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

III.—GENERAL PRINCIPLES

Allocation of Revenue and Expenditure

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

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

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

(2) **Other "Central" Departments—**

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

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

Allocation of Capital Assets

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

stated in general terms, will operate as follows :—

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

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

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

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

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

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

Allocation of Current Liabilities and Liquid Assets

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

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

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

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

(*iii*) Capital Reserve Funds;

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

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

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

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

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

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

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

Plan of Detailed Working

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

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

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

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

IV.—INTEGRATION OF "CENTRAL" REVENUES AND EXPENDITURE

"Central" Revenues

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

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