M.R.O. 1—77,000—3-6-37.

(1) Number of pages 11

(2) Date of repair

(3) Initials of the Referencer

# MADRAS RECORD OFFICE.

## Government of Madras.

Public works DEPARTMENT.

G.O. No. 83 Press Mis.

167-68

Dated 12 1 1871.

**Not to be folded or roughly handled**

No. 167. Read the following letter from the Deputy Secretary to the Government of India, Public Works Department, (Railway,) to the Secretary to the Government of Madras, Public Works Department, (Railway,) dated Simla, 2nd September 1870, No. 1,515-R.:—

REFERRING to the Despatch from the Secretary of State to the Government of Madras, No. 9, Railway, dated the 28th July 1870, I am directed to forward, *confidentially*, for the information of His Excellency the Governor in Council, copy of a despatch addressed by the Government of India to the Secretary of State on the 12th August 1870, No. 80, Railway, regarding the relinquishment by the State of the right of purchase of certain of the guaranteed Railways at the end of the first 25 years of the term of the contracts.

2. I am specially to request that this document may be regarded as strictly confidential, and every care taken against its being made public in any way.

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From the Government of India, to the Secretary of State for India, dated Simla, 12th August 1870, No. 80-R.

IN your Grace's Despatch No. 42 of 1869, on the subject of Railway extensions, Her Majesty's Government affirmed that the time had arrived, when, both in raising and expending such additional capital as may be required for new lines of Railway in India, the Government should secure for itself the full benefit of the credit which it lends, and of the cheaper agencies which ought to be at its command. It was added that the formation of branches and of subsidiary extensions of existing lines, where such extensions are of comparatively small extent may, perhaps, be more conveniently left in the hands of the guaranteed Companies.

2. Your Grace further assented to our recommendations that, in future contracts with guaranteed Companies, (1) the defective control of the Government under existing contracts should be met by reserving to Government the simple power of taking over the works from the Companies, in the event of their not being constructed, as well as worked, to the satisfaction of Government; and (2) the net profits above the guaranteed interest should be divided equally between the Government and the Company during the entire term of the contract, all mention of the repayment of guaranteed interest being dropped as unnecessary. While declaring that the first of these conditions ought to be made applicable in all cases, your Grace limited the application of the second to all cases in which the new amount of capital to be expended is sufficient to make it worthwhile to establish a separate system of account.

3. Accordingly, it is with much satisfaction that we have noticed that, in offering important extensions to the Bombay, Baroda, and Central India, and to the Great Southern of India Railway Companies, these conditions have been made applicable and have been accepted by those Companies; also that, with the new Carnatic Company, the contract entered into with the Oudh and Rohilkhund Company has been further improved by the introduction of these conditions.

4. With reference, however, to the first of these stipulations, it should be borne in mind that the means last suggested, and by your Grace adopted, of nullifying to some extent, in future contracts, the evils of the defective control of the

Government under the old contracts were the result of a compromise. The defects in this respect of the old contract had been brought to the prominent notice of Her Majesty's Government, on more than one occasion, during the Viceroyalty of the late Lord Canning. They were again specially dwelt upon in the Minutes by the Members of Government, which were laid before Her Majesty's Government with our Despatch No. 125 of 1867, and at considerable length in the Minute of His Excellency the late Viceroy, dated the 16th August 1867.

Despatch No. 90, dated 24th November 1868, paragraph 13.

Sir Stafford Northcote, however, did not assent to the measures proposed for obtaining a better control over the officials of the Railway Companies, being of opinion that no body of shareholders, or their Directors, are ever likely to consent to look upon themselves and their officers as mere agents and servants of the Government, imperatively bound by its behests, and liable in the case of officers of the Company to suspension and removal at its pleasure.

5. With the view of meeting these objections, the Government of India suggested the condition already referred to, which has been not only accepted, but acted upon in the cases quoted.

6. A little consideration will, however, suffice to show that this condition has the inherent defect of reserving a power of such magnitude that it should only be exercised in very exceptional and extreme cases. As remarked in our Despatch No 122 of 1868, the contracts have hitherto been made by the Secretary of State, but their practical working is carried out under our immediate supervision. The defects of existing arrangements and especially the absence of any real power over the officials in this country of the Railway Companies has, consequently, been realized by us more fully than they possibly can be by others. Differences arise, references to England become necessary, and delays ensue prejudicial to efficiency, and productive of tedious correspondence.

7. The power of "possession as a remedy" now to be reserved in the case of construction, is already reserved in the old contracts in the case of working; but it would be exceedingly difficult to justify the exercise of such an extreme power in order to compass the removal of an individual Railway official, whose obstructiveness or incompetency is more patent to a disinterested Government on the spot, than to a Board of Directors at a distance, dependent, perhaps, on that very official for an account of his doings.

8. It is not our present object, however, in making these remarks that your Grace should re-consider the condition assented to, for we believe that it may be a check upon extravagance, if the Companies into whose contracts it may be introduced be given clearly to understand that the power will not be suffered to become a dead letter. But these remarks will explain how it is that the power of "possession as a remedy," as provided either in the old or in the new contracts, cannot, in our opinion, obviate all those defects of control, the removal of which was so strongly insisted upon in the Minutes of 1867.

9. The fact that these defects do not appear to be otherwise removable is one reason for making it desirable that the guaranteed lines should become the absolute property of the State. But we further hold that, in an administrative point of view,



circumstances might probably arise when it would be highly advantageous to the public as well as to the State that these Railways should, as soon as possible under the contracts with the Companies, become the property of the State. Your Grace will not, therefore, be unprepared to find that we cannot regard, otherwise than as inexpedient, any measure which shall have the effect of depriving the State of its option under the contracts of acquiring possession of the existing Railways, or even of postponing the time when that option can be exercised.

10. It is with much regret that we have learnt, partly from the recent reports of the Directors of the Madras and the East Indian Railway Companies, and generally from the public prints that, in consideration of the guaranteed Companies surrendering their right to a reversion of the second moiety of surplus profits (thereby allowing of a perpetual equal division between the Government and the Companies of all surplus profit which may be earned in any half-year beyond the guarantee,) your Grace has not only agreed to cancel the whole existing debt against the Companies for guaranteed interest advanced (and for simple interest accrued thereon,) and in future to meet the charge for guaranteed interest without taking account against the Companies of any deficiency between the amount thereof and the net earnings in each half-year, but has relinquished the right which the Government possess under the contracts of purchasing the Railways at the expiration of the first 25 years of the term.

11. The East Indian Railway Company appears to have declined the offer, and late as it is, it may not, therefore, be altogether useless for us to place on record our views of the policy of this transaction. But in any case it is the obvious duty of the Government in India, which is responsible for the finances, to protest in behalf of the tax-payers of India, very respectfully, against the adoption of any purely financial measure without the opportunity having been afforded us of previously expressing our views on the subject.

12. The suggestion as to sharing surplus profits throughout the term of the contract having emanated from the Government of India, it might appear that the negotiations that have been carried out with the old guaranteed Companies, of which this condition forms an element, had also in some degree originated with us. That such is not the case is clear alike from our Despatches Nos. 122 of 1868 and 24 of 1869, and your Grace's reply to the latter No. 42 of 1869. It was manifestly with special reference to future Railway undertakings under guarantee that we advocated a modification in the terms relating to the appropriation of surplus profits.

13. We are not insensible to the simplification of accounts that would result from the adoption, on the old lines as well as on new lines, of this modification of the contract in respect of the manner of dealing with surplus profits and guaranteed interest advances, and we should regard its acceptance by the other Companies with the same satisfaction as we have expressed in the case of the Great Southern of India, and Bombay, Baroda, and Central India Companies, provided it be not hampered with conditions assented to under the impression that the Companies had, in agreeing to it, conceded something to the Government; for, as will be seen in the sequel, there is not, in our opinion, any probability of advantage beyond that of account, to either party to the contract, from its adoption.

14. The East Indian Railway is the most prosperous of the guaranteed undertakings, and has deferred its acceptance of the offer that has been made to it. The prudence of this hesitation will be duly proved as time lapses, but it may be as well to notice that the average rate of profit on this Railway must be 7¼ per cent. throughout the remainder of the term of the contract, in order to repay its present guaranteed interest debt, omitting the present simple interest debt, probably not less than one million sterling. At present the profits of this Railway slightly exceed the guarantee in each alternate half-year, and the average above arrived at implies that the profits must rise to at least 9½ per cent. by the end of the term. It is very evident that this Company, in consenting to share profits with the Government throughout the term of the contract instead of until its debt is extinguished, would have little in its hand to negotiate with.

15. And, taking all the lines together, it is found that to pay off the total guaranteed interest debt (omitting the simple interest debt) within the term of the contracts, the average rate of interest throughout the remainder of the term must be rather over 7¼ per cent. The average profit of all the lines realized last year was not quite 3¼ per cent., so that the rate must rise to at least 11¼ per cent. by the end of the term.

16. Consideration of the foregoing statements as well as of the results of the negotiations of last year with the Great Southern of India, and Bombay, Baroda, and Central India Companies make it abundantly evident that, in consenting to share with the Government the surplus profits throughout the term of the contracts, the old Companies concede nothing; and as any advances remaining unliquidated at the period at which the Railways may come into the possession of Government, whether by purchase or otherwise, cannot be recovered from the Companies, the Government also have nothing to concede to the Companies in this respect. We arrive, therefore, at the conclusion that, saving in respect of simplification of account, the advantage of which is common to both, neither party to the contract has any basis of negotiation derived from the modifications that have been agreed to in regard to the application of surplus profits, or the method of dealing with advances of guaranteed interest in excess of net earnings.

17. When, then, the Government consents to waive its power of purchase at the end of the first 25 years, what have any of the Companies to offer on the other side? With two exceptions,—the Madras and the East Indian Companies,—literally nothing! They each consist of two undertakings with separate capital accounts, the amalgamation of which is to some extent desirable, so as to simplify accounts as well as to eliminate all questions of allocation of charge, whether capital or revenue, between the two lines. Looking to the few years that need only have elapsed before the Government could, under the contract, have exercised the option of purchase, we have no hesitation in declaring that these minor advantages would be bought too dearly on the terms offered.

18. The relinquishment of the option to purchase the Railways at the expiration of the first 25 years appears to us, therefore, to be a concession, inexpedient and uncalled for under the terms of the contract in every case. We are apprehensive that the policy which has dictated this measure, if not inconsistent with the decision arrived at scarcely a year ago, in favour of the extension of Railways



by the direct agency of the State, is opposed in a great degree to the reasons on which our recommendation in favour of that course was based, and which we hoped had been completely accepted by Her Majesty's Government.

19. The immediate effect of the measure is to prolong the existence of the old guaranteed Railway Companies for at least 25 years longer. In the contracts more recently entered into with the Oudh and Rohilkhund and the Carnatic Companies, the Government have been careful to secure the power of purchase, first after 20 years, and then after every succeeding 10 years, but under the contracts with the old Companies the State had the option of purchase at two periods only. One of these opportunities has been deliberately abandoned, apparently in the case of all the Companies, excepting the East Indian, and but one opportunity of withdrawing from the disadvantages of the system now remains to the Government. Should the circumstances of the period render purchase at that particular moment inexpedient, the guarantee system of 1849 will be perpetuated for 100 years, without, so far as we are capable of forming a judgment, any compensating advantage being secured to the State.

20. We have said that the measure is not in any way called for under the contract. The contracts are the record of certain terms on which at various periods, in some cases more than 20 years ago, capitalists have found it convenient to subscribe funds for the construction of Railways in India. The terms of the contracts were the subject of long consideration, and may be said to have been dictated by the state of the money market at the time they were entered into. The fact that one party in the enjoyment of terms, certainly not unfavourable to itself, has performed its part of the contract, is no reason that the other contracting party should grant concessions, even supposing that the Government, as trustee for the Indian tax-payers, were justified in rendering more unfavourable to itself a contract under which it suffers the whole loss, while the Companies reap the whole direct profit.

21. But the nature of the negotiations, so far as they are known to us, forbid the idea that the matter has been regarded by the State, at least, as involving on its part concessions without corresponding compensation. There is, moreover, no apparent object to be served by making concessions. The credit of the Government never was better: the undertakings of these Companies are approaching completion; their demands on the money market have almost ceased, and their stocks are quoted at a considerable premium.

22. It is, therefore, in vain that we seek to discover the grounds which have actuated Her Majesty's Government in this matter; and, looking at the stage at which it has arrived, as evidenced by the interpellations in Parliament, we cannot but regret that no opportunity was afforded to us of placing your Grace in possession of the views we entertain on this important question.

23. We have already explained that our opinions incline to the view that many, if not all, of the guaranteed Railways might with advantage become, at an early date, the property of the State, but this is a matter on which opinions may differ. When, however, the financial bearings of the case are regarded, we venture to think that there can be no room for difference of opinion as to the expediency of holding to the terms of the contract, so that the Government should have the

option of exercising the power of acquiring possession of the Railways as the period presents itself for each. Whether the Government would exercise the power must, of course, depend on circumstances at the time.

24. One result of the purchase by the State of the guaranteed Railways would be the abolition of the seven different Boards of Directors in London, and the substitution of another agency in their place. Although this would lead to a large saving of money, we do not mean to imply that the expenses of these several Boards are excessive, and reference to the 33rd paragraph of the Minute of the 16th August 1867 of His Excellency the late Viceroy, will show how far an annual investment of a comparatively small sum of money, if regularly made over a prolonged period, will go in reducing a large capital.

25. Under the terms of the contract, the Government must, in the event of purchase, pay the full amount of the shares and capital stock calculated according to the mean market value in London of such shares or stock during the three years immediately preceding; but in lieu thereof, the Government may, during the residue of the term of 99 years, pay an annuity, the rate of interest which shall be used in calculating such annuity being determined by the average rate of interest during the preceding two years received in London upon public obligations of the Indian Government.

26. Calculations show that with money at 4½ per cent., we could afford at the end of the first period of 25 years to redeem the capital at 110⅝, or to pay an annuity in commutation thereof throughout the remainder of the term, thus discharging the principal as well as interest. Similarly, with money at 4 per cent. (at about which our obligations now stand in the London market), we could afford to redeem the capital at 123⅜. The Railways would, thereupon, become the property of Government to be managed exactly as it chooses, and the entire surplus profits that may accrue on the more prosperous lines would pass to the State.

27. But if, with money at 4 per cent., the Railway stock should be redeemable at 110, the annual saving of charge to the Indian Government would be £283,000, taking the total guaranteed capital at £80,000,000; and at 115, the saving would be £112,800. A fair comparison should not, however, neglect consideration of the sum that ought to be put by yearly to redeem the Railway guaranteed capital at the end of the term of the contract, when, if not previously purchased, the lines will be surrendered, and the Government will become liable for the re-payment of the full capital subscribed. The annual sum that at 4 per cent. must be set aside, on the expiration of the first 25 years, to make up the principal by the end of the term of the contract is £0·225 for every £100 of stock, so that the figures already given as representing the annual saving of charge, should in each case be increased by £180,000* (taking the Railway capital at 80 millions sterling) in order to exhibit the real financial bearings of the case under the assumptions made.

$$* \frac{0{\cdot}225 \times 80{,}000{,}000}{100} = 1{,}80{,}000$$

28. The stocks of the different Companies are at present quoted from about 106½ to 114. They may be expected to rise considerably in the course of the additional 25 years now secured to most of the Companies with this result (the difference in value of an annuity for 74 and 49 years being so small), that money must become very much cheaper than it now is to admit of this financial operation being performed, except at a disadvantage. Calculations, in fact, show that whilst, with money at 4 per cent., the Government can afford to redeem the Railway capital at the end of the first period of 25 years at 118½, without bringing any additional current charge on the State than the guaranteed interest, they could not give more than 107 at the end of the 50th year, unless money should become cheaper than 4 per cent. In order to redeem the capital at the second period at the same premium as at the first period, money must fall to rather less than 3½ per cent.

29. And, if the second opportunity of purchase be abandoned, the State will not only have to sustain the same current liability throughout the term of the contract, but at the end of the period will have to repay the whole capital expended on the Railways, as the Companies will of course not fail to surrender them at the expiration of the 98½ years.

30. There is a clause in the contracts, of which the Companies can avail themselves at any moment, to get out of the undertakings without loss. This course has already been taken by one Company. There is another clause under which the Government can extricate itself at two specified periods, but on penal terms. The contract was entered into at a time when the credit of the Government was not so good as at present. The Government has faithfully fulfilled its part of the contract, and *up to the present time it has contributed* 15 millions sterling towards the construction of the Railways, exclusive of the cost of land and of control, and of loss by exchange. Its guarantee has never failed. It appears to us, therefore, that the surrender of the power which the Government possessed of acquiring the possession of these Railways at the earliest possible moment, is not only to abandon the opportunity of extricating itself from the disadvantages of the position, but is to sacrifice a great source of income, to forego an economical financial arrangement, and unnecessarily to prolong, for an almost indefinite period, a heavy burden on the tax-payers of India.

31. In addition to the foregoing financial considerations, we must further impress on your Grace the views that we have on former occasions expressed to the effect that it is most desirable that in all transactions regarding money borrowed, whether for agricultural works or for guaranteed Railways, some provision should be made for its gradual redemption. Considerations not only of a financial but of a political character are involved in this view of the important matter discussed in this despatch, and we regret that they have apparently escaped notice on this occasion. The exercise by the State of the option of purchasing the guaranteed Railways would involve, under the annuity commutation clause of the contract, the application of the principle herein inculcated.

32. We respectfully submit these observations for your Grace's consideration, and we trust that, in the case of at least some of the Railways, it is not too late to retain the right in question to which we attach so much importance.

certain of the guaranteed Railways at

*Proceedings of the Madras Government, Public Works Department,*
*12th January* 1871.

No. 168. ORDER THEREON, 12th January 1871, No. 83.

RAILWAY, No. 23.

ORDERED to be recorded.

(True Extract.)

(Signed) CHARLES A. ORR, Colonel, R.E.,
*Secretary to Government.*

Exd. E. C. Shunker.

No. 1575 R.

GOVERNMENT OF INDIA.

PUBLIC WORKS DEPARTMENT.

RAILWAY.

*All communications should be addressed to the Secretary.*

To

The Secy. to the Govt. of Madras
Public Works Department (Railway)

Simla, 2d. September 1870

Sir,

Referring to the despatch from the Secretary of State to the Govt. of Madras No. 9, Railway, dated the 28th July 1870, I am directed to forward, confidentially, for the information of His Excellency the Governor in Council, copy of a despatch addressed by the Govt. of India to the Secretary of State on the 12th August 1870, No. 80, Railway, regarding the relinquishment by the State of the right of purchase of certain of the guaranteed Railways at

at the end of the first twenty five years of the term of the Contracts.—

2. I am specially to request that this document may be regarded as strictly confidential, and every care taken against its being made public in any way.—

I have the honor to be
Sir
Your most obed.t serv.t

E. Wilmot Major R.E.

Deputy Secretary

No 1870 Dept:

(3) No 4748.

From.

Govt of India

Dated 4 Sept^r
Rec^d 25 Sept^r } 1870

Encl. 1 ✓ No 1515 P.

Forwarding copy of a Despatch addressed to the Secy of State regarding the relinquishment by the State of the right of purchase of certain guaranteed Railways at the end of the first term of the Contract, & requesting that the document be treated as confidential. With an adv

Ans^d by the mail of 30th Nov^r

Pub. Sanitary Work

12th January 1871

Rec^d

1870 Madras

Govt. of

PUBLIC WORKS.

To

Dated

Rcvd.

No. 1

G. O. 12th January 1871. No. 83.

Nos. 167 / 168

Guaranteed Railways. Letter

From the Govt of India forwarding Copy of a Despatch addressed to the Secretary of State regarding the relinquishment by the Secretary of State of the right of purchase of certain Guaranteed Railways at the end of the first term of the Contract, and requesting that the document may be treated as confidential, recorded.

Lo 30