Chapter 14: Public Economics

Question: 1

Fill in the blank with appropriate alternatives given below:

The term budget is derived from ___________ word Bougette

Options

- Latin
- French
- Germen
- Greek

Solution

The term budget is derived from **French** word Bougette.

Explanation: 'Bougette' is a french word meaning a bag, or a wallet containing financial proposals. The term budget has been derived from this. A budget is a financial statement showing item-wise expected government receipts and government payments during a financial year.

Question: 2

Fill in the blank with appropriate alternatives given below

___________ is an example of direct tax.

Options

- Excise duty
- Wealth tax
- Sales tax
- Gifts

Solution

Wealth tax is an example of direct tax.

Explanation:
Direct taxes are those taxes which are borne by the person on whom they

are imposed. Since a wealth tax is directly imposed on the wealth of an individual, and the burden of this tax cannot be shifted to other, it is an example of direct tax.

Question: 3

Fill in the blank with appropriate alternatives given below

When Government revenue exceeds, government expenditure it is known as ___________ budget.

Options

- surplus
- balanced
- deficit
- unbalanced

Solution

When Government revenue exceeds, government expenditure it is known as **<u>surplus</u>** budget.

Explanation:
Surplus budget refers to the excess of government revenue over the expenditure. In other words, when the government revenue is greater than its expenditure, it is called a surplus budget.

That is, Surplus budget = Government revenue – Government expenditure

Question: 4

Fill in the blank with appropriate alternatives given below

During depression, ___________ budget is preferable.

Options

- balanced
- surplus
- deficit
- zero

Solution

During depression, **deficit** budget is preferable.

Explanation:
Deficit budget is a situation where the government expenditure exceeds its receipts. This kind of budget is preferable at the time of depression as during depression, the output and economic activities are low causing unemployment in the country. In order to solve this problem, the government can increase expenditure for productive purposes and and use it for generating employment opportunities. This will help in increasing demand for goods and services and lowering unemployment.

Question: 5

Match the following groups:

Group A		**Group B**	
1.	Deficit budget	a.	Tax revenue
2.	Government budget	b.	Capital receipts
3.	Fees, license fee	c.	Irrigation
4.	Borrowings	d.	Non-tax revenue
5.	Plan expenditure	e.	One year
		f.	Government expenditure > Government revenue
		g.	Two years

Solution

Group A		**Group B**	
1.	Deficit budget	f.	Government expenditure > Government revenue
2.	Government budget	e.	One year
3.	Fees, license fee	d.	Non-tax revenue
4.	Borrowings	b.	Capital receipts
5.	Plan expenditure	c.	Irrigation

Explanations:

1. Deficit budget refers to the excess of the total budgeted expenditure over the total budgeted receipts. In other words, budget deficit implies a situation where the total budget receipts of the government fall short of the total budget expenditure of the government. That is,
Deficit budget = Government expenditure > Government revenue

2. A government budget is a financial statement showing item-wise expected government receipts and government payments during a financial year. A financial year is typically for one year. Hence, it can be concluded that the government budget is for one year.

3. Non-tax revenue refers to the revenue received by the government from sources other than the taxes. Fees and license fee are imposed by the government for providing various services to people. Since they are not a part of taxes, the revenue generated from them is classified as non-tax revenue.

4. Capital receipts are those receipts of the government which either create a liability or cause a reduction in the assets of the government. Since the borrowing of funds by the government creates a liability on it, receipts from the borrowing activities are treated as capital receipts.

5. Plan expenditure refers to that budget expenditure which is incurred by the government on the planned programmes as per five year plan. As the expenditure of the government on irrigation is a planned one, it is plan expenditure.

Question: 6

State whether the following statement is true or false.

The budget is a monthly statement.

Options

- True
- False

Solution

The budget is a monthly statement. - **False**

Explanation: The above statement is incorrect. In fact, the budget is an annual financial statement showing item-wise expected government receipts and government payments during a financial year.

Question: 7

State whether the following statement is true or false.

Fiscal policy is related to public revenue and public expenditure.

Options

- True
- False

Solution

Fiscal policy is related to public revenue and public expenditure. - **True**

Explanation: Yes. The above statement is correct. Fiscal policy refers to the policy undertaken by the government to influence the economy through the process of public expenditure (government expenditure, subsidies and transfer payments) and public revenue collection (taxation). In other words, fiscal policy refers to a policy whereby the government alters its expenditure and revenue receipts.

Question: 8

State whether the following statement is true or false.

Indirect taxes are paid directly by people to the government.

Options

- True
- False

Solution

Indirect taxes are paid directly by people to the government. - **False**

Explanation: The above statement is incorrect. Indirect taxes are not paid directly the by people to the government. In fact, indirect taxes are paid indirectly by the people to the government. Example, sales tax, VAT

Question: 9

State whether the following statement is true or false.

Financial year in India is from 1st March to 28th February.

Options

- True

- False

Solution

Define or Explain.

Fine and Penalty

Solution

Fines and penalties are imposed by the government on those who boycott law. Since they are indirect payments made for the maintenance of law and order in a country, they form a part of the non-tax revenue of the government.

Question: 10

Define or Explain.

Budget

Solution

Budget is a financial statement showing item-wise expected government receipts and government payments during a financial year. It also presents the government's report on the financial performance during the previous fiscal year. A government budget is not only a financial statement, but also a reflection of the government objectives, policies and their expected effects.

Question: 11

Define or Explain.

Plan expenditure

Solution

Plan expenditure refers to that budget expenditure which is incurred by the government on the planned programmes of the five year plan. For example - the expenditure on different sectors of the economy such as agriculture, health, transport, energy etc.

Question: 12

Define or Explain.

Recovery of Debt

Solution

Recovery of debt implies taking back the money lent by the government to others (state government, union territories, public sector undertakings etc.). It is a part of the capital receipts of the government budget. The government can use the recovered debt to purchase assets, leading to an increase in the assets of the government.

Question: 13

Give reason of Explain the statement

Income collected from tax is a main source of government revenue.

Solution

Income collected from taxes forms a main part of the government revenue as a tax is a legally compulsory monetary contribution to the government by different economic units, such as households, firms and other economic units. Taxes are imposed by the government on different activities like income, property, production, occupation etc.

Question: 14

Give reason of Explain the statement

Revenue receipts and Revenue expenditure is known as Revenue Budget.

Solution

Revenue budget consists of items which neither lead to a change in the assets nor changes the liabilities of the government. In other words, it consists of the revenue receipts and revenue expenditure, as they do not change either the liabilities or the assets of the government.

Question: 15

Give reason of Explain the statement

Government revenue is more than government expenditure.

Solution

When government revenue is more than its expenditure, it is called a surplus budget. In other words, it refers to the excess of government revenue over its expenditure. That is, Surplus budget = Government revenue – Government expenditure.

Question: 16

Distinguish between:

Revenue budget and capital budget

Solution

Revenue budget	Capital budget
It consists of items that neither lead to a change in the assets nor change the liabilities of a government.	It consists of items that lead either to a change in the assets or a change in the liabilities of a government.
It consists of revenue receipts and revenue expenditure.	It consists of the capital receipts and capital expenditure.
It consists of revenue and expenditure that are incurred in day to day life.	These include items which are long term in nature.

Question: 17

Distinguish between:

Direct tax and indirect tax

Solution

Direct tax	Indirect tax
It is imposed directly on the taxpayer and is paid by the taxpayer directly to the government.	It is a tax collected by intermediaries (for example, retailers) from the ultimate taxpayers i.e. the consumers.
The incidence and impact of the tax is on the same person.	The incidence and impact of the tax is on different persons.
For example - Income tax, property tax.	For example - VAT, custom duty.

Question: 18

Distinguish between:

Deficit budget and balanced budget

Solution

Deficit budget	Balanced budget
It refers to the excess of total budget expenditure over the total budget receipts.	It refers to the budget in which the total budget expenditure is equal to the total budget receipts.
It leads to an increase in the	It has no effect on the liabilities or

liabilities of the government or causes a reduction in its reserves.	the reserves of the government.

Question: 19

Write short note on:

Capital expenditure

Solution

Capital expenditure refers to that government expenditure which causes a reduction in the government liabilities as well as creates assets for the government. For example - expenditure on purchasing land or buildings, expenditure on purchasing bonds etc.

Question: 20

Write short note on:

Revenue receipts

Solution

Revenue receipts are those receipts of the government which neither creates any liability nor any reduction in the assets of the government. These comprise of tax and non-tax receipts, duties and fines, interest and dividends receipts on government investments and assets. These receipts can be classified into the following two categories:

a. Tax revenue
b. Non-tax revenue

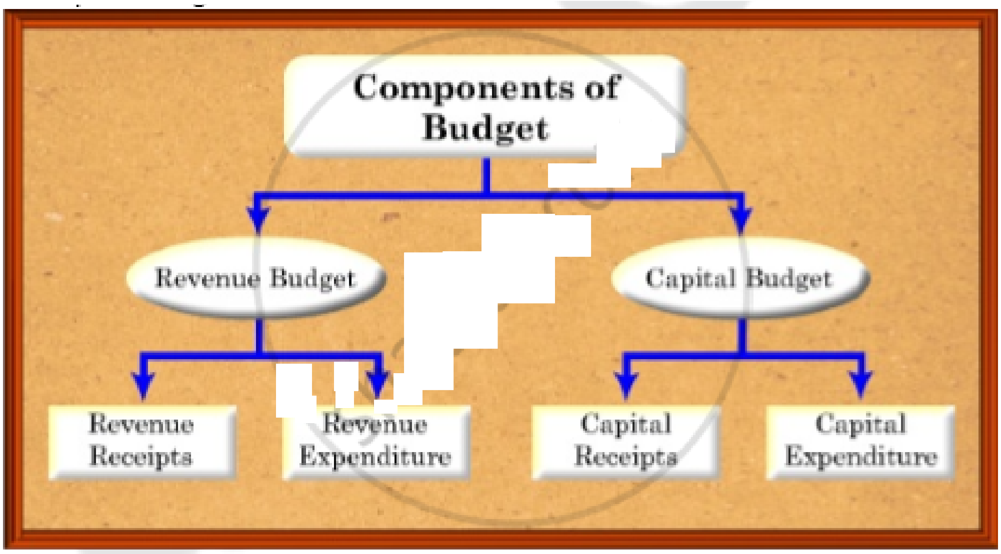
Question: 21

Answer the following question

What are the main components of budget?

Solution

Components of the budget can be divided into two broad categories:
1. Revenue budget
2. Capital budget



i. Revenue budget - It consists of those items that lead neither to a change in the assets nor a change in the liabilities of the government. This can further be classified into two categories, namely: a. Revenue receipts - These are those receipts of the government which neither create any liability nor any reduction in the assets of the government. These comprise of tax and non-tax receipts, duties and fines, interest and dividends receipts on government investments and assets.

b. Revenue expenditure - This refers to the government expenditure which does not cause any reduction in government liabilities nor create any assets for the government. For example- expenditure on salaries, pensions, subsidies, interest payments etc.

ii. Capital Budget - It consists of items that lead either to a change in the assets or a change in the liabilities of the government. This can further be classified into two categories, namely: a. Capital receipts - These are those receipts of the government, which cause a reduction in the government assets and also create a liability. For example - recovery of loans, borrowings etc.

b. Capital expenditure - This refers to that government expenditure which causes reduction in the government liabilities as well as creates assets for the government. For example - expenditure on purchasing shares, bonds etc.

Question: 22

Answer the following question

What are the source of non-tax revenue?

Solution

The following are some of the main sources of non-tax revenue:

i. Fees and license fee - The government receives fees in return of various services provided to the people. For example college fees, passport fees, registration fees etc.

ii. Gifts and grants - Gifts, grants and donations received by the government in the event of a natural calamity, war etc. also form a source of revenue for the government.

iii. Fines and penalties - Fines and penalties are imposed by the government on those who boycott law.

iv. Escheat - It refers to the income from a property of a person who dies without legal heirs.

v. Income from public enterprises - Income and profits from various enterprises owned by the government such as railways, SAIL etc. form an important source of revenue for the government.

Question: 23

Answer the following question

Explain the government's development and non development expenditure.

Solution

Development expenditure - This refers to the budget expenditure which is incurred by the government on economic growth and development activities. For example, expenditure on education, development of infrastructures etc.

Non-development expenditure- This refers to the budget expenditure which is incurred on the non-developmental activities. This expenditure does not directly contribute to the national income but accelerates the process of economic growth and development. For example, expenditure on administration, law and order, transfer of payments etc.

Question: 24

State with reason whether you agree or disagree with the following statement.

Capital budget consists of revenue receipts and revenue expenditure.

Solution

No, the above statement is not correct. A capital budget is mainly concerned with the capital items in the government budget, such as loans, borrowings, land, buildings etc., It consists of capital receipts and capital expenditure. On the other hand, revenue receipts and revenues expenditure form a part of the revenue budget.

Question: 25

State with reason whether you agree or disagree with the following statement.

When government expenditure is greater than government revenue, it is called Surplus Budget.

Solution

No, the above statement is not correct. This is because surplus budget refers to the excess of government revenue over the government expenditure. In other words, when government revenue is greater than its expenditure, it is called a surplus budget. On the other hand, when government expenditure is greater than its revenue, it is called a deficit budget.

Question: 26

State with reason whether you agree or disagree with the following statement.

During the period of inflation, Surplus Budget is advisable.

Solution

Yes, the above mentioned statement is correct. Inflation refers to the continuous increase in the general price level of the economy. This rise in the price level must be controlled by the government in order to safeguard the interest of the people. This can be done by increasing taxes and lowering the government expenditure, thereby causing a reduction in the effective demand in the country. An increase in taxes and reduction in expenditure of the government will lead to a surplus budget. That is why we say that surplus budget is advisable during the period of inflation.

Question: 27

Answer in detail :

Explain the concept of Balanced Budget.

Solution

A balanced budget refers to the budget when the total budget expenditure is equal to the total budget receipts.

Balanced budget = Total budget revenue – Total budget expenditure = 0

Adam Smith and other classical economists advocated the concept of balanced budget. They said that a balanced budget is the best since it has a neutral effect on the economy. However, it was argued by the modern economists that a balanced budget is not always suitable for the economy. For instance, during depression, the output and economic activities are low, causing unemployment in the country.

In order to solve the problem of unemployment, the government must step in. The government can borrow money and use it for generating employment opportunities, thereby increasing demand and lowering unemployment. Thus, during depression, only a deficit budget is useful, while the balanced budget fails to correct the situation.

Question: 28

Answer in detail:

Explain capital receipts and capital expenditure as a part of Capital Budget.

Solution

Capital budget is a financial proposal of the government which contains items that either lead to a change in the assets or liabilities of the government. Capital budget of the government can be decomposed into the following two categories:

i. Capital receipts - It refers to those receipts of the government which either create a liability or causes a reduction in the assets of the government. These receipts can be classified into the following three categories:

a. Borrowings - Borrowing of funds by the government creates a liability on it. Therefore, the receipts from the borrowing activities of the government are treated as capital receipts.

b. Recovery of loans - The central government often offers loans to the state government and union territories for various purposes. The recovery of such loans forms a part of the receipts for the government.

c. Other receipts - These include disinvestment and small savings. Disinvestment refers to selling a part or whole of the shares of the enterprises that are owned by the government. As disinvestment results in the reduction of government assets, it is treated as capital receipts. Similarly, small savings lead to an increase in the government liabilities as they include the money of the public deposited in post offices, national savings certificates etc.

ii. Capital expenditure - It refers to that government expenditure, which causes a reduction in the government liabilities as well as creates assets for the government. These receipts can be classified into the following three categories:

a. Expenditure on purchasing shares or bonds.
b. Expenditure on buying buildings or machinery.
c. Loans granted to the state government, union territories or the public companies.