IMPACT: International Journal of Research in Humanities, Arts and Literature (IMPACT: IJRHAL)
ISSN (P): 2347-4564; ISSN (E): 2321-8878
Vol. 7, Issue 4, Apr 2019, 485-496

PUBLIC FINANCE: REVENUE AND EXPENDITURE

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Received: 10 Apr 2019 **Accepted:** 16 Apr 2019 **Published:** 30 Apr 2019

ABSTRACT

Public finance deals with the finances of the Government. It deals with the problem of how the Government raises it's resources to meet it's ever –rising expenditure. According to Dalton public finance is "concerned with the income and expenditure of public authorities and with the adjustment of one to the other". Thus effects of taxation, Government expenditure, public borrowing and deficit financing on the economy constitutes the subject matter of public finance. It also explains in detail fiscal policies which ought to be adopted to achieve certain objectives such as price stability, economic growth, more equal distribution of income. Economic thinking about the role that public finance is expected to play has changed from time to time according to the changes in economic situation. During the thirties the great depression hit the western industrialized countries. Before that, the role of public finance was considered to be raising sufficient resources for carrying out the Government functions of civil administration and defence from foreign countries. During this period, the classical economistsconsidered it necessary to keep expenditure to the minimum so that taxing of the people is avoided as far as possible.

KEYWORDS: *Public Finance, Taxation, Revenue, Expenditure*

INTRODUCTION

According to professor Otto Eckstein "Public Finance is the study of the effects of budgets on the economy, particularly the effect on the achievement of the major economic objects – growth, stability, equity and efficiency". Public finance is the study of income and expenditure of a government. It studies about the income raised through revenue and expenditure that is spend on different activities of public authorities. Through marginal adjustments income and expenditure of the government are regulated so as to give the maximum benefit to the public. The term 'public authorities' includes all sorts of governments though they differ in their functions, operations, sources of income and objectives of expenditure. It also relate to the raising and utilisation of their resources. There is difference in the Central or Federal, State and Local Governments. In the modern era, different governments all over the world have entered into a number of public projects for the economic and social security of their citizens such as railways, post and telegraphs, dams heavy electrical and atomic energy projects. The scope of state activity has expanded with the adoption of planning in almost all the countries. With the gradual expansion of the functions of the modern governments, the total public expenditure is increasing at a very rapid rate. On the other hand, the total expenditure and income of a government are much larger than the revenue and expenditure of a single individual or single economic and social organization. According to one of the greatest poets Kalidasa“ It is only for the good of the people that the king collects taxes from them just as the sun draws moisture from the Earth only to give it back a thousand fold”

Objectives of the Study

- To understand in detail the revenue and expenditure of the government
- To understand the sources of public finance.
- To analyse the similarities and dissimilarities between public and private finance.

RESEARCH METHODOLOGY

The study is based on secondary data collected from various books of national and international authors. The study is designed as a descriptive one because it describes in detail the state of affairs related to public finance.

Importance of Public Finance

- **Increase in Use of Money :-** In modern times there has been an increase in the use of money and mainly of credit. All the functions of the state came to be performed through money with the increasing use of this medium in all fields of life.
- **Expansion of State Activities :-**As social life became more complex, the state found it necessary and important to take upon itself some further responsibilities such as those of protection against internal disorders, regulation of commerce and trade, development of industry and planned economic development of the country.
- **Growth of Employment :-**The government provides grants, subsidies, grant exemption from excise duty, sales tax etc. to employment oriented cottage and small scale industries. This promote job opportunities.
- **Significance in Developed Countries :-** The main point of consideration in developed countries is stability in business conditions with all- round rapid progress in the economy. So fiscal policy has gained importance as effective means of stabilization in developed countries.
- **Significance in Developing Countries :-** Fiscal policies play an important role in increasing capital formation and rapid economic growth.
- **Significance in Under Developed Economies :-** The vicious circle of poverty has encircled the economies of under developed countries. Public financeplays an important role in increasing capital formation, savings, incomes, standard of living, national and per capita income, employment, rapid reduction in poverty etc. All these helps to break the vicious circle of poverty.

- **Decrease in Economic Inequalities :-** Economic inequalities are the causes of dissatisfaction, class- struggle, poverty etc.The government can levy heavy taxes on richer sections of society and there by spend the income so received on providing food, cheap housing, free medical facility etc. for the poorer sections of the society.
- **Useful in Social Sphere :-**The public finance plays an active role in organising and directing social welfare programmescotrolling consumption of harmful commodities, removing social inequalities etc.
- **Emergence of Generalized Services :-** The significance of public finance has increased due to the emergence of gen- eralized services which can be performed more conveniently and efficiently at minimum cost. Such services include education, health, social security and protection from some uncertainties.

Difference between Public Finance and Private Finance

Public finance relates to the finance of the state and private finance relates to the finance of individuals. The basic principles of private finance and public finance are almost the same, because both individuals and states need resources.Both attempt to get the best out of all items of expenditure. Some major differences are the following.

- **Period of Time** :- The state tries to balance its budget in the course of the year. In the case of an individual there is no definite period over which the account must be balanced.
- **Adjustment of Income to Expenditure:-**According to a state it first fixes the size of its expenditure and then proceeds to raise the necessary income. Therefore it has to adjust income to expenditure.First expenditure is determined and the revenues are raised according to expenditure. But according to an individual he adjusts his expenditure to his income. He is supposed to cut his coat according to his cloth.
- **Collection of Revenue :-**An individual has to earn his revenue,whereas the state gets most of it's revenue from other people's income. Sometimes the state also run productive enterprises and get revenue on their own account.
- **Private Finance is Shrouded in Mystery:-** No individual will allow his friends or neighbours to get any information about how he stands financially. But there is no such mystery in government finance.
- **Borrowing :-** In the case of an individual there is scope for internal borrowing only. But the state can borrow both internally from it's own people and externally from foreign governments and from foreign people.
- **Provision for the Future:-** In the case of providing for the future, a government is much more far sighted and liberal. Gov- ernment spends large amount of money on social welfare schemes,public works, infrastructure,social security schemes from which either there may be no monetary returns. Human life is so uncertain that some individuals discount the future at a very heavy rate.
- **No Equi-Marginalising of Utilities :-** An individual always try to maximize satisfaction from his revenue by distributing his expenditure in such a manner as to have equi-marginal utility in every case. But the government expenditure is

handled by the finance department in an objective manner. There is no such equi-marginalisingof utilities.

- **Surplus Budgeting:-** If a budget is in surplus it means the revenue is greater than the expenditure. Surplus budgeting is avirtue for an individual but need not be so for the government.

Similarities between Public Finance and Private Finance

- Public finance and private finance needs efficient administration and management. If there is no effective management both private finance and public finance are compelled to face problems.
- Both the government and the individual have broadly the same aim which is the satisfaction of human wants. Public finance deals with the satisfaction of society or collective wants while private finance deals with the satisfaction of personal wants.
- Borrowing is inevitable for public and private finances when current revenue becomes less than current expenditure. Both individuals and state has to repay the loans obtained during deficit.
- Both private and public finance have receipts and expenditures. Both of them try to balance receipts and expenditures to get the maximum satisfaction.
- For both public and private finances there is adjustment of income and expenditure. Both of them aims at the achievement of unlimited ends with scarce and minimum resources. Therefore the problem of economic choice is common to both of them.

Public Revenue

The term public revenue includes all receipts obtained by the state. Everyone knows that one needs money to live in the present society. Just like that a government also needs funds to finance it's activities. The funds are raised from different sources. Public revenue is an important part of public economics. Public revenue is the means for public expenditure. Some important sources of public revenue includes taxes, income from currency, market borrowings, sale of public assets etc. A government needs income for the performance of a variety of functions and meeting it's expenditure.

Sources of Public Revenue

- **Tax Revenue :-** It includes all revenues collected from taxation which may be defined as a compulsory contribution collected from the people for the general services performed by the state or government and not specifically related to any particular service performed by it. "Taxes are general compulsory contributions of wealth levied upon persons, natural or corporate to defray the expenses incurred in conferring a common benefit upon the residents of the state". Some examples of taxes are income tax, customs duties, sales tax and excise duties.

- **Non Tax Revenue :-** It contains all other receipts of the state. It includes the following.
- **Receipts from Public Property:-** The government receives income from buildings and lands which is owned by it. example. Land revenue
- **Fines and penalties :-**The court of law can impose fines or penalties for various offences. The government or other executive departments can under certain situations impose penalties for the break of rules and regulations.
- **Special Assessment :-** A special assessment is a compulsory contribution levied in proportion to the special benefit derived from improvement of property brought about by government action such as betterment of land and building sites which are usually subjected to special assessments.
- **Receipts from Public Enterprises :-**The government usually starts business enterprises for public welfare. They supply goods and services at a reasonable price to the public. The government also receives profit from public enterprises like railways, The Central Bank, post offices etc. State enterprises are generally monopolies.
- **Borrowing from the Public :-** The proceeds of loans given by the governments may be included within public revenues.
- **Fees :-** A fee is a charge made by the state for a service which is for the general benefit but which also confers a special benefit to a particular individual. For example, registration fees for legal documents, gun license fees etc.
- **Income from Printing Money :-** Finance obtained by printing paper money is atype of non- tax revenue. Inflation is a source of income to the government.
- **Escheats:-** If anyone die without a legal heir then his property and assets can be acquired by the government.
- **Gifts and Grants :-**Gifts can be the voluntary contribution from private individuals or non -governmental donors to the government fund for specific purpose such as relief fund, defence fund etc. Some kind and patriotic individuals contribute to the government funds in special occasions.

Characteristics of Tax

- **Compulsory Contribution to the State:-** A tax is a compulsory contribution by the citizen to the state. If anyone does not pay the tax it leads to punishment under law. No one can refuse to pay tax on the ground that he is not getting the benefit of certain services provided by the state. If a particular commodity is taxed, the tax can be avoided by ignoring the consumption of that commodity.
- **Common Interest :-** Undoubtedly the state confers benefits for not an individual or group of individuals but for the common benefits of all. The state performs various activities with the aim of giving benefit to all.
- **No Direct Relationship of Benefit and Tax Payment :-** A tax is a compulsory contribution and this contribution is for the benefit of all and there is no relationship of benefit as between the services rendered by the government and payment of tax by an individual. A tax is not a fees for any services of the government to the individual.

- **Individual is a Tax Payer :-** An important feature of tax is that it is imposed on income, property or commodities but the taxes paid by persons and not by things.
- **Personal Obligation to Pay Tax :-**It is the personal obligation of the individual to pay taxes under all circumstances. Tax is utilized for the common interest of the public. Taxes are imposed on all citizens and they may share the common interest of the public. No individual can survive without the care and security provided by the state.

Canons of Taxation

- **The Canon of Ability or Equality :-** The people of each and every state have the responsibility to contribute towards the support of the government as nearly as possible in proportion to their respective abilities. If every person pays according to his ability there is equality of sacrifice. The real burden on individual tax payers is more or less equal and the total burden is least.
- **The canon of Convenience :-**All taxes are supposed to be levied at the time or on the manner in which it is most likely to be convenient for the contributor to pay it. The state has many sources of income. The particular time when it gets payment from an individual is not very material to it, but it is very important to the tax payer. The principle of convenience is a natural sequence to the principle of certainty.
- **The canon of Economy :-** This canon demands that cost of collection of taxes should be the minimum. Possible maxi- mum part of the collected amount should be deposited in the government treasury. Thus all unnecessary expenditure in the collection should be avoided at all costs. This highlight the principle of least aggregate sacrifice.
- **The Canon of Certainty :-** The tax which are paid by each individual is supposed to be certain and not arbitrary. The time of payment, the quantity to be paid etc. should be clear to the contributor and every other person. Adam Smith considers certainty more important than equality.
- **Canon of Flexibility :-** Flexibility explains the absence of rigidity in the tax system. A tax which is flexible quickly adjust to the new conditions of the government. Lack of flexibility in a tax can cause financial problems to a state.
- **Canon of Productivity :-** This canon emphasizes that the tax should collect adequate amount of money to the state. The main aim of the taxing authority is to secure funds. So a tax which does not yield a fair income is useless.
- **Canon of Variety :-** It is also important that the tax system of a country should be diversified. Dependence on just a few taxes is risky. The revenue will not be sufficient nor will it be fair, because it will not cover a large number of people. The tax system must be broad- based. It must be diversified having a wide coverage over goods and people.
- **Canon of Elasticity :-** It shows that a tax should automatically bring in more income as the country’s population or income increases. There should be an automatic link between the needs of the state and the resources of the people. If in a necessary situation an increase in the tax rate brings in increased revenue, the tax is elastic.

- **Canon of Simplicity :-** It says that the tax system should be simple. Otherwise, there would be confusion and corruption. The tax system should be free from complexities.

Public Expenditure

The concept of public expenditure plays a very important role in public finance. Public expenditure is the expenses incurred by public authorities that is Central Government, State Government and Local bodies for the satisfaction of collective needs of the citizens or for promotion of economic and social welfare. The development functions include education, public health, social securities, irrigation, canal, drainage, roads etc. These functions of social welfare have increased public expenditure to a greater extent. Public expenditure refers to the expenses incurred by the government for the maintenance of the government and to preserve the welfare of the society as a whole.Public expenditure shows the decisions of the parliament and other independent executive bodies for the scope of public expenses.

Principles of Public Expenditure

The canons or principles of public expenditure are the fundamental rules which should govern the expenditure policy of the state authority. It includes

- **Principle of Benefit :-** The ideal of this canon is maximum social advantage. Other things being equal, public expendi- ture should bring with it important social advantages such as increased production, the preservation of social life against external attack and internal disorders and as far as possible a reduction in the inequality of incomes. Public funds must be spent in those directions which are most helpful to the public interest.

- **Principle of Productivity :-**This canon implies that the public expenditure policy should encourage production in the country. It means that major part of the country's public expenditure should be allocated for production and development purposes.

- **Principle of Economy :-**This principle means that the state should be economical in spending money. It means that the extravagant and wasteful expenditure should be avoided. Public expenditure should be efficient and productive. It should also develop the productive powers of the community as much as possible.

- **Principle of Equitable Distribution :-**This canon means that the public expenditure should be carried out in such a way that the inequalities in the distribution of income are swiped out. There should be justice and equity in the distribution of income among different groups of the community. Public expense like medical assistance, education, housing and old age pension can achieve this objective.

- **Principle of Elasticity :-**This principle explains that the expenditure policy of the state should be able to alter itself with the change in circumstances of the country. It must be possible to change the size and the direction of public expenditure according to the needs of the country.

- **Principle of Surplus :-** This principle requires that government should avoid deficits and aim at surpluses in their budget. Their revenue should always exceed their expenditure. According to Professor Shirras, " Public authorities must earn their living and pay their way like ordinary citizens. Balanced budgets must, as in the private expenditure, be the order of the day. Annual expenditure must be balanced without the creation of fresh credits unrepresented by the new assets.

- **Principle of Sanction :-** This principle lays down that no public expenditure should be incurred without the sanction of proper authority. It requires that the spending authority should obtain sanction from a higher authority established for the purpose. This does not mean that government has no freedom of incurring expenditure. The implication is that expenses beyond a particular limit should have sanction from the proper authority.

Causes for the Growth of Public Expenditure

- **Economic Development :-** Expenses of the government has been increasing very rapidly especially in under developed countries because they aim at rapid economic development. They have to provide infrastructure in the economy such as transport, communication etc. All these expenses are necessary for industries to develop.

- **Increase in the Activities of the State :-**Continuous extension of social activities lead to increase in the public expenses. Governments have enlarged the field of services supplied to the consumer either free of cost or less than cost. Education, public health etc. are good examples.

- **Urbanization :-** The process of urbanization lead to an increase in public expenditure because it necessitates protection of life and property. Also per capita cost of water supply, traffic service and control, health and sanitation rises with the size of the city.

- **Great Depression :-** The great depression of 1930's lead to increase in public expenditure. It demanded governmental intervention. Thus investment activities of modern governments is another cause of increase in public expenditure.

- **War and Preparation for War :-** In most countries, expenditure for national defence accounts for half of the total expen- diture. War preparations include purchase of the most modern weapons which are very costly.

- **Rise in Prices** :-The increase in prices is another cause for increase in public expenditure. With increase in the level of prices, governments have been compelled to pay more for the commodities and services they use.

- **Industrial Development :-** Industrial revolution has brought about industrial development, political and social trans-formations. New problems created by production relations, the regulation of industry, the protection of consumers, distribution of income and wealth and economic insecurity have arisen. All these problems call for expansion of gov-ernment action.

- **Development of Agriculture :-**Agriculture is the backbone of all developing countries. There is a close link between agriculture and industry.The agricultural sector provides raw materials for the industries. Increased agricultural incomecreate market demand for industrial goods. This provide a stimulus to industrialization. Industrialization in turn improve agriculture by providing sophisticated tools and techniques. So the governments of developing countries spend huge amounts for the development of agriculture.

- **Social Security Measure :-** Modern welfare governments have taken up the responsibility of protecting the interests of the community as a whole and promoting the implementation of welfare programmes. They have taken up the responsibility to see that enough wages are paid to the workers. Also they have to make sure that sufficient provision for social security measures are made. Increase in population also increased the responsibility of the governments.

Classification of Public Expenditure

It is classified into two. They are

- Expenditure on revenue account
- Expenditure on capital account

The Revenue Account Includes the Following

- **Civil Services :-** It includes expenditure on Parliament administration, justice, election and on the office of the Comptroller and Auditor General. Other types of expenditures are on Secretariat and attached offices of Ministries such as Edu- cation and Social Welfare, Health and Family Welfare, Information and Broadcasting, Labour and Employment and Department of Atomic Energy, Culture, Science and Technology and Space.
- **Defence Expenditure :-**Defence expenditure is must for saving the country and it's wealth against external aggression and internal disorder. It is increasing, as the modern warfare instruments are becoming more costlier and sophisticated. There are three major defence services- Army, Navy and Air force.
- **Economic Services :-** It includes the expenditure on Department of Commerce, Shipping and Transport, Irrigation, Energy, Chemicals and Fertilizers, Company Affairs and Election etc.
- **Interest Payments :-** It includes expenses on the payment of interest on the outstanding debt. In the current year these payments have been increasing rapidly.
- **Grants-in-Aid and States :-** Without the help of Central Government, the State Government cannot function properly. The state expenses have always been increasing because of increase insalaries and allowances of government employees and functional relations with other states.
- **Tax Collection :-** Taxes also play an important role in the revenue of any government.

The Capital Account includes the following-

- **Economic Services:-** Capital expenditure on economic services are of the kind of foreign trade and other allied services like irrigation, animal husbandry, diary, fishery development, industrial and mineral development, atomic energy, transport and communication etc.
- **General Services:-** It refers to the expenditure on currency, coinage and mint. It also includes expenses on fiscal services like India's contribution to International Monetary Fund and other international financial institutions.
- **Social Services:-**These are helpful to increase the efficiency and productivity of human resources. They are also helpful in raising the standard of living of people. They include expenditure on services like education, health, art, culture, family planning, sanitation, water supply, housing etc.
- **Loans and Advances to States and Union Territories:-** Generally State Governments and Union Territories face acute shortages of fund to meet the needs of development activities in the region. So Central Government provides them loans and assistance to undertake such development activities.
- **Defence Services:-** This consists of Central Government expenditure on capital as on Army, Navy and Air Force. It includes capital expenditures of the construction of non- residential buildings, machine tools and other equipments.

CONCLUSIONS

Public finance had little importance in the nineteenth century. The origin of public finance is traceable in the origin of the modern welfare state. Either due to necessity or due to man being by nature a political animal, some form of governmental organization has existed ever since man passed beyond the most primitive stage of development. The origin of public finance is deep rooted in antiquity. The two main components of public finance are public expenditure and public revenue. Public expenditure means the expenses of public authorities like Central, State and Local Governments of protecting the interest of the citizens or for promoting their economic and social welfare. Public revenue deals with the various sources from which the state might derive it's income. These sources include incomes from taxes, commercial revenues in the form of prices of goods and services supplied by public enterprises etc.

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