

8. Public Finance in India

Q. 1. A) Choose the correct option:

1) Optional functions of Government:

- a) Protection from external attack
- b) Provision of education and health services
- c) Provision of social security measures
- d) Collection of tax

Options :

1) b and c

- 2) a, b and c
- 3) b, c and
- 4) All of the above

2) Obligatory functions of the Government :

- a) Provision of employment
- b) Maintaining internal law and order
- c) Welfare measures
- d) Exporting goods and services

Options :

- 1) c and d
- 2) a and b

3) only b

- 4) a, c and d

3) "Definition - Public finance is one of those subjects which are on the borderline between economics and politics." given by

- a) Adam Smith
- b) Alfred Marshall
- c) Prof. Hugh Dalton
- d) Prof. Findlay Shirras

Options :

- 1) only a
- 2) only b

3) only c

- 4) only d

4) Non-tax sources of revenue:

- a) Direct and Indirect Tax
- b) Direct Tax and Fees
- c) Fees
- d) Special Levy

Options :

- 1) b and c
- 2) a and c
- 3) a, b, c and d

4) c and d

5) Trends shown by Public expenditure of any Government shows following trend.

- a) Constant
- b) Increasing
- c) Decreasing
- d) Fluctuating

Options:

1) only a

2) only b

3) only c

4) only d

6) Identify the right group of pairs from the given options.

i) Direct tax	a) Non-tax revenue
ii) Indirect tax	b) Inflation
iii) Fees and Fines	c) GST
iv) Surplus budget	d) Personal income tax

Options :

a) i-d ii-c iii-b iv-a

b) i-c ii-d ii-a iv-b

c) i-d ii-c ii-a iv-b

d) i-a ii-b iii-c iv-d

Q.2 Distinguish between the following:

(1) Public Finance and Private Finance :

Ans.

Public finance	Private Finance
1. Meaning: The financial transactions carried out by the government with the objective of providing maximum social advantage to the society are called public finance.	The financial transactions carried out by an individual or a private enterprise to fulfil private interest are called private finance.
2. Elasticity: Public finance is comparatively more elastic. There is much scope for changes in public finance.	Private finance is comparatively less elastic. There is not much scope for changes in private finance.

(2) Internal Debt and External Debt:**Ans.**

Internal Debt	External Debt
1. Meaning: Debt raised by the government from borrowings from economic sources within the economy is called internal debt.	Debt raised by the government from borrowings from economic sources outside the economy is called external debt.
2. Nature of Management: Internal debt is comparatively less complex for management.	External debt is comparatively more complex for management.

(3) Developmental Expenditure and Non-Developmental Expenditure:**Ans.**

Developmental Expenditure	Non-Developmental Expenditure
1. Meaning: The government expenditure which yields direct productive impact on the economy is called developmental expenditure.	The government expenditure which does not yield any direct productive impact on the economy is called non-developmental expenditure.
2. Examples: Expenditure incurred on health, education, industrial development, etc. are the examples of developmental expenditure.	Expenditure incurred on administrative services, war, social welfare, etc. are the examples of non-developmental expenditure.

(4) Special Assessment and Special Levy:**Ans.**

Special Assessment	Special Levy
1. Meaning The payment made by the citizens of a particular locality in exchange for certain special facilities given to them by	A duty levied by the government on unhealthy items with the basic intention of discouraging citizens from consuming unhealthy items is known as special levy.

the authorities is known as special assessment.	
2. Examples: A special tax levied by local bodies on the residents of a particular area where extra/special facilities of roads, energy, water supply are provided is an example of special assessment.	Duty levied on wine, opium and other intoxicants are the examples of special levy.

(5) Direct Tax and Indirect Tax :

Ans.

Direct Tax	Indirect Tax
1. Meaning: A tax which is levied on the income or property of an individual and so in which the impact and incidence of tax is on same head is called direct tax.	A tax which is levied on goods and services and so in which the impact of tax is on one person (seller) and the incidence of tax is on another person (buyer) is called indirect tax.
2. Examples: Income tax, property tax, etc. are the examples of direct tax.	Goods and Services Tax, Custom Duty, etc. are the examples of indirect tax.

Q. 3. State with reasons whether you agree or disagree with the following statement

1) Obligatory function is the only function of the Government.

Ans: No, I disagree with this statement.

Reasons :

(1) In modern times, modern government performs many other modern optional functions in addition to the traditional obligatory functions of defence and civic administration.

(2) The government performs optional functions for the purpose of boosting economic and social development in the country. The optional functions of the government are constantly increasing.

(3) Provision of education and health services, implementation of social security schemes, promotion of industrial development, employment generation, etc. optional functions are carried out by the government.

Thus, obligatory function is not the only function of government: it is one of many functions.

(2) Fines and penalties are a major source of revenue for the government.

Ans. No, I disagree with this statement.

Reasons: (1) Revenue from fees and penalties is non-tax revenue. The government receives less revenue from non-tax sources than it does from tax sources

(2) The Government receives revenue in the form of fines and penalties only if a person violates the law.

(3) However, it cannot be said that many individuals will consistently violate the laws of the country. Therefore, fines and penalties are not a major source of revenue for the government.

(3) The Goods and Services Tax (GST) has replaced almost all indirect taxes in India.

Ans. Yes, I agree with this statement.

Reasons: (1) Goods and Services Tax IGST has been implemented in India from 1st July 2017. Goods and Services Tax (GST) is a broad indirect tax levied on goods and services across the country

(2) Goods and Services Tax has been imposed in place of Central Excise Duty Service Tax, Additional Customs Duty, Value Added Tax of States, Entrance Tax, Entertainment Tax, etc.

(3) The price of goods and services sold to the customer is no longer subject to various indirect taxes, but includes goods and services tax (GST). The consumer pays Goods and Services Tax (GST) which is included in the price of goods and services when purchasing various goods. Thus, Goods and Services Tax (GST) has replaced almost all indirect taxes in India,

(4) Democratic governments do not lead to increase in public expenditure.

Ans. No, I disagree with this statement.

Reasons: (1) In many countries of the world, the modern government has adopted a policy of intervention for the economic and social development of the country instead of adopting a policy of non-intervention (laissez faire).

(2) For the economic and social development of the country, the modern government is spending heavily on optional functions such as dissemination of education, provision of public health facilities, provision of recreational facilities, implementation of social welfare schemes, etc.

(3) The modern government is constantly adopting new optional (voluntary) functions on a large scale and carrying out traditional functions more efficiently. For this, the modern government is constantly spending more and more amount of money.

Thus, democratic governments lead to increase in public expenditure.

(5) Public finance is more elastic than private finance.

Ans. Yes, I agree with this statement.

Reasons: (1) Private financial transactions (finance) are carried out by individuals or private entities for fulfilling private interests. In contrast, public finance transactions (finance) are carried out by the government for the purpose of maximizing the benefits to the society.

(2) The economic and social needs of an individual do not change constantly, the needs of an individual are relatively constant. On the contrary, the economic and social needs of the society are constantly changing. As a result, a person's private finance remains relatively stable. In contrast, the government's public finance is constantly changing.

(3) For example, in the event of a major outbreak of an infectious disease in a country, there will not be a significant change in a person's personal expenditure and income. But in this situation, the government has to increase the expenditure on health facilities and for this the government can get financial funds in various ways. Thus, public finance is more elastic than private finance.

Q. 4. Read the given passage and answer the questions:

"The conventional notion of social security is that the government would make periodic payments to look after people in their old age, ill-health, disability and poverty. This idea should itself change from writing a cheque for the beneficiary to institutional arrangements to care for beneficiaries, including by enabling them to look after themselves, to a large extent.

The write-a-cheque model of social security is a legacy from the rich world at the optimal phase of its demographic transition, when the working population was numerals enough and earning enough to generate the taxes to pay for the care of those not working. This model is ill-suited for less, well off India with growing life expectancy, increasing urbanization and resultant migration. Social security under urbanization will be different from social security in a static society.

1) State the conventional notion of social security.

Ans: The conventional notion of social security is that the government should provide periodic payments to concerned people to look after their old age, ill-health, disability and poverty.

2) What kind of conceptual change is suggested in the given paragraph.

Ans: Conceptual change in social security in the form of making institutional arrangements to take

care of the beneficiaries and making them self-reliant instead of paying them in the form of cheques is suggested in the given paragraph.

3) What is a legacy of social security from the rich world?

Ans: Optimal phase of demographic transition is a legacy of social security in a rich world.

4) Which features of India make the traditional model of social security ill-suited for the economy?

Ans: The features of India like low economic resources, increasing life expectancy, increasing urbanization and resultant migration make the traditional model of social security ill-suited for the economy.

Q. 5. Answer the following:

1) State the types and importance of Government budget.

Ans. The types and importance of government budget is as followings :

(A) Balanced budget :

(1) **Meaning :** A budget in which government estimated revenue and its anticipated expenditure is equal to each other is called balanced budget.

(2) **Importance :** Classical economists considered a balanced budget as the best budget. However, according to modern economists it may not be always suitable for the modern economy.

(B) Surplus budget:

(1) **Meaning:** A budget in which government estimated revenue exceeds its anticipated expenditure is called surplus budget.

(2) **Importance :** Surplus budget is used during inflation to pull down the effective demand.

(C) Deficit budget :

(1) **Meaning :** A budget in which government anticipated expenditure exceeds its estimated revenue is called deficit budget.

(2) **Importance :** Deficit budget is used during depression to push up the effective demand.

2) Explain the principles of taxation.

Ans. The principles (canons) of taxation propounded by Adam Smith are as follows:

(1) **Canon of equity or equality :** Adam Smith suggested that every person will pay the taxes to the government in proportion to his/her 'ability to pay'. It means rich people should pay more tax compared to the poor.

(2) **Canon of certainty :** According to Adam Smith, the taxpayer should know in advance how much tax he/she has to pay, at what time he/she has to pay the tax and in what form the tax is to be paid to the government.

(3) **Canon of convenience :** According to this canon, every tax should be levied in such a manner and at such a time that its payment becomes convenient to the tax payer.

(4) **Canon of economy :** According to this canon, the cost of tax collection should be the minimum. If a major portion of the tax proceeds is spent on the tax collection itself, then such a tax cannot be considered as a good tax.

3) Explain non-tax sources of revenue of the government.

Ans. Non-tax sources of revenue of the government are as follows:

(1) **Fees :** Fee is paid by citizens in return for certain specific services rendered by the government.

For example, education fee, registration fee, etc.

(2) Prices of public goods and services: Modern governments sell various types of commodities and services to the citizens. A price is a payment made by the citizens to the government for the goods and services sold to them. For example, railway fares, postal charges, etc.

(3) Special assessment: The payment made by the citizens of a particular locality in exchange for certain special facilities given to them by the authorities is known as special assessment.' For example, local bodies can levy a special tax on the residents of a particular area where extra/special facilities of roads, energy, water supply etc. are provided

(4) Fines and penalties : The government imposes fines and penalties on those who violate the laws of the country. The objective of the imposition of fines and penalties is not to earn income, but to discourage the citizens from violating the laws framed by the government. For example, fines for violating traffic rules. However, the revenue from this source is comparatively limited

(5) Gifts, grants and donations : The government may also earn some income in the form of gifts by the citizens and others. The government may also receive grants from the foreign governments and institutions for general and specific purposes. Foreign aid has become an important source of development finance for a developing country like India. However, this source of revenue is uncertain in nature.

(6) Special levies : The government levies duties on those commodities, the consumption of which is harmful to the health and well-being of the citizens. Like fines and penalties, the objective of special levies is not to earn income, but to discourage citizens from the consumption of harmful commodities. For example, duties levied on wine, opium and other intoxicants.

(7) Borrowings : The government borrows from the citizens in the form of deposits, bonds, etc. Government also get loans from foreign governments and international organizations such as IMF, World Bank, etc. In modern times, loans are becoming more and more popular source of revenue for the governments.

Q. 6. Answer in detail:

1) Explain various reasons for the growth of public expenditure.

Ans: The reasons for the growth of public expenditure are as follows:

(1) Increase in the activities of the Government: For the economic and social development of the country, the modern government is continuously sending large amount on activities like dissemination of education, provision of health facilities, provision of recreational services. implementation of social welfare schemes. The government is adopting new optional functions and performing traditional obligatory functions more efficiently. The government has to spend a lot to carry out all these functions. As a result, public expenditure is rising.

(2) Rapid increase in population : As India is a developing country, population growth in India is accelerating. According to the 2011 census, India's population was 121.02 crore. Public expenditure is increasing as the government has to spend heavily to meet the various needs of the growing population.

(3) Growing urbanization: In modern times, the pace of urbanization is increasing in many countries of the world. In newly emerging and developed urban areas, the government has to provide water supply, electricity supply, transportation facilities, sanitation facilities, recreational facilities. For providing these various facilities, the government has to incur continuous expenditure and as a result public expenditure is increasing

(4) Increasing defence expenditure : In modern times, unstable and hostile international relations have increased. Many countries around the world are increasing defence spending to cope with potential foreign aggression and war. As a result, public expenditure is rising.

(5) Spread of democracy : Most of the countries of the world have adopted the system of democracy. In a democratic system, the process of forming a government is carried out by holding

general elections after a certain period of time. In a country like India, which is large in size and population, huge expenses have to be incurred for elections. As a result, public expenditure is rising.

(6) Inflation : Just as a person spends money on purchasing various goods and services to meet his personal needs, so the government spends money on purchasing various goods and services to meet the needs of the society. Prices of most goods and services continue to rise. As a result, public expenditure is rising.

(7) Industrial Development : In order to achieve the objectives of increase in production, increase in employment and overall growth in the economy, large scale industrial development is required in the country. As a result, in developing countries like India, a large amount of money is being spent on industrial development schemes to boost industrial development. As a result, public expenditure is rising.

(8) Disaster Management: The modern government is spending heavily on managing natural disasters like floods, earthquakes, hurricanes and man-made disasters like social unrest, riots, wars, etc. As a result, public expenditure is rising.