Government of Bombay were unsuccessful in their endeavours to persuade the Government of India to sanction certain charges affecting the educational staff. The proposals adopted by a resolution moved in the Bombay
Legislature. The Bombay Government thereupon accepted the resolution which was carried unanimously, and once more put forward their proposals to the Government of India on the ground that they had the Legislature's entire support. But the Government of India and the Secretary of State held that these tactics were out of order and that it was "the duty of the Local Government in dealing with the resolutions to uphold with all their authority the decision of the Government of India," (Moon 1989) and hence it had to the resolution even if it agreed with the Legislature in the principle thereof.

As Dr. Ambedkar clearly points out it was the strong ties of subordination which bound the Provinces to the Central Government were therefore the chief obstacles in the path of Provincial autonomy. In order that the Provincial Government be made subject to Provincial Legislatures, the first thing to do was to curtail the powers which the Government of India possessed of interference in provincial finance, provincial legislation, and provincial administration.

The recommendations of the Functions Committee appointed to make a division between all-India and Provincial subjects, were with minor amendments embodied in what are called Devolution Rules under section 45A of the Government of India Act of 1919. These rules gave effect to the policy of responsible government and are made a part of the constitutional law of the land. The subjects devolving upon the Provinces became the services over which the Provinces gained an acknowledged authority of their own such as they never had before 1833 and were known to be Provincial subjects.
The second task that of allocating the revenue resources between the Central and provincial Governments were a comparatively difficult one. The first step in that direction was therefore to abolish the system of "divided heads" or budget by shared revenues. This was especially as there was a consensus that this system, as long as it gave a handle to the Central Government to interfere in the domestic affairs of the Provinces, was a source of friction and was evidently incompatible with provincial independence. But difficulties persisted in this new arrangement. With regard to the disposal of dividend heads, the question was as to whom should they be handed over.

Also, when all the existing sources of revenue were completely distributed between the Central and Provincial Governments as proposed, it becomes inevitable that a deficit in the Budget of the Government of India is created. The question as to how to make up this deficit was therefore the second difficulty that was involved in replacing the system of divided heads by a system of separate heads of revenue.

"For the consummation of its plan the Committee held that the augmentation of Provincial Surpluses was an essential step. Without it, the task was deemed to be futile. The only way to augment the provincial surplus was to allocate some other source of Imperial revenue in addition to those already provincialised. The deficit the Committee accepted in the year 1921-2 was to be contributed by each of the nine Provinces. This ratio of initial contributions was not intended in any manner by the Committee "to represent the ideal scale on which the Provinces should have in equity to be called upon to contribute." (Moon 1989) The Committee recognised that "an initial ratio of this nature can only be defended as a measure of transition. It is necessary, but it is necessary only in order to give time to the provinces to adjust their budgets to a
new state of affairs; and we are clearly of opinion that no scheme of contribution can be satisfactory that does not provide for a more equitable distribution of the burden of the deficit within a reasonable time.” (Moon 1989)

Dr. Ambedkar points out to the fact that the Committee proceeded next to consider the question of standard contributions as distinguished from initial contributions, which were only transitional. As to what should be the ideal basis for such an equitable distribution of the burden, the Committee stated that “to do equity between the provinces, it is necessary that the total contribution of each to the purse of the Government of India should be proportionate to its capacity to contribute.” (Moon 1989) Here, Dr. Ambedkar raises two questions. One is as to what is the total contribution of a province to the purse of the Government of India and the other as to what is the measure of the capacity of a Province to contribute. To the first, the Committee answers as Dr. Ambedkar puts it “the pressure of the taxes from within its jurisdiction for the benefit of the Central Government.” With regard to the second the Committee held that “the capacity of a Province to contribute is its taxable capacity, which is the sum of the incomes of its taxpayers, or the average income of its taxpayers multiplied by their number.” (Moon 1989).

The Committee therefore proposed that contributions should be made on the standard ratio to any deficit that there may be in the seventh year of contribution, and that the process of transition from the initial to the standard ratio should be continuous beginning in the second year of contribution, and proceeding in six equal annual steps. Though the recommendations were accepted by the Government of India and the Secretary of State, later it was believed that the dissatisfaction as the proposals have aroused is inevitable in distributing resources
between a Central and Provincial Governments. Such dissatisfaction was impossible to be removed easily; but still it was desirable on the grounds of policy, to alleviate the disappointment caused by the restraints that the system of contribution laid on the employment by the provinces of their revenues.

Dr. Ambedkar looks into two other matters, which had to be settled in order to make the separation between Provincial and Central Finance as complete as possible. Both were connected with capital transactions. One was with regard to the Provincial Loan Account. This Account represented the fund from which Provincial Government advanced agricultural loans, loans to indebted landholders, to municipalities and other local bodies, etc. The capital was provided by the Government of India as required and was returned to it as it was repaid. It was commonly agreed that it was the natural result of the Reforms Scheme that the Provinces should for the future finance their own loan transactions, and that joint accounts of this nature between them and the Government of India should be wound up as quickly as possible. The other was the question of responsibility for capital expenditure on irrigation works. In this as in the matter of Provincial Loan Account, it was agreed that it would be incompatible with the scheme of complete separation of Provincial Finance to hand over to the former the control of irrigation works and to make the latter responsible for the capital transaction incurred thereon.

This essentially broke the financial and administrative strand that tied the Provincial Governments to the Central Government and prevented a responsible government to fall in place. As Dr. Ambedkar puts it, the Provinces thereby acquired 'an acknowledged authority of their own' (Moon 1989) over the services and sources allocated to them it followed that they should have the freedom to borrow in their own name,
which was denied to them heretofore. This led to the Local Government Borrowing Rules to come into being made under the Reforms Act. Further, with the cutting off of the financial and administrative strands, there remained only the legislative strand which had so far debarred the growth of provincial autonomy. This legislative strand, as mentioned earlier, operated through the principle of requiring previous sanction and subsequent assent of the Government of India. Now by the rules made under the Reforms Act, a field has been marked off for the free exercise of the Legislative powers of the Provinces in which that principle has been dispensed with.

The rule of processor adopted was slightly been different In the matter of non-tax legislation the procedure adopted by the rules has been slightly different. In tax legislation the rules stated in what cases previous sanction was not necessary. In non-tax legislation the rules required in what cases previous sanction was necessary. The effect of this difference in the requirements of the rules of previous sanction was that while in matters of tax legislation Provincial Government could only levy certain named taxes, in the matter of non-tax legislation it could do anything provided it did not infringe certain laws. As Dr. Ambedkar puts the reasons for the same- "A widening of the basis of provincial taxation means a narrowing field for imperial taxation. Such a detrimental effect could not flow to the Government in the matter of non-tax legislation, be the non-tax legislative powers of the Provinces howsoever large. The taxing power to be granted to the Provinces had therefore to be more strictly circumscribed than the grant of legislative power. None the less it cannot be denied that the rules regarding previous sanction sufficiently loosened the legislative strand as to permit of the Provinces being autonomous in theory as well as in practice." (Moon 1989)
“This autonomy is well reflected in the new Budget Procedure in the Provinces. Under the old regime, the Provincial Budgets had to be passed by the Finance Department of the Government of India, the Provincial Accounts to be supervised by the Accountant-General and audited by the Controller and Auditor-General of the Government of India and appropriation reports submitted to the Finance Department of the Government of India. All this is changed under the new regime. There is no more as blatant a subordination as before. The Provincial Budget, is framed by the Finance Department constituted in each Province under the Reforms Act as opposed to it being passed by the Finance Department of the Government of India, and is voted item by item by the Provincial Legislature. Though the accounts of the Provinces still continue to be supervised and audited by the officers of the Government of India, instead of being sent to the Government of India for action, the appropriation reports are now sent to the Committee of Public Accounts constituted from amongst the members of the Provincial Legislature which sanctioned the Budget for report that the money voted by the Legislature was spent within the scope of the grants made by the Legislature. This clearly shows the hallmark of provincial independence under the new regime” (Moon 1989).

The demarcation of the field for the governance of India into Central and Provincial is, thus effectuated. Dr. Ambedkar concludes by pointing out that such a demarcation of administrative and financial matters was actually the dream of many an Indian politician and statesman. “Now that such an alteration has been made the ideal of Provincial autonomy bids fair to become real.”(Moon 1989).
CHAPTER XII
4D.4.1.3 A CRITIQUE OF THE CHANGE

Ambedkar points out that "the fuel of the whole administrative machine" is finance as good administration cannot do without good finance. The study of the financial arrangements with which the new system of administration starts is necessitated the most in the scheme of Reforms. The fact that this aspect of the Reforms Scheme has received comparatively little intelligent criticism at the hands either of the public or the expert makes it imperative for a closer examination.

The first question Dr. Ambedkar asks is whether new financial arrangements can be said to be administratively workable. To this he says, "To make administrative polities independent by requiring them to finance themselves entirely out of their own respective resources without having to depend upon one another must always be regarded as a very important end to be kept in view in devising a new financial arrangement. It is true that it is not always possible to realise this end, and it may in some cases be actually helpful to their working that the polities should be made mutually dependent; for interdependence, at least in matters of public finance, instead of being an impediment might conceivably furnish a basis for co-operation and strength. Nonetheless independence in finance for each administrative policy is to be sought for wherever possible. There can be no doubt that from this standpoint the system of contributions is better than the system of divided heads. This is not to condemn the system of divided heads. The existence of several concurrent or overlapping tax jurisdictions must always be a source of difficulty whenever an attempt is to be made to distribute the different sources of revenue among the competing tax jurisdictions so as to allow each a sufficiency of funds." (Moon 1989) Giving the reason he states that distribution of the sources of revenue must not only be governed by considerations of adequacy, but must also be governed by considerations
of suitability and further quotes Prof. Seligman, "The problem of efficiency of taxation is naturally of vital importance. No matter how well intentioned a scheme may be, or how completely it may harmonise with the abstract principles of justice, if the tax does not work administratively it is doomed to failure." (Moon 1989)

Dr. Ambedkar further states that it is the basis of the tax that actually decides among the sources of revenue to be partitioned, which are naturally more suitable for utilisation by one tax jurisdiction rather than by another. "If the basis of the tax is narrow then the argument in favour of its utilisation by a narrower tax jurisdiction will be correspondingly stronger. If its basis is wide then the scales would weigh in favour of its utilisation by the broader tax jurisdiction. But as a result of following the dictates of suitability it is not always possible to make a partition such as to give each administrative polity revenues adequate for its purposes. For it may so happen that a particular tax is suitable for one jurisdiction, while its yield, instead of being necessary for that jurisdiction, may be required for another jurisdiction which is unfit to levy it, or may be partially necessary for both." (Moon 1989) And to this, he suggests two remedies so as to see how are the ends of adequacy to be subserved. One would be the adoption of the system of divided heads, and other would be to apportion the deficiency among the several component states and require them to make a definite contribution towards meeting it.

Now this system of divided heads was not limited to the Indian fiscal system only as it had been adopted in some form or other by many other countries. In England, for example, the inheritance tax was assessed by the Central Government, but a part of the proceeds was allotted to the Local Government. This was also true with regard to some other taxes in England. In Germany too, under the Empire, the proceeds
of certain indirect taxes were divided between the federal and state governments. Also, in Canada, a large part of the provincial revenues were derived from proceeds of taxes that are levied by the federal government.

Dr. Ambedkar regrets the prejudice that exists in India against the system of divided heads of revenue as it was thought to be opposed to the principle of separation of revenues. People who opposed it had stated that this system involved divided heads of expenditure which led to the fettering of the spending powers of the Provinces and enabled the Government of India to directly interfere in their Budget estimates. Stating that the system of divided heads was no doubt characterised by these objectionable features, he further adds that the division of expenditure was not a necessary accompaniment of division of revenue. Nor was it a necessary incident of it that a polity, which shared in the yield of a tax but did not administer it, should interfere in calculating the estimates of the yield. He states, “Chipped of its evil features, the system of divided heads of revenue is simply another name for what Prof. Seligman calls the system of segregation of source and the division of the yield. The essence of the system consists in the exclusive assessment of a particular source of revenue by one tax jurisdiction, coupled, however, with an apportionment of a part of the proceeds to another tax jurisdiction. The system of divided heads of revenue does not cease to be a system of separation of sources merely because there is the division of the yield. In such a system of divided heads there is a separation because the assessment of the tax is segregated—which is the essence of separation-exclusively in the hands of one tax jurisdiction, and the division of the yield can be so regulated that it need not be incompatible with real separation.” (Moon 1989)
What the system of divided heads aimed to do was now achieved by the system of contributions. The system of contributions like the system of divided heads, answers the tests of suitability by allowing the tax to be administered by the jurisdiction most competent to do it, and also of that of adequacy by making the taxing jurisdiction hand over a sum to the non-taxing jurisdiction. Comparing the two systems, he states that there is no difference between the two except that so far as the apportionment of proceeds are concerned, one is an itemised arrangement while the other can be said to be a lump-sum arrangement. Dr. Ambedkar, however, gives the system of contributions a status of superiority as compared with the system of divided heads. He states that it merely does not permit of separation of assessment, but it also makes for a greater separation than as done under the system of divided heads. To put it in his words, “Under the system of divided heads the receiving party has still an anxious concern in the assessment and collection of the tax for any laxity in the administration of a divided head of revenues is bound to affect its interests adversely, and may therefore claim a hand in the administration of the tax. But under the system of contributions there is no room for such a possibility. Its quota being assured it is out of the business of assessing and collecting the tax. There is thus a greater separation under the system of contributions than there can be under the system of divided heads.” (Moon 1989)

Dr. Ambedkar rejects many of the objections raised to the system of contributions while analysing the equity of the new financial arrangements as being misconceived. As mentioned in earlier, contributions from the Provinces to the Central Government in India were regulated according to the spending powers of such Provinces. In fact it could be said to be apportionment by expenditure method of dealing with the deficit. Though it was obvious that this method subserves the ends of adequacy, what was not and which actually was a great virtue of the system of contributions, was that it promoted economy in the giving as
well as in the receiving tax jurisdiction. For, extravagance in the contributing tax jurisdiction immediately increases its burden, while extravagance in the receiving tax jurisdiction is directly reflected in enhancing the contributions. But he adds, "Nonetheless, the contributions, it is protested, are iniquitous, for they are held to be based not on population, nor on area, nor on wealth, nor on the capacity of the Provinces. It is also complained that the system of contributions according to spending powers is unwise, for it tends to check desirable expenditures in the more progressive Provinces. The latter is, of course, a real objection to the apportionment by expenditure method of contributions in its general form. But it may be said, on the other hand, that in the first place if a jurisdiction is willing to undertake the burdens of a larger expenditure for desirable aims, it will scarcely be deterred by the slight additional burden, which might result from the increase in the contribution. Secondly, if it were found that the contribution did produce such a result it would be possible to obviate it by adopting the simple expedient of exempting certain kinds of expenditure, which might be deemed to be necessary." (Moon 1989) And as far as the question as to what these expenditures should be, it would be a matter of adjustment, and this might differ from province to province. This would not change the virtues of the system of apportionment by expenditure method of levying contributions. Its automatic features would work equally well even if only some of the expenditures only, rather than all, were selected to be the basis of calculations.

However, Dr. Ambedkar states that this objection could not be urged against the Indian system of contributions. As he puts it, "In the first place, the contribution is not a varying sum as is the case in the financial systems of other countries. Because the Provinces are made contributory towards the deficit of the Central Government it is to be remembered that they are not liable to the whole of the central deficit
whatsoever it may be from year to year. On the other hand, in ordinary years the Provinces are only liable to make contributions towards meeting what is called the Standard Central Deficit of Rs. 9.83 lakhs. That being the case, the contributions do not form an element of uncertainty in the Provincial Budgets. Secondly, the contributions are not a permanent feature of the financial arrangements between the Central and Provincial Governments. The levy of the contributions is contemplated to be only transitional, to allow the Government of India to work out its financial salvation, and the Government of India has promised that they will adopt such a policy as to bring about the extinction of the contributions in as short a time as possible. Lastly, the ratio of the contributions to the standard revenues or expenditure of any of the Provinces is not so great as to place a heavy incubus on their financial system, and not being a varying quantity cannot be said to check useful expenditures by Provinces which propose to incur them.” (Moon 1989)

Dr. Ambedkar points out that despite the flaws in the apportionment by expenditure method of levying contributions, this system eminently answers the requirements of equity and this would be truer than under any other system. Assuming that expenditures very nearly correspond to the actual abilities of the communities concerned compared to that of population or area, he states that not only is the principle equitable in itself, but it is also seen that equity is done in its application as between the different Provinces. This is as contributions are regulated so that Provinces, rich as well as poor, are left with a reserve of spending power in order to enable them to meet any pressing need as might not have been covered by the figure for standard expenditure. And so the main purpose of rejecting equal contributions in favour of unequal contributions was essentially to see that the burden of
the contributions did not prevent any of the Provinces from meeting such extra expenditure as might have been absolutely necessary. Therefore by doing so, no system of contributions can be said to be calculated to produce greater equity than the Indian system.

Dr. Ambedkar then goes on to delve into whether the new financial arrangement had proved itself to be financially adequate. The Financial Relations Committee had held that considering that the general resources of the country were abundant, it was only necessary that there be a wise plan of distribution in order to leave each Province with a sufficiently large "spending power" or surplus. Thus came about a plan recommended by the Committee calculated to bring about such a result. However, when Dr. Ambedkar goes on to analyse the Budgets of the different Provinces since the introduction of the Reforms the result appears to be entirely disappointing. He states, "Thus, taking the estimated revenue and expenditure of the nine Provinces for 1922-3, equilibrium between current revenue and expenditure is only to be found in two of them, Burma and Bengal. In the latter, this result could not have been attained but for the temporary remission of its annual contribution to the Central Government, and a programme of taxation calculated to bring in Rs. 140 lakhs. In the rest of the Provinces the deficits of the year aggregated to the large figure of Rs. 7,74 lakhs. This huge deficit was financed by new taxation to the extent of Rs. 3,52 lakhs, and for the rest by drawing on balances and by raising loans from the public and from the Central Government." (Moon 1989) He, further, quotes Secretary of State in his dispatch as stating, "(this) process of financing provincial deficits in part from the accumulated revenue balances of the past will now practically come to an end, as such balances will be generally exhausted by the end of the current financial year... If the financial stability of the Provinces is not to be undermined,
with ultimate jeopardy to the Government of India itself, it is impossible to contemplate the continuance of a series of Provincial deficits financed by borrowing either direct from the public or from the Central Government.” (Moon 1989)

The remedy did not come easy as the Government of India and the Provinces were divided as to the proper solution for the rehabilitation of Provincial Finance on a stable and secure footing at the Conference held in Simla in April, 1922. The Provinces had proposed an increase in their resources by revising the financial arrangements made by the Reforms Act. While on the other hand, the Secretary of State as a mouthpiece of the Government of India urged that “Equilibrium can only be achieved by reduction of expenditure and the adoption of measures which will lead to an increase of revenue.” (Moon 1989)

The division of opinion was clear in the way the Provinces made their suggestions too, as there was no unanimity amongst them. Some like the Government of Bombay had suggested a return to the system of “divided heads” while others were opposed to it. But the majority was for securing relief through the abolition of contributions. Dr. Ambedkar considers this attitude of the Provinces towards the new financial arrangements on the face of it a very unreasonable one. This was because they were opposed both to the system of divided heads and the system of contributions. He points out, “Inadequacy of finance is not always the result of a paucity of revenue resources. National prosperity may be great and growing and the increase of national wealth may be proceeding unchecked. If under such circumstances enough revenue is not obtained the fault does not lie with the social income. Rather it is a fault of the government, which must be said to have failed to organize and marshal the national resources for fiscal purposes. The same is to some extent true of the Indian Government.” (Moon 1989)
Speaking of the national resources of the country, Dr. Ambedkar points out that there are two sources that the Government has not been able to marshal properly. One is the land revenue and this considering that land revenue actually had been the biggest resource to the Government of India. In the collection of the land revenue every landholder is laid under contribution, but the rate of assessment is not periodically enhanced for each one of them. In another case, in Bengal and in other parts of India the rate of assessment is permanently settled. Consequently in such parts of India had seen a consequent influx of capital, and also attained a greater advance in prosperity than any others. In effect, the land revenue yields practically no increase and the landowners, with enormously increased incomes, contribute nothing to the increase in the financial burdens of the State. Permanent Settlement has ever since the days of Lord Canning been suggested as a panacea for improving the financial condition of the people. In fact, after the severe famine of 1860, Lord Canning, then Viceroy and Governor-General of India, had recommended the extension of the Permanent Settlement to all parts of India. Despite many supporters, the proposal was rejected in 1883. Many agitations arose favouring it but the main reason was to put a limit on the financial resources of an alien and an irresponsible bureaucracy. However, Dr. Ambedkar states that many did not realise that some day a responsible government of the people and the Permanent Settlement which would lead to placing a fetter on the freedom of a popular government to enter upon the path of orderly progress. As he puts it, "A bad government may abuse its financial powers, but a government cannot be a good government if there is a serious limitation on its financial powers. It was therefore a good thing that this evil of a permanent settlement was not allowed to spread to the whole of India."
(Moon 1989) However, he goes on to add that it would have been better if the new financial arrangements had contrived to replace the permanent
settlement system of land revenue by a periodical settlement system. This was one way in which the general resources of the country could be augmented and thereby resulting in adequacy to all the governments concerned. Instead, the financial arrangements were so founded as not to "subject the permanently settled provinces to financial pressure, which would have the practical result of forcing them to reconsider the permanent settlement." In fact, if this would have resulted in augmenting the general resources to the benefit of all. But, not only a provision was made favouring the retention of the Permanent Settlement, but the Bengal Government, which has the largest number of permanently settled holders of land, was later on exempted from contributing to the Government of India which was compelled to meet its deficit in other ways.

The other source of revenue, which, in Dr. Ambedkar's words "the Government refuses to tap", is the customs revenue. He states that the kind of fiscal policy adopted during the pre-Mutiny days and post-Mutiny days was, of a suicidal character. In fact, the Government of India had never looked upon the customs revenue as a resource to be used to meet the exigencies of the State and when it has used it, it is only very reluctantly, and never to the fullest extent. The reason given in favour of such a fiscal policy is that the customs revenue is wrong in principle, though however the actual reason was that it was feared that under it Indian industries would be protected against English industries. The Government of India had essentially been subjected to a pernicious kind of limitation on its fiscal powers and which prevented it from using a source of revenue which had everywhere else proved to be most elastic and abundant of financial resources. As Dr. Ambedkar puts it, "If these limitations were not there the present financial inadequacy in all probability might not have ensued at all, and there would have been no
necessity either for adopting the system of divided heads or for imposing contributions. As it is, owing to these limitations on the taxable resources of the country, a deficit in the Budget of the Central Government is inevitable. Given this fact, the adoption of some method of meeting that deficit was imperative, and there is no doubt that the system adopted is better than the system it replaced. In the present circumstances of the finances of the Central Government, contributions must be taken as a settled issue. Nor can it be said that the abolition of contributions would restore stability to Provincial Finance." (Moon 1989) He, further, points out that this was the prevalent view of the Provincial Governments and also of non-official politicians. In fact, the Resolution moved in the Indian Legislative Assembly on the 14th September, 1922, rested on the same view that if the Government of India were only to dispense with the contributions it would immediately restore equilibrium in the financial position of the Provinces. This belief was strengthened by the assumption that the aggregate estimated deficit of all the Provinces disclosed itself to be 352 lakhs of rupees for the financial year 1922-3; and as the total contribution to the Imperial Government by the Provinces aggregated to the sum of 983 lakhs. And so, a remission of this amount would more than wipe off the deficit in the Provincial Budgets. However, Dr. Ambedkar, notes, "the deficit of 352 lakhs of rupees does not disclose the true position of the Provinces as derived from the financial arrangements made by the Act. If we are to deduce the true position of the Provinces as following from the new arrangement we must take note of the new taxation imposed and of the gain to Bengal through the remission of its contribution to the Imperial exchequer. According to this calculation the aggregate deficit of the Provinces would have been about 867 lakhs. But we must make some further adjustments to this account. It has not been possible to deduct from the revenues of the Central Provinces the sum derived from the enhancement of the Excise duty in the Provinces.
Secondly, the revenues of the Central Provinces for the year 1922-3 include collections of suspended revenue of previous years. If these adjustments were made the aggregate deficit of the Provinces would give rise to a figure which would be barely covered by the remission of contributions. We must therefore conclude that remission of contributions would have at best been a very inadequate measure for removing the financial stringency of the Provinces, even if the problem of financing the extra deficit caused by such remission in the budget of the Central Government were to be ignored.” (Moon 1989)

Considering that remission of contributions cannot improve the difficult situation that has arisen with regard to Provincial Finance, it is thus important that one goes to the root of the matter and inquire what are the causes which have brought on that situation. The questions as posed by Dr. Ambedkar are thus: “Is it due to the normal expenditure of the Provinces being under-rated? Or is it due to the normal revenues of the Provinces being over-estimated?” (Moon 1989) And so he goes on to ascertain whether the resources allocated to the Provinces were really inadequate to their normal needs.

By way of an empirical study he concludes that except in the case of two Provinces the standard revenue has left a sufficient margin over standard expenditure. As he notes, “Only in Bengal and Central Provinces there was no margin, owing to the fact that the standard expenditure was slightly in excess of the standard revenue. But this defect was more than remedied in the case of Bengal by the remission of the contributions to the Central Government, and the excess of standard expenditure over standard revenue in the case of Central Provinces was indeed very small. Barring this, in the rest of the Provinces the margin allowed was substantial.” (Moon 1989) Then comparing the actual figures
with that of the standard figures in case of the revenue side of the Provincial Budgets, he asks as to whether the realised revenue had fallen short of the standard revenue. And to thus he concludes that the table clearly showed that the realised revenue has in no case fallen short of the standard revenue. Then the question one might ask is as to whether the increase in the realised revenue had been equal to the margin allowed under the allocation between the standard revenue and of the Provinces. Giving more figures, he states that it is obvious that except in the case of Madras the realised margin has in no case fallen below the standard margin. The excess of the realised over the standard margin is enormous. “It cannot, therefore, be said that the financial deficit in the Provinces is due to provincial revenue having failed to reach the assumed normal. On the other hand, the revenues were more than necessary to cover the normal expenditure of the Provinces. The only conclusion that can fairly be drawn from the facts of the case is that the provincial deficits are due to an extraordinary increase in the expenditure of the Provinces.” (Moon 1989)

The view of the Secretary of State that reduction of expenditure and increase of taxation is the only remedy for placing provincial finance on a sound footing is then concluded.

Then Dr. Ambedkar asks as to what chances are there that the Provinces will undertake the reduction of expenditure and increase of taxation so very necessary for their safety and quotes Mr. James Wilson, “Finance is not mere arithmetic; finance is a great policy. Without sound finance no sound government is possible: without sound government no sound finance is possible.” He goes on to add, “If there is any truth in this (as stated by Mr. Wilson), then whether or not the Provincial Governments will undertake economy or face increase of taxation depends upon whether or not the system of government established in
the Provinces by the Reforms Act is a sound system." (Moon 1989) Going into the nature of the government that is established in the Provinces under the Reforms Act, he states the system is known as dyarchy and goes on to describe the system. He states, "Under it the Executive of the Province, instead of being composed of the Governor in Council as before, is now divided into the Governor in Council and the Governor in Ministry. Under it the subjects marked off as Provincial from the Central are further divided into "Reserved" and "Transferred" subjects. The former are in charge of the Governor in Council, and the latter in that of the Governor in Ministry. Of these parts of the Provincial Executive the Council in charge of the "reserved" subjects still remains as before irresponsible to the Provincial Legislature, is unremovable by it, and in that sense is a non-parliamentary executive. The other part of the Provincial Executive, namely the Ministry in charge of the "transferred" subjects, is recruited from the elected members of the Provincial Legislature, which is made responsible to the Provincial Legislature which is based on a more or less popular franchise, and is removable by it, and in that sense is a Parliamentary Executive." (Moon 1989)

Further describing the Provincial Legislature, he states it, "...is supreme with regard to both the parts of the Provincial Executive. It has not only full powers of legislation, but has also full and unfettered powers of interpellation. Its powers of sanctioning and voting upon the Provincial Budget are complete, although provision is made in the Reforms Act, which allows that "the Local Government shall have power in relation to any such demand (for a money grant) to act as if it had been assented to, notwithstanding the withholding of such assent or the reduction of the amount therein referred to (by the Provincial Legislature), if the demand relates to a reserved subject (which is assigned to the charge of the Governor in Council) and the Governor certified that the Expenditure provided for by the demand is essential to the discharge of his responsibility for the subject." (Moon 1989)
Dr. Ambedkar then questions whether such a government could tackle the problems of sound finance and states. "It is obvious that of the two parts of this dyarchical Executive, one, i.e. the Governor in Council, need have very little anxiety for reduction of expenditure or for the increase of taxation. It derives its mandate from Parliament, and as such is free to adopt any policy-backed up as it is by the certification power of the Governor without any regard for the best interests of the taxpayer. The authors of the Joint Report had seen that this certifying power to override the wishes of the Legislature might lead to irresponsible extravagance on the part of the Governor in Council, and had proposed to endow the Governor in Ministry with a countervailing power which was to act as a curb on the former. That power was to have consisted in the Proviso which laid down that no taxation even in the interests of the "reserved" subjects should be imposed in any Province without the consent of the ministry. The Extremists—a class of politicians in India who were bent upon minimising the reforms as being inadequate—disliked the proviso as calculated to make scapegoats of ministers and to bring them into discredit with the people. But their rivals, the "Moderates", now calling themselves "Liberals"—one does not know why—saw clearly what the proviso meant. If this had materialised, there can be no doubt that the ministry would not have been a mere outsider tendering advice to the Council which might be accepted or rejected, but would have obtained a powerful voice in the settlement of the budget." (Moon 1989)

No minister unless he was in a position to justify the budget proposals, including even those, which pertained to the reserved subjects, would have hoped to persuade the Legislature to agree to a proposal of new taxation. One could say that the influence of the ministry on the "reserved" subjects, i.e. on the Council, would have
inevitably been in the direction of thrift and retrenchment. Dr. Ambedkar
go on to elaborate thus:

“The moderates were entirely right in their interpretation of the proviso
and also in their insistence upon acquiring power, even at the cost of
burdening the country with new taxation. But in the heat of the
controversy and their desire to convince the public of the substantiality
of the Reforms, they drew some very amusing pictures of how the
ministers working under the aegis of the proviso would be able to hold
the Council at bay. This alarmed the bureaucracy, which raised the cry
that it was dangerous to leave the provision for the “reserved” subjects to
the tender mercy of ministers who bore no responsibility for the
consequences of refusing adequate Budget provision for those subjects.
The authors of the Joint Report had realised the force of this argument,
and had confessed that the success of the arrangements depended upon
their being worked by reasonable men who would conduct themselves in
a reasonable manner. They were probably right in refusing to assume
that the ministers would not co-operate, either by reducing their own
claims or by imposing taxation, in order to meet expenditure which the
Council considered essential for the proper administration of the
“reserved” subjects. But the bureaucracy, which had been frightened by
the tactless jubilation of the Moderates, insisted that even reasonable
men would at times, in all good faith, differ vitally from other reasonable
men when it was a question of providing supply for work which one party
was responsible for safeguarding and developing, while the other was
only concerned in getting a share of the money. In its opinion,
circumstances could well be imagined in which reasonableness might not
prevail. Let us suppose, it was argued, that the Governor in Council finds
new and heavy expenditure imperative on some reserved subject, but
that he cannot induce ministers to consent to accept less for their subjects or impose taxation for it. The Governor then, under his exceptional powers, insists on the expenditure being provided for in the next budget, and the result is to leave ministers with inadequate funds for their transferred subjects. What is to happen? Are ministers to be compelled to raise a tax which is apparently for their own need, but a need which has been created against their will by the Council refusing to curtail their demands? Such a procedure, it was pointed out, would be tortuous, provocative, and indefensible. Again, let us suppose that ministers consented to raise the necessary money, but the legislature refused to pass their revenue measures. Are the ministers to resign as having lost its confidence? The bureaucracy placed another dilemma before the authors of the Joint Report. Ministers have raised a new tax for some purpose of their own. In the next budget the Governor finds himself compelled to add substantially to the reserved provision for some new necessity, and thus to curtail the provision for "transferred" subjects. Ministers virtually see their new taxation receipts going to finance some development for which they are not responsible, and of which indeed they may disapprove. What are they to do? To avoid these difficulties the proviso was dropped and in its place the changes were made in the Devolution Rules.” (Moon 1989)

Dr. Ambedkar thus, goes on to list the changes under their various heads: taxation and borrowing, allocation of revenues for the administration of transferred subjects, procedure in the event of failure to agree, period in order of allocation, and the preparation of budget in default of agreement of order of allocation.
As Ambedkar states, “Thus, rather than depend too implicitly on reasonableness when circumstances must often be provocative, effective precaution is taken by these rules against the ministry disapproving the allocation of funds to the “reserved” subjects by allowing the Governor to make such an allocation which is to be binding on both parts of the executive. They also by arm him with the power of veto over the Provincial Legislature by allowing the Governor, should he deem it necessary, to restore a Budget grant on a reserved subject if it were refused or reduced by the Provincial Legislature which has the right to determine the Provincial Budget, and thirdly by allowing the Governor in Council equally with the Governor in Ministry to raise new taxation or new loans for the development of the subjects in its own charge. The result is that one part of this dyarchical Executive, namely the Governor in Council, can have little reason to be interested in economy or be overweighed by considerations of taxation. Its supply being assured its concern in the stability of provincial finance must be deemed to be somewhat remote. The whole burden of meeting the problem of restoring sound finance, therefore, falls upon the Governor in Ministry in charge of the “transferred” subjects. For, under the distribution and certification powers it is the “transferred” subjects which must go without the funds they need, and it is those in charge of them, namely the Ministers, who must bear the brunt of economy or resort to new taxation to bring about an equilibrium in the finances of the Provinces. For it is doubtful that the Governor in Council will choose the onerous task of raising new taxes or practice economy when there are open to them other ways of amply providing themselves for the subjects they have under their control.” (Moon 1989)
To the question whether the other half of the Government, namely the Governor in Ministry, would consent to practice economy, or if need be undertake the burden of new taxation, Dr. Ambedkar states that this would obviously depend upon the temper of the Legislature. Here, Dr. Ambedkar clearly points out that the Legislature will not readily favour projects of increased taxation. Giving reasons, he states "...any proposals for extra taxation would be shunned as likely to prejudice the chances of the legislators at the polls. So long as nomination was the general mode of obtaining a seat in the Legislature it was unnecessary to mind the prejudices of the electors. But when a seat is in the gift of the elector a candidate to the Legislature who proposes to touch his pocket has a small chance of success, even though the new taxes are to result in more than proportionate benefit. Besides, a political party, which has won power from a bureaucracy by accusing it of heavy taxation, cannot easily consent to disgrace itself by continuing the same policy. This innate aversion to taxation on the part of the Legislature is strengthened by the peculiar attitude of the Legislature towards the "reserved" and "transferred" subjects. The reserved subjects are those which mostly pertain to peace and order, while the transferred subjects are those which largely pertain to progress. But as has already been pointed out, the policy of the bureaucracy before the Reforms was calculated to sacrifice progress to order. It is therefore obvious that under the revised constitution the popular Legislatures should aim at turning the scales in favour of subjects tending towards progress. Their aversion to increase of taxation and their partiality for the transferred subjects will favour them to welcome proposals on the part of ministers making drastic reduction in the funds allotted to the reserved subjects. Their attitude towards the ministers will be largely governed by the amount of economy they will be able to effect in the reserved subjects for the benefit of the transferred
subjects. Thus, in the absence of any very large chances of increase of revenue the two halves of the Executive, the Governor in Council backed by the distribution and certification power and the Governor in Ministry backed by the general Budget powers of, a popular Legislature, will compete in the matter of developing their subjects by forcing economy on each other. The Legislature being unwilling to tax, the Governor in Council being in a position to resist retrenchment and the Governor in Ministry anxious to expand, the chances of an early equilibrium in Provincial finance are very small.” (Moon 1989)

Dr. Ambedkar, therefore concludes that the reason that the Provinces have no good finance is because dyarchy is not a good form of government. He, further, goes on to say dyarchy is a bad form of government because it is opposed to the principle of collective responsibility. It is imperative that an administrative machine must work smoothly and harmoniously and to do so it must recognise the “principle of impartibility of governmental work and a collective responsibility of the administrators in the execution thereof.” He goes on to add, “That the work of government is by its nature impartible may not seem to accord with facts: for, in practice the functions of government can be and commonly are partitioned, as they are between local bodies and between departments. Nevertheless it is true that a common thread runs through them all: that no function of government acts in vacuum; that each reacts on some other function, and that the various functions cannot act at all to produce orderly progress unless there is some force to harmonise them. Otherwise a policy enunciated in one department may fail to fructify for want of helpful action on behalf of other departments.” (Moon 1989) And it is only in the principle of collective responsibility that this harmonising force can be found. He points out the reason by quoting
Hearn, "Each minister acts in his own department as the recognised agent of his colleagues in that particular department, subject, however, to inquiry and control by the whole body. But in all cases on which any difficulty is likely to arise each minister, from motives not merely of prudence but of honour, takes the opinion of the Cabinet. When the precaution is taken the measure becomes the common act of the Ministry." (Moon 1989)

Dr. Ambedkar goes on to point out that a unified government based on collective responsibility is guided by a common co-ordinated policy. On the other hand, having made a partition of governmental work, dyarchy should have introduced an element of divided responsibility in the Executive. He goes on to state that though there is an element of partition in responsibility, the Legislature and the Executive are not completely divorced from each other. The partition is hence "not horizontal but vertical." By setting up two parts it has not meant that there are two separate Legislatures for two separate executives nor that each should make its own laws, control its own finance, frame its own budget, impose its own taxation, and raise its own loans. It has also not been held that each should have its separate staff for the administration of subjects allotted to it and have its own methods of recruitment, pay and pension for its services. This indicates that the authorities have no clearly defined spheres of their own exclusively within them. Dr. Ambedkar goes on to mention that though the Government of India had suggested that some if not all, of these concomitants of a typically dual executive be made a part of the dyarchical system adopted to carry on the government of the Provinces, the framers of the new constitution were wise enough not to allow such a thing. He quotes them as saying, "...wisdom lies not in equipping each of the different elements with a
complete paraphernalia of its own, and trusting to their orbits lying sufficiently apart for collision to be avoided; but in taking every opportunity of bringing the two elements into contact so as to induce the habits of joint action.” The authors of the Joint Report further add, “It is our intention that the Government thus composed and with this distinction of functions shall discharge them as one Government,” and that “the Provincial budget should be framed by the Executive Government as a whole.” (Moon 1989)

Dr. Ambedkar commends the fact that subjecting it to the interplay of two principles modified the working of dyarchy. One of division was so that a clear definition as possible of the several responsibilities of the two parts of the government be given and the other, of union, in order to get association in aims and policy between those parts. As he states, “For to equip each part of the Executive with separate paraphernalia would have been nothing short of a calamity. But because there is an understanding that when ministers will act in matters of transferred subjects the councillors will advise them, and that when councillors will act in matters of reserved subjects the ministers will advise them, it does not alter the fact that dyarchy is a system of divided responsibility. It is not a system which ensures the work of government being conducted in harmony and in accordance with a common policy.” (Moon 1989) On the other hand, the system was also fraught with, as he puts it “organised quarrel”. He adds, “The dividing line between dyarchy and anarchy is very narrow. If such a system is not rent in practice it is because of two transient circumstances. One such circumstance consists in the Provincial Legislature being a weakling sapped of its vitality by political dissensions. The other consists in the tenure of the Ministers not being at the will of the Legislature, but for the duration of the Legislature’s
existence, and is to hold office during the pleasure of the governor. To allow a governor to choose ministers from among the elected members of the Legislature instead of requiring him to accept ministers who are elected by the Legislature is a grave derogation from the principle of responsible government which was avowedly the object of the Reforms Act.” (Moon 1989) Dr. Ambedkar draws a distinction between a minister who has the confidence of the governor, and a minister, who has the confidence of the Legislature. He gives the example of the English political history of the eighteenth and the nineteenth centuries wherein the difference between the two in so far as good government is concerned is writ large. Now the fact that such a system had been adopted against which the whole English constitutional history cannot be but without some reason. The plausible reason, as Dr. Ambedkar points out, advanced is that the Legislature “had had no experience of the power of dismissing Ministers, or the results attending the exercise of such power. Nobody in India is yet familiar with the obligations imposed by tenure of office at the will of a representative assembly. It is only by actual experience that these lessons can be learned... By the device of appointing the ministers from the elected members of the (Legislature) and making their tenure of office conditional on the retention of their seats (there is) established at once some measure of responsibility, in the form of responsibility to their constituents and thus (is) put an end to the condition of affairs in which those entrusted with the administration are wholly irresponsible to the constituents who elect the (Legislature).” (Moon 1989)

Dr. Ambedkar points out that it is evidently difficult to believe in the wisdom of this reasoning as given above. He states that the need is for a proper conduct on the part of an individual or a group is to
understand the meanings and values of things rather than to argue that nothing can be learned without experience. And so, a Legislature composed of responsible persons may be trusted to know the consequences of dismissing a Minister and there is no need for them to learn it by experience. He quotes Prof. Dicey in this regard, "any expressions which attribute to Parliamentary electors a legal part in the process of law-making are quite inconsistent with the view taken by the law of the position of an elector. The sole legal right of electors under the English constitution (and the same is true under the Indian constitution) is to elect members of Parliament. Electors have no legal means of initiating, of sanctioning, or of repealing the legislation of parliament. No court will consider for a moment the argument that a law is invalid as being opposed to the opinion of the electorate" (Moon 1989); and adds on to say that it is this which exactly defines the status of the Indian electors. He states, "To make the minister responsible to such a nonentity is to make him virtually irresponsible. That the framers of the constitution were not alive to these considerations in suggesting this particular mode of appointing Ministers it is hard to believe. What is more probable is that this particular mode of appointing ministers was adopted because it permitted to select a man who was more likely to cooperate with those in charge of the reserved subjects and who being irremovable by the Legislature would be less swayed by its wishes. But the Ministers cannot remain altogether immune from the axe of the Legislature."

(Moon 1989) Dr. Ambedkar clearly sees the dangers underlying this system as he points out that when a minister has cultivated a friendship with the councillor and so fails to ingratiate himself into the favour of the Legislature, this thus cannot fail to come home to him on budget occasions. The proposals that the minister embodies in the budget would be liable to be reversed by a vote of the
majority of the Legislature, and with regard to this, he would be completely handicapped for neither he himself nor the governor will be able to intervene. The only remedy can lie in his resignation.

However, Dr. Ambedkar states that these circumstances which have, so to say, saved dyarchy from failure are only transitory. As he puts it, "The political dissensions may be no more than a passing phase, and the ministers from the second term of the reformed Legislature will become amenable to it: so that before long the forces may be organised better than they are, when dyarchy is sure to fail." (Moon 1989)

Dr. Ambedkar points out that hybrid executives, divided responsibility, division of functions, reservation of powers, cannot make for a good system of government, and where there is no good system of government there can be little hope for a sound system of finance. The primary solution to that is an undivided government with a collective responsibility. However, it can only be achieved, as he puts it, "when the whole of government derives its mandate from a common source." He, further adds, "That such a consummation should take place as early as possible is devoutly to be wished. In that behalf it is encouraging to know that dyarchy is but a transitional system." (Moon 1989) The issue, which arises here, is as to how long and protracted will the period of transition be. To put it in Dr. Ambedkar's words, "The justification for introducing a dyarchical form of government rests on the supposition that India is at present ill-prepared to sustain a system of responsible government in anything like completeness, for owing to the lack of education and political experience, the Indian electorate will for some time be unable either to formulate their requirements intelligently or effectively impose a mandate upon their representatives, and that owing to the inveterate
social prejudices of the educated classes there is a great danger of their abusing the political power to exploit the masses. This cardinal fact, it was held, must differentiate the degree and the kind of responsibility which can be introduced at the outset from that which will be the eventual resultant of the new system, and must impose the obligation of ensuring that the forces which now hold the people together are not completely withdrawn before satisfactory substitutes are ready to take their place." (Moon 1989) On the other hand, he states that there is no necessity to wait till the cardinal fact disappears, for "in all countries responsibility in the beginning has been entrusted to a very small section of the people, and government has been in the hands of a small educated minority, who have naturally cared for the interests of the uneducated masses pending the spread of education and the consequent extension of the franchise." (Moon 1989) Dr. Ambedkar argues that the fact that there exist downtrodden communities suffering from social oppression and social injustice has not led to no country to be without political power on that account. He says that those who use this argument forget that if other countries like America with her Negroes and Japan with her Hitas are in possession of political power without having first destroyed social inequality, it is due to the fact of their having been in possession of military power. According to him, "Military force and moral force are the two chief means to political freedom, and a country which cannot generate the former must cultivate the latter. Thus in India the political problem is entirely a social problem, and a postponement of its solution virtually postpones the day when India can have a free government subject to the mandate of none but her own people." (Moon 1989)
References: