

Saturday, 28th February, 1942

COUNCIL OF STATE DEBATES

(OFFICIAL REPORT)

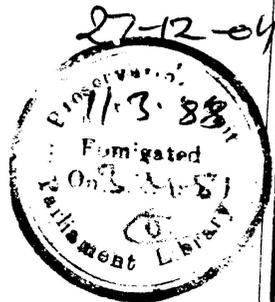
VOLUME I, 1942

(18th February to 2nd April, 1942)

ELEVENTH SESSION

OF THE

FOURTH COUNCIL OF STATE, 1942



PUBLISHED BY THE MANAGER OF PUBLICATIONS, DELHI
PRINTED BY THE MANAGER, GOVERNMENT OF INDIA PRESS, NEW DELHI
1943

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COUNCIL OF STATE.

Saturday, 28th February, 1942.

The Council met in the Council Chamber of the Council House at Half Past Five of the Clock, the Honourable the President in the Chair.

PRESENTATION OF THE GENERAL BUDGET, 1942-43.

THE HONOURABLE MR. C. E. JONES (Finance Secretary) : Sir, I have the honour to present the revised estimates of revenue and expenditure of the Governor General in Council in respect of subjects other than railways for the year 1941-42, and the corresponding estimates of revenue and expenditure for the year 1942-43.

2. This is the third war budget which it has fallen to my lot to bring before this House, and each successive year has seen the grim conflict which began in that fateful autumn of the year 1939 become more intense and more widespread until it has now become, in fact as in name, a World War. As the struggle has progressively extended from country to country and from continent to continent, so has it and the conditions created by it increasingly affected the economic structure of this country, so that it is no exaggeration to say that at the present time it dominates every facet of our economic life and directly affects the living conditions of every member of the community, even to the very humblest. In Part II of the Explanatory Memorandum, a new departure which it is believed Honourable Members will welcome, will be found statistical information regarding the trend during the course of the war of various important aspects of our national life such as the level of prices, the cost of living, the import and export trade, the volume of currency in circulation, and so on. The factors there portrayed cannot be properly viewed in isolation as they are all closely inter-dependent and inter-related and, in combination with the extreme pressure on the industrial capacity of the country for the production of war supplies, and the rapidly growing defence measures with its inevitable corollary of steeply rising war expenditure, form the background against which the budget proposals have to be considered. In so far as it is possible to single out features of particular significance, special mention might perhaps be made of the utilisation to full capacity of India's industrial potential which has resulted in a great increase in employment, a larger national income, rapidly growing defence expenditure, rapid expansion of rupee currency in India and of sterling resources in England. These factors have resulted in a rising pressure of domestic and external demand on the total volume of consumable goods in India, which in certain directions are developing shortages as against the expanding demand. These indicate considerations which will require attention if India's economy is to be kept on an even keel in the midst of the severe stresses and strains of a war on the scale of that in which we are now involved. So far as the near future is concerned we must necessarily take into account the deterioration in the Eastern theatre of war, the threat to sea communications and the overburdening of available means of transport within the country, which for a time cannot but affect adversely its economic activity.

[Mr. C. E. Jones.]

3. Before we come to consider the revised estimates for the current year a brief reference might first be made to the final results for the financial year 1940-41. The deficit on revenue account which, according to the revised estimates presented last year, was expected to be Rs. 8,42 lakhs in actual fact amounted to Rs. 6,53 lakhs. The improvement of Rs. 1,89 lakhs was the net result of an improvement of revenue by Rs. 3,94 lakhs and an increase in expenditure of Rs. 2,05 lakhs. The latter was almost entirely on account of Defence, where the difficulties of close estimation in present conditions will be readily appreciated. Of the increase in revenue, Rs. 2,20 lakhs or more than half came in the form of a larger contribution from the Railways for the reasons explained in the Railway Budget Speech last week, while Income-tax accounted for an additional Rs. 96 lakhs and Central Excise Duties for an extra Rs. 99 lakhs. As a result of the improvement in Income-Tax receipts the divisible pool shared with the Provinces rose from Rs. 16,47 lakhs to Rs. 18,08 lakhs, thereby increasing the share payable to the Provinces from Rs. 3,73 lakhs to Rs. 4,54 lakhs. The balance of Rs. 81 lakhs will be paid to the Provinces along with their share for the current year.

4. The revised estimates for the current financial year 1941-42 are as follows:—

	Budget.	(In lakhs of rupees.)	
		Revised.	Improvement (+) Worsening (—)
Net Defence expenditure	84,13	102,45	—18,32
Civil expenditure	42,72	44,44	—1,72
Total expenditure	126,85	146,89	—20,04
Total revenue	113,00	129,62	+16,62
Deficit (—)	—13,85	—17,27	—3,42

thus showing an increase in the year's deficit of Rs. 3,42 lakhs as the net result of an improvement in revenue of Rs. 16,62 lakhs and an increase in expenditure, mainly on account of the Defence services, of Rs. 20,04 lakhs. I will proceed to explain the main contributory reasons for these variations.

5. Of the Rs. 16,62 lakhs increase in revenue Rs. 8,94 lakhs or well over half is accounted for by the fact that, as explained in the Railway budget, the net contribution from the railways to general revenues is expected to amount to as much as Rs. 19,12 lakhs as against Rs. 10,18 lakhs provided in the budget estimates. The net surplus of the other great commercial Department of Government, the Posts and Telegraphs Department, which will be taken to general revenues, is expected now to amount to Rs. 3,19 lakhs, or Rs. 1,79 lakhs more than was provided in the budget, as a result of the growth in all branches of traffic, especially the telegraphs and telephones which have been worked practically to full capacity. Under Currency and Mint there is an improvement of Rs. 1,21 lakhs, the bulk of which represents the increase in the surplus profits of the Reserve Bank of India for the year ending 30th June, 1941, and the balance the profits on foreign orders for coinage and notes which have been executed in our Mints and Currency Note Press. We anticipate that our Customs receipts for the year will exceed the budget figure by about a crore in spite of the deterioration in the last month or two consequent upon Japan's entry into the war, while Central Excises should give us a further increase of Rs. 20 lakhs. Income-tax and Corporation tax show a rise of about Rs. 3 crores as compared with the budget, in spite of the fact that collections on account of

Excess Profits Tax are likely to fall short of the Rs. 11 crores originally anticipated by as much as Rs. 3 crores. Against this improvement however we have to set off the additional amount of Rs. 2 crores which is payable to the Provinces as a result of the divisible pool having increased from Rs. 18,35 lakhs to Rs. 22,17 lakhs. Inclusive of this increase and of the Rs. 81 lakhs arrears from last year the Provinces will this year receive on account of Income tax the altogether unexpectedly high figure of Rs. 7,39 lakhs.

6. The increase of Rs. 18,32 lakhs in net Defence expenditure for the current year 1941-42 is made up as follows :—

	(Rs. in lakhs.)	
	Budget.	Revised.
(1) Basic normal budget	36,77	36,77
(2) Effect of rise in prices on (1)	3,55	4,24
(3) India's war measures	35,40	53,03
(4) Non-effective charges	8,41	8,41
Total	84,13	102,45

Item (1) of course shows no change, while item (4) is retained at its original figure pending settlement with His Majesty's Government regarding the allocation of non-effective charges arising out of the war. The rise in item (2) is merely a reflection of the rise in the general level of prices of indigenous stores. Interest therefore chiefly centres in item (3) which shows an increase over budget of Rs. 17,63 lakhs in respect of the cost of war measures debitable to Indian revenues. The increase would have been Rs. 18½ crores but for contributions amounting to Rs. 85 lakhs received through the Viceroy's War Purposes Fund. I would here remind Honourable Members that under the Financial Settlement with His Majesty's Government only such portion of the expansion of India's Defence services as is related to India's local defence requirements is chargeable to Indian revenues. Thus, broadly speaking, India bears the cost of raising, training, and in part equipping any additional forces raised and retained in this country in pursuance of her expansion scheme, while the whole cost, initial and recurring, of such additional forces as are sent overseas is recoverable from His Majesty's Government. The House will be interested to know that the gross expenditure on defence services and supplies expected to be brought to account in India's books for the year 1941-42 amounts in all to Rs. 300 crores, so that after India's share of Rs. 102,45 lakhs mentioned above has been deducted a balance of nearly Rs. 200 crores is left to be borne by His Majesty's Government. These figures do not include the value of equipment supplied and other services rendered by His Majesty's Government without charge.

7. Judged by past Indian budgetary standards, these are large figures, and I feel that some explanation is due to the House as to how the money is being spent, brief and inadequate though that explanation must necessarily be having regard to the limited time at my disposal. The primary objective is, of course, the provision of the maximum possible strength of up-to-date military, naval and air forces, subject to the limiting factors of equipment and training, first for the local defence of India's land and sea frontiers, and secondly for employment overseas to secure the approaches to India. The rapid increase in the danger and imminence of the threats to India's security have rendered imperative substantial modifications and enlargement of the expansion schemes to which reference was made in connection with the budget a year ago, involving a considerable increase in cost. Recruiting activities have been stepped up

[Mr. C. E. Jones.]

during the last 12 months from an average intake of recruits of roughly 20,000 per month to an average of about 50,000 per month, and we now have over a million men under arms as against the half million to which I referred in my Budget Speech last year. Apart from the pay and allowances of these men, in itself a substantial item, the cost of feeding, housing, clothing, equipping and transporting them constitutes a very heavy additional burden on Indian revenues.

8. Concentrated efforts continue to be made to train intensively not only the new units which are being formed but the thousands of officers required to instruct and lead them. Last year special stress was laid upon the extreme importance of adequate training and the fact that, next to the provision of arms and equipment, the pace of our expansion was conditioned by the quality of our training. During the last 12 months the various schools and other training institutions of the Defence services have been greatly increased. Thus the Staff College has increased its output by 100 per cent. since March, 1941. The Fighting Vehicles School and the Artillery School have also doubled in size since that date. The Tactical School, Small Arms School and Army Signals School have all been greatly expanded. Many new training institutions have also come into being. An Air Landing School for the training of parachute troops is now in full operation. A special centre for instruction in anti-aircraft and coast defence artillery has also been created. In addition to the Officers' Training Schools, where several thousand cadets and newly commissioned officers are learning the rudiments of their profession, a Higher War School has been established at the other end of the scale for the instruction of senior officers.

9. The programme of expansion for the Royal Indian Navy which I indicated last year is now materialising rapidly. The strength of officers and ratings has been approximately doubled. Two new sloops of the latest type, fast and well-armed, are fully commissioned and have already seen service. Others are under construction in the United Kingdom. A large programme of building in connection with our Local Naval Defence requirements has been undertaken in India and some vessels have already been completed and commissioned. New and enlarged accommodation for the Gunnery School and Mechanical Training Establishment has been provided during the past year.

10. The development of the Air Forces has proceeded as fast as the provision of equipment and skilled technical personnel permitted, and much progress has been made during the year. Modern aircraft are now arriving in India and a substantial quantity of modern training equipment has been received. The rapid and continuous increase in the complexity and requirements of modern aircraft, the introduction of new types of squadrons, and the increases in the establishments of both personnel and machines for the various types add greatly to the difficulties of organising our air defences. For the operation of the new makes of machines landing grounds have to be constructed to much higher standards than those accepted as suitable two years ago, while accommodation both for personnel and machines and other operational facilities incidental to modern air defence are necessary on a far larger scale than was then envisaged. All these factors, I need hardly point out, add substantially to the cost of building up India's air defences. The formation and expansion of training institutions has gone ahead rapidly, and there has been a recent increase in the civil repair and maintenance organisation. Under the scheme for the creation of a reserve of Indian Air Force officers, to which reference was made

Last year, approximately 300 officers have been produced by the civil organisation and passed on to service training institutions, whence they should eventually be absorbed into active formations. The fullest use possible is being made of civil resources and the scheme inaugurated by the Director of Civil Aviation for pre-entry basic training for Indian Air Force mechanics is in full working order. Finally, the scheme for the assembly and manufacture of aeroplanes in India has made good progress. It is confidently hoped that the factory will complete its programme of fighter and bomber construction before the end of the present calendar year although considerable difficulties have been encountered in securing the release from America of the necessary materials, particularly since America entered the war. It has not yet been possible to secure from America all the materials needed for the programme of trainer aircraft and this may be delayed in consequence. In addition the factory is doing valuable work in carrying out major repairs to aeroplanes of many types.

11. To complete the picture of expenditure in the current year there now only remains for me to explain the increase of Rs. 1,72 lakhs in the civil expenditure. This increase would have amounted to Rs. 4½ crores but for a saving in interest charges of a little over Rs. 3 crores consequent upon the repatriation operations which were carried out last February. Of this Rs. 4½ crores increase, however, Rs. 1½ crores are accounted for by items which, while they figure as expenditure on the charges side of the account, are offset by corresponding receipts on the revenue side. The main items of this nature are Rs. 1,41 lakhs for the transfer of additional premia received under the War Risks (Goods) Insurance Act to the War Risks (Goods) Insurance Fund, due to the raising of the rate of premium from 1/32 per cent. to 1/16 per cent. and to the more extensive insurance of goods by merchants; Rs. 7 lakhs for the share of the higher match excise duty receipts payable to Indian States; Rs. 5½ lakhs for the payment to the Coal Mines Stowing Board of the net proceeds of the excise duty on coal and coke under the Coal Mines Safety (Stowing) Act; Rs. 2 lakhs required for increased production of salt; Rs. 3 lakhs representing larger payments to the I. C. A. R. due to an increase in agricultural cess receipts and a higher block grant to the Sugar Excise Fund following an increase in Sugar Excise revenue; and Rs. 6 lakhs spent on increased coinage, both on the Government of India's account and on behalf of other Governments. Of the balance of Rs. 3 crores, roughly Rs. ½ crore has been spent for obvious reasons on the provision of larger reserve stock of essential stores, such as currency note paper, security printing paper, stationery stores, etc. The remainder of the additional Civil expenditure has been incurred almost entirely in connection with the war. Thus expenditure on A. R. P. shows an increase of Rs. 92 lakhs, of which Rs. 84 lakhs goes as grants to the Provinces, Rs. 3 lakhs on A. R. P. schemes in centrally administered areas, and Rs. 5 lakhs for A. R. P. schools and other miscellaneous schemes. Equipment of the new Mint which is now being built in Alipore, Calcutta, to meet the rising war-time demands for coin both for India and for Allied Governments, is costing Rs. 26 lakhs. Rs. 14 lakhs excess under Civil Works has been necessitated by the need for additional buildings in New Delhi and Simla to provide accommodation for new departments or for expansion of existing departments as a result of the war. War-time expansion in other directions includes the Chief Controller of Imports, the Wheat Commissioner, the Controller of Coal Distribution, a Petrol rationing organisation, additional staff and overtime allowances in the Bombay and Calcutta Customs Houses, expansion of publicity, the Board of Scientific and Industrial Research, the Agent-General for India in the U. S. A. and so on. Last, but by no means least, an additional Rs. 64 lakhs is required

[Mr. C. E. Jones.]

for the expanded activities of the Supply Department and its subordinate organisations, regarding which the House will perhaps desire a little more detailed information.

12. The activities of the Department of Supply have expanded considerably during the past twelve months. While its main organisation has remained substantially unchanged, the Indian Stores Department, the Contracts Directorate and the temporary officers employed on purchase duties have for the duration of the war been merged into a single Purchase Branch with a view to utilising the available staff to maximum advantage. On the other hand it has been found necessary to divide the Textiles Directorate into two, one of which has been located at Bombay to deal exclusively with cotton textiles. During the coming financial year it is anticipated that about 700 million yards of cotton textiles will have to be purchased, which this Directorate will have to arrange by a system of bulk purchases in close co-operation with the industry. Clothing factories have multiplied ten-fold since the outbreak of war and are now turning out more than 8 million garments a month. The output of leather goods has increased thirty-fold. A new parachute factory has been established and the first Indian made statichutes have successfully passed the required tests. Timber extractions and purchases are rapidly expanding while many new chemicals are now in process of production in India for the first time. As regards munitions production, 20 new projects arising out of the recommendations of the Roger Mission have now been approved and are in process of execution, involving a capital outlay of about Rs. 12 crores, as a result of which new factories will be constructed and old ones expanded for the production in India of weapons, ammunition, steel and other stores urgently required for war purposes. The whole of the capital outlay on the erection and establishment of these factories will be borne by His Majesty's Government, although India will of course pay for such of the articles produced by them as are utilised for purposes of India's local defence. Railway workshops and trade workshops are being increasingly utilised, with the ready co-operation of industrial concerns and Railway Administrations, for the production of a large range of military requirements from armoured fighting vehicles and small auxiliary naval craft downwards. As a result of these various activities India will henceforth be self-supporting in respect of many items of war supply which hitherto have had to be imported.

13. I should perhaps say a word here on the subject of the application to India of Lease-Lend assistance from the U. S. A. Honourable Members must have been gratified to learn that, largely as a result of the activities of the Indian Purchasing Mission in the U. S. A. under the chairmanship of Sir Shanmukham Chetty, India has been admitted to the benefits of Lease-Lend facilities on the same terms as the United Kingdom and other members of the British Commonwealth of Nations. The indents placed for supplies on Lease-Lend terms up to the end of January 1942 amounted in value to roughly Rs. 47 crores of which, if all goes well, about Rs. 11 crores worth of goods are expected to arrive in India during the current year and three times as much during the coming year. In so far as stores received on Lease-Lend terms are utilised for the equipment of troops sent overseas or for other needs which are paid for by His Majesty's Government under the Financial Settlement, the benefits and obligations conferred by Lease-Lend will be passed on to that Government. In respect of such of the stores as are utilised for Indian purposes, whether by the Defence services, Civil Departments of the Central Government or Provincial

Governments, their value will be debited to the budgets concerned and corresponding credits taken to a suspense account. This accounting procedure is being followed in view of the fact that the precise nature of the obligations imposed by Lease-Lend facilities on the Governments making use of them has not yet been determined, and the suspense credits will therefore remain until the method of liquidation of Lease-Lend liabilities has been defined.

14. I come now to a consideration of the estimates of revenue for the financial year 1942-43. The only substantial variations from the revised estimates of revenue for the current year are in respect of customs duties and income tax. There can be little doubt that war developments in the Pacific will cause a degree of interference with our foreign trade which will be reflected in an appreciable drop in customs revenue. It is by no means easy to estimate the extent of the fall, but in circumstances as they are now we have decided to take the figure at Rs. 30 crores against the current year's revised estimate of Rs. 36 crores. The figure of Rs. 30 crores is inclusive of the proceeds of the additional import duty on raw cotton, estimated at Rs. 2 crores, which will be taken to the special fund for the relief of the short staple cotton situation. Against this, however, the yield from Income-tax and Corporation tax including surcharge is expected to increase by over Rs. 3 crores, while the collections of Excess Profits Tax have been put at Rs. 20 crores as compared with Rs. 8 crores in the current year. As a result of these and the various other smaller changes in the estimates, our total revenue on the existing basis for 1942-43 is expected to amount to Rs. 140,00 lakhs as compared with Rs. 129,62 lakhs according to the revised estimates for 1941-42.

15. The anticipated increase in the yield of Income-tax next year will result in a further increase in the divisible pool which, on the basis of our estimates, will amount to as much as Rs. 25,75 lakhs. Assuming that the sum to be retained by the Centre from the Provincial moiety will be maintained at Rs. 4½ crores, the share of Income Tax revenue payable to the Provinces next year comes to the record figure of Rs. 8,37 lakhs, as compared with the corresponding figure of Rs. 6,58 lakhs for the current year. For the sake of comparison I would like to remind the House that the amounts paid to the Provinces since the Niemeyer Award first began to operate have been Rs. 1,63 lakhs for the year 1937-38, Rs. 1,51 lakhs for 1938-39, Rs. 2,83 lakhs for 1939-40 and Rs. 4,54 lakhs for 1940-41. The present level of payments to the Provinces on account of Income Tax is therefore several times what it was before the war and, incidentally, is considerably higher than what Sir Otto Niemeyer calculated they would receive as their full half share of the divisible pool at the end of the ten-year devolution period.

16. Coming now to the expenditure side of the account for the year 1942-43, Defence expenditure chargeable to Indian revenues is expected to reach a total of Rs. 133,00 lakhs which, following the usual classification, may be expressed thus :

	(Rs. in lakhs.)	
	Revised, 1941-42.	Budget, 1942-43.
(1) Basic normal budget	36,77	36,77
(2) Effect of rise in prices on (1)	4,24	6,52
(3) India's war measures	53,03	81,30
(4) Non-effective charges	8,41	8,41
Total	102,45	133,00

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For the reasons which I have already given, items (1) and (4) remain unaltered, while the increase in the case of item (2) merely reflects the anticipated further rise in the general price level during the coming year. The major increase occurs under item (3) and is occasioned by the growth of our war measures on the lines which I have already explained. The increase would have been higher by Rs. 1½ crores but for the fact that contributions totalling that amount from the Viceroy's War Purposes Fund are anticipated during the year. Great as is this total of Rs. 133 crores, it represents only about one-quarter of the gross Defence expenditure which is likely to be brought to account in India's books during 1942-43; that is, the amount of expenditure on Defence services and supplies that we expect to recover from His Majesty's Government next year under the operation of the Financial Settlement exceeds the huge total of Rs. 400 crores. The greater part of this latter amount represents expenditure connected with the maintenance or provision of forces overseas in the interests of the security of India against external aggression. In addition to bearing this vast expenditure His Majesty's Government have undertaken to supply to India free of charge large quantities of aeroplanes, vehicles, guns and other equipment required in connection with the expansion of India's fighting forces, naval, air and military. The total value of such free supplies which are expected to be received by the end of 1942-43 is roughly Rs. 60 crores.

17. Civil expenditure in 1942-43 is expected to amount to Rs. 54,07 lakhs, an increase of Rs. 9,63 lakhs over the revised estimate for 1941-42. Much of this large increase is however more apparent than real for the reason to which I have already made reference in considering the revenue estimates, *viz.*, the necessity for accounting purposes of passing the transactions relating to special funds through the revenue and expenditure accounts, thereby swelling both sides of the account. Thus the receipts from War Risks Insurance premia, the enhanced import duty on raw cotton and the cess on exports of agricultural produce, which are shown as expenditure under the relative heads of account for transfer to the special funds next year, amount to Rs. 3,24 lakhs, Rs. 2,00 lakhs and Rs. 18 lakhs respectively. The greatest real increase is in respect of expenditure on Civil Defence for which Rs. 4 crores have to be provided as against our revised estimate for the current year of a little over Rs. 1 crore. A new scheme of allocation of the cost of A. R. P. measures has been drawn up by the Central Government in consultation with the Provincial Governments, which has been designed to secure that the financial assistance given by the Centre should be determined in the light of the magnitude of the A. R. P. expenditure to be incurred by each Provincial Government and the ability of the Province to shoulder this extra burden, having regard to the additional resources deriving from the larger distribution of Income-tax. Under the scheme every Provincial Government will in each financial year itself bear its Civil Defence expenditure up to a specified amount, which is to be fixed in a certain broad relation to the Provincial revenue receipts. Expenditure over and above this initial slab will be divided into further slabs of which the first is to be shared 50 : 50 by the Central and the Provincial Governments, the next 75 : 25 and anything beyond that 87½ : 12½. I need hardly stress the point that the estimates of A. R. P. expenditure are at present largely speculative and purely tentative since the amount to be spent will inevitably depend very much on the future course of events in the Eastern theatre of war.

Of the remaining factors contributing to next year's increase in Civil expenditure I will confine myself to a brief mention of the more outstanding items. Half a crore of the increase arises out of the expansion of the technical

training scheme for skilled artisans so as to provide for the training of 48,000 men by the end of 1942-43 in place of the 15,000 men contemplated under the original scheme. A special provision of over a quarter of a crore has been made for expediting the civil aviation programme in addition to the annual subvention of Rs. 35 lakhs. An extra half a crore has also had to be provided next year for the continued expansion of the Supply Department's activities. Interest charges will be increased to the extent of Rs. 175 lakhs as compared with the revised estimate for the current year, although still showing a saving of Rs. 134 lakhs as compared with the budget figure for the current year. For further details of the civil estimates for 1942-43 I must refer Honourable Members to the Explanatory Memorandum on the Budget.

18. The budgetary position for the coming year on the existing level of taxation can now be summarised as follows :—

	(Rs. in lakhs.)		
	Revised, 1941-42.	Budget, 1942-43.	Improvement (+) Worsening (—).
Net Defence expenditure	102,45	133,00	—30,55
Civil expenditure	44,44	54,07	—9,63
Total expenditure	146,89	187,07	—40,18
Total revenue	129,62	140,00	+ 10,38
Deficit (—)	—17,27	—47,07	—29,80

There is thus a prospective deficit on revenue account of Rs. 47,07 lakhs, but before I deal with the problem of this deficit I will follow the usual procedure of giving at this stage an account of our ways and means position, which is a matter of considerable importance in the scheme of war-time finance.

19. Honourable Members are, I trust, already acquainted with the details of our Defence Loan programme, for during the past year we have taken great pains at considerable expense to publicise them throughout the length and breadth of the land. By far the greater part of the amount subscribed this year has been to the Second Defence Loan, i.e., the 3 per cent. Defence Bonds, 1949-52, which has been continuously on tap from the 1st February 1941 to its recent closure. Up to the end of January 1942 this loan has produced Rs. 58,10 lakhs, the interest-free Bonds Rs. 2,67 lakhs, and the Post Office 10-year Defence Savings Certificates Rs. 4,67 lakhs. The total investment in our Defence Loans from June 1940 when they were first issued to the end of January 1942 amounts to Rs. 110,30 lakhs.

20. Great though this total may be, there is an imperative need for a rapid and continuous increase in the rate of saving and investment. The circumstances of the time and the interests of the country alike demand it. Borrowing, and borrowing on a large scale, is necessary for the financing of India's defence expenditure which is now approximating to Rs. 40 lakhs a day and is still growing. But that is only a part of the picture. There is also the very much larger expenditure on account of supplies and services to His Majesty's Government and other Allied Governments which has assumed the huge dimensions mentioned earlier in this speech. It is true that we receive payment in sterling for these supplies and services, but the fact remains that the equivalent amount in rupees, which now has to be measured in units of Rs. 100 crores, has to be paid out within the country to those who have provided them. The result is inevitably a very large increase of purchasing power in the hands of the people of the country. With a large part of the productive power of the country devoted to the war effort, and with imports from outside severely restricted by war conditions, it is obvious that purchasing capacity must rapidly outgrow the limited available

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supply of consumers' goods; and if it is utilised in intensive competition for those goods, the only effect will be the forcing up of prices. Such a state of affairs could benefit no one, and would prove a definite hardship to the many with small fixed incomes. On the other hand, if claims to consumers' goods are postponed to more propitious times when the supply of goods and services can be expanded in satisfaction of the wider demand, not only will the general economy of the country be preserved in a sound and healthy condition but the people will have provided themselves with a reserve which may well prove invaluable for meeting the uncertainties of the post-war period. It is therefore of fundamental importance that saving on a national scale should be stimulated and encouraged by all who have the interests of this country and its peoples at heart.

21. During the current year the outstanding balance of the 3 per cent. Bonds, 1941, amounting to Rs. 10½ crores was repaid, Rs. 8¼ crores by conversion and the remainder in cash. Apart from the undated sterling loans, to which I shall presently refer, the only loan we have the option of repaying next year is the 5 per cent. Loan, 1942-47, but of this the balance still outstanding is only Rs. 65 lakhs.

22. Intimately connected with our ways and means position is the question of the repatriation of India's sterling debt. In my speech a year ago I explained at some length the lines of general policy in this regard, the advantages to India resulting from the replacement of external obligations by internal debt, and the financial implications of the repatriation of the six dated sterling loans. I have no wish to weary the House by repeating what I said then, but as the plan for the rupee financing of that important operation could at that stage be indicated only tentatively I ought perhaps to complete the story now. The total terminable stock acquired amounted to Rs. 97 crores, leaving only Rs. 15 crores outstanding as being outside the scope of both the British and the Indian Vesting Orders. Sterling payments however amounted to only £66·3 million, the amount coming under the Indian Order being Rs. 14·56 crores of which Rs. 13·30 crores were paid for by counterparts and the small balance in cash. The Reserve Bank naturally had no difficulty in providing the sterling required, in view of its large sterling resources but the crux of the problem was to devise a plan by which the Government could make rupee payment for that sterling without unduly depressing security prices and thereby endangering our cheap money policy, while at the same time avoiding the financially doubtful course of large scale replacement of long-dated maturities by very short-term commitments. This was secured by the creation of rupee counterparts, about half of which were taken over by the Reserve Bank. The other half was held by Government who paid the balance due to the Reserve Bank from its balances, supplemented by ways and means advances, and by *ad hoc* treasury bills. Thus both the Government and the Reserve Bank were provided with a portfolio which could be sold gradually to meet market demand.

23. Once these initial arrangements had been completed the whole position was brought under survey, and such stock as was considered to be in excess of the absorptive capacity of the market over the next few years and was not required for ensuring the marketability of counterpart stocks in the hands of the public was cancelled. The amount of stocks so cancelled amounted to some Rs. 47 crores, and a further amount of stock was converted into existing loans of roughly corresponding maturity for which there was known to be a

fairly sustained demand from the market. The combined result of these operations was an increase of Rs. 92 crores in our rupee debt and of Rs. 3 crores in our rupee interest charges against a reduction in sterling debt by Rs. 135 crores and sterling interest by Rs. $5\frac{1}{2}$ crores. As opportunity occurred during the year, by arrangement with the Reserve Bank, *ad hoc* treasury bills taken up by the Bank in connection with the repatriation were gradually cancelled against the transfer of sterling from the Banking Department to the Issue Department. In the result by December 1941 the Reserve Bank held only Rs. 2.71 crores of *ad hoc* treasury bills. Meanwhile counterparts on Government's account were sold to the public as they required them, and by the end of December last, out of some Rs. 139 crores of rupee counterparts created since repatriation was first undertaken, Rs. $47\frac{1}{2}$ crores had been cancelled, Rs. 51 crores were in the hands of the public, a little over Rs. 31 crores were held by the Reserve Bank and Rs. $9\frac{3}{4}$ crores were held on Government account. As our outstanding of treasury bills actually decreased by Rs. 14 crores between the 1st March 1941 (*i.e.*, prior to the repatriation payments) and the end of January, 1942, we may conclude that the cash payments on account of the counterparts which were cancelled have ultimately been financed almost entirely from Defence Loan proceeds. We may, therefore, claim that the bulk of the floating debt incurred for the financing of the first instalment of repatriation has already been funded, and there is good cause for gratification that so large and so complex a transaction was carried through with such remarkable smoothness and with little or no disturbance to the market.

24. Towards the end of last December we were able to adopt, again with the assistance of His Majesty's Government, a somewhat similar scheme for the repatriation of the remaining non-terminable portion of our sterling debt. The $2\frac{1}{2}$ per cent. and 3 per cent. stock totalling some £70 million (market value) is being compulsorily acquired under British and Indian Vesting Orders as in the first scheme of repatriation, while the outstandings of the $3\frac{1}{2}$ per cent. stock amounting to another £70 million will be redeemed on the 5th of January, 1943 under a year's notice which has already been given. Some criticism has been directed against the Government for not applying the machinery of compulsory acquisition to the $3\frac{1}{2}$ per cent. stock as in the case of the other stock, but it must be remembered that compulsion is an extraordinary measure which cannot be resorted to without solid and substantial reasons. Since the $3\frac{1}{2}$ per cent. stock was standing very near to par and was redeemable at any time on a year's notice, there was no sufficiently valid reason which could be urged on His Majesty's Government to use their special war-time powers to acquire it for us. After this second measure of repatriation has been carried through, practically the whole of India's external obligations will have been liquidated to the immense strengthening of India's credit position.

25. In spite of the vast scale of these debt repatriation transactions there is no room for apprehension as to their effect on the Reserve Bank's sterling resources, in view of the rate at which sterling has been and is accumulating with the Reserve Bank on account of the large war demand for supplies from India to which I have already referred. I will give a few figures by way of illustration. Purchases by the Bank during the first ten months of the current year amounted to approximately £57 million. At the time of the budget for the current year we estimated a net refund by the Secretary of State of £26 million. Since then, however, the volume of recoverable war expenditure and purchases on behalf of His Majesty's Government and Allied Governments has increased continuously, and the net refunds for the year are now expected to aggregate £53 million after providing for the repayment of the $2\frac{1}{2}$ per cent.

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and 3 per cent. undated sterling loans next month. For next year the net refunds by the Secretary of State are estimated at £164 million after allowing for the repayment of the remaining undated sterling loans and for the payment of £13 million for the purchase of the Bengal and North Western Railway and the Rohilkhand and Kumaon Railway. There can be no doubt that the sterling required this year and next for payments in connection with our second repatriation scheme will be available without any strain on the Reserve Bank's sterling resources.

26. In the matter of sterling debt repatriation there is a tendency in some quarters to concentrate attention on the revenue aspect resulting from the reduction in interest charges. This fact however, as I explained last year, is largely incidental and to a certain extent temporary, being merely the natural result of the method of finance employed, viz., payment to holders of long-term securities out of short-term obligations which will be gradually replaced by funded loans. It is difficult to give any precise estimate of the revenue effect of our second repatriation scheme since it depends on the terms on which we can fund our short-term obligations. On present indications, however it is possible that the net saving to the revenue budget under interest will be of the order of Rs. 90 lakhs. In addition to this the Reserve Bank's profits will increase as a result of its holding for a time higher interest bearing rupee securities in its Issue Department instead of short-term sterling securities of lower yield. These surplus profits of the Reserve Bank will ultimately be transferred to Government and may possibly amount to as much as Rs. 50 lakhs.

27. As regards our treasury bill position, the budget for the current year contemplated a net decrease in outstandings of Rs. 11½ crores. The decrease to the end of January 1942 has actually amounted to Rs. 23½ crores. The improvement has been due partly to better Defence Loan receipts than we had counted upon and partly to sales of rupee stock held by the Government. Furthermore, the Government have realised Rs. 10 crores from the sale of silver in India. Next month, however, in connection with the repayment of the 2½ per cent. and 3 per cent. undated sterling loans we may have to create additional treasury bills to the extent of Rs. 39 crores but this will present no difficulty in view of the abnormally low level of outstandings at the present time.

28. The net discharge of cash certificates this year is not likely to be appreciably more than the budget estimate of Rs. 6 crores and we are adopting for next year the figure of Rs. 5 crores. On the other hand, Savings Bank transactions are likely to result in a net outgo of Rs. 7 crores as against the net credit of Rs. 2 crores assumed in the budget. For next year we are assuming a net withdrawal of Savings Bank deposits of Rs. 2 crores.

29. I must now return to a consideration of the gap with which we are faced in the coming financial year between our anticipated revenue and our estimated expenditure on revenue account. By way of context I would remind Honourable Members that for the year 1940-41 we budgeted for a nominal surplus of Rs. 5 lakhs and in the actual result realised a deficit of Rs. 6½ crores. For 1941-42 we budgeted for a deficit of Rs. 13½ crores, but according to the revised estimates the deficit will amount to Rs. 17½ crores. Now for the year 1942-43 on the estimates we have made and at the existing level of taxation we are faced with a prospective deficit of the order of Rs. 47 crores, or well over half the total pre-war budget of the Government of India. Serious as the problem of this deficit is, the Government feel, for reasons of

which I have already given some indication, that the situation which now confronts them is of wider dimensions than that of mere balancing of Government revenue against Government expenditure. There can be no doubt that those tendencies which are only too characteristic of war-time economy are beginning to operate in India, as they are operating in practically every country in the world today. Although it is probably true to say that in India the process has not gone either so fast or so far as in many other countries, where counter-action of a drastic nature has had to be taken, the fact remains that the tendencies are in evidence here and the Government are satisfied that the stage has been reached when it is their clear duty at least to make a beginning with measures, in addition to the ordinary process of taxation, of a kind which will assist in relieving the pressure of the enhanced volume of purchasing power on the limited supplies of goods and services which in present conditions are available for consumption. It is in the light of this broad conclusion that the budget proposals which I will now proceed to explain have been framed.

30. The first proposal is that incomes of from Rs. 1,000 to Rs. 2,000 per annum shall be made liable to income-tax, but that the tax will not be leviable if the assessee deposits in a Savings Bank account a prescribed sum which works out to approximately $1\frac{1}{2}$ times the amount of tax which he would otherwise have to pay. The proposed rate of tax is 6 pies in the rupee on the excess of the year's income over Rs. 750. The sum to be deposited in the Savings Bank account to discharge the liability to tax is Rs. 1 for every Re. 25 of the excess of income over Rs. 750. Thus on an income of Rs. 1,500 the tax would be Rs. 23-7-0 and the optional Savings Bank deposit would be Rs. 30. The intention is that the deposit should be made in the Post Office Defence Savings Bank, from which sums cannot ordinarily be withdrawn until the expiry of 12 months after the end of the war, and the deposits in which earn interest at the rate of $2\frac{1}{2}$ per cent. per annum. It will be realised that this is a scheme of saving rather than of taxation, and is considered to be the most suitable way of tackling the problem outlined above in the case of persons with incomes below the existing income-tax limit. The option allowed being of such a favourable nature, the revenue yield must be taken as nil.

31. The second proposal is in respect of the Central surcharge on incomes exceeding Rs. 2,000 per annum. Hitherto the surcharge has been applied in the form of a flat percentage on the basic rates of income-tax and super-tax throughout the whole range of incomes. The percentage method however inevitably results in a rapid steepening of the rate of progression of the incidence of the tax up the income-tax scale. With the basic scale itself highly progressive, as it has been in India since 1939, there are obvious limitations to the extent to which any further steepening can proceed. It is therefore proposed to abandon that method now and to fix the income-tax surcharge for next year at 6 pies in the rupee on the first slab of taxable income between Rs. 1,500 and Rs. 5,000, at 9 pies in the rupee on the next Rs. 5,000, 1 anna 2 pies in the rupee on the next Rs. 5,000, and 1 anna 3 pies in the rupee on the balance of total income. The last-named surcharge is a 50 per cent. surcharge, and similarly the surcharge proposed on the rates of super-tax are equivalent to a 50 per cent. surcharge, while at the same time corporation tax is to be raised to $1\frac{1}{2}$ annas in the rupee. Since, for the reasons I have just stated, the rate of surcharge in the lower ranges of income will be somewhat in excess of 50 per cent. it is proposed that a portion of the tax paid in respect of incomes up to Rs. 6,000 will be funded and repaid to the assessee after the end of the war. The amount to be so funded will be one-half per cent. of the assessee's total income. Thus on an income of Rs. 3,000 per annum the gross tax would be Rs. 117-3-0, of which an amount of Rs. 15 would be funded. The way in

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which these proposals will work out in practice will be apparent from the statement which forms Part III of the Explanatory Memorandum. It will be seen that the incidence of the tax progresses steadily from less than 2 per cent on an income of a little over Rs. 2,000 to 85 per cent. on an income of Rs. 30 lakhs a year.

32. The third proposal in the sphere of direct taxation relates to the Excess Profits Tax. It is proposed that the profits of a further period of one year shall be subjected to this tax, and that the rate applicable to such profits shall be the existing rate of 66 $\frac{2}{3}$ per cent. One modification is however proposed. The Government are impressed with the need for stimulating the incentive to economy and efficiency in the administration of business ; they also realise the importance of enabling industry to build up a reserve for its rehabilitation and re-equipment after the war ; and they are convinced of the necessity for immobilising during the period of the war as much as possible of the excess profits earned so as to prevent postponable private expenditure from exerting an undesirable influence on the price level. In order to assist in securing these several, and in a sense mutually incompatible, objectives the Government are prepared to contribute an amount not exceeding one-tenth of the net excess profits tax ultimately paid at the rate of 66 $\frac{2}{3}$ per cent. (*i.e.*, the odd 6 $\frac{2}{3}$ per cent.) provided the assessee deposits double the amount so contributed. The assessee's deposit will be repayable within 12 months after the end of the war and will earn simple interest at the rate of 2 per cent. per annum. The Government's contribution will also be paid out after the war, at such time and subject to such conditions as may be determined. The Post-War Reconstruction Committee will be asked to advise on the formulation of these conditions. Both the Government contribution and the interest on the assessee's deposit will be treated as taxable receipts in the year in which they are paid.

33. In the sphere of indirect taxation, the main proposal is to levy a 20 per cent. emergency surcharge over the whole field of customs import duties in view of the anticipated heavy shortfall in this, for long the main pillar of Central revenues. Raw cotton will be exempted from this surcharge, since it has only recently been subjected to an additional duty for a special purpose. Motor spirit will constitute another exception as being the subject of separate treatment, since it is proposed to enhance the excise duty on motor spirit by three annas a gallon with a corresponding automatic increase in the import duty. A few imports from Burma will also have to be exempted from the general surcharge on account of the provisions of the trade agreement concluded with that country last year, while the import duty on salt will continue at the same rate as the duty now levied on indigenous salt. These proposals will, by virtue of a declaration under the Provisional Collection of Taxes Act, come into effect at once.

34. Lastly, certain increases are proposed in the posts and telegraphs rates, *viz.*, an increase in the ordinary letter rate from 1 $\frac{1}{2}$ annas to 1 $\frac{1}{2}$ annas, the postcard rate remaining unchanged ; an increase in the minimum charge for an ordinary telegram from 10 annas to 12 annas and for an express telegram from Rs. 1-4-0 to Rs. 1-8-0 ; also increases in telephone rentals, and the surcharge on trunk call fees to be raised from 10 per cent. to 20 per cent.

35. It is difficult, if not impossible, to estimate with any approach to accuracy the additional revenue which will be derived from these various measures. Much depends upon the future course of world events. On the best information available to us we put the net addition to revenue from the proposals relating to direct taxation at Rs. 5,30 lakhs, excluding repayable

deposits and refundable elements which are to be treated as borrowings. Similarly we estimate the additional revenue in the field of indirect taxation at Rs. 5,70 lakhs, and that from the increases in posts and telegraphs rates at Rs. 1,00 lakhs. The total additional revenue from all the proposals thus comes to Rs. 12 crores, or about one-quarter of the prospective deficit with which we were faced, leaving an uncovered deficit to be met from borrowings of Rs. 35,07 lakhs. This will mean a substantial addition to the public debt but, as I stated at the beginning of this speech, it has to be regarded against the background of the growing intensity of India's war effort and of the resulting changes in her economy, which on balance have undoubtedly been greatly to her advantage. However dark and anxious the present may be, there are solid grounds for a spirit of confidence and sober optimism that India will emerge strong and well-equipped to play a worthy part in the new world that lies ahead after victory has been achieved. (Applause.)

THE HONOURABLE THE PRESIDENT : Before I adjourn the Council, I wish to remind the Honourable Members that a group photograph will be taken on Thursday, the 5th March, 1942, at 10-30 A.M.

The Council then adjourned till Eleven of the Clock on Thursday, the 5th March, 1942.
