B.Com. Part II

PUBLIC FINANCE

(Unit 1)

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INTRODUCTION

- The government of every country has to perform certain special functions which can be classified under two heads

  1. Obligatory Functions
  2. Optional Functions

- To perform all these functions adequately and efficiently, the government needs funds from the public.

MEANING OF PUBLIC FINANCE

- The study of public finance as a branch of economics has come to occupy a very important place in economic literature since last nine decades.
- Public finance is that science which deals with the income and expenditure of the public authorities.
- The word public authorities include all sorts of governments.

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- The term public finance is a combination of two words, namely Public and Finance.
- The 'public' is represented by the government or state.
- The other word 'finance' means money resources.
- These money resources are in the form of income and expenditure.
- Thus, public finance refers to the systematic study of the operations of public income and expenditures of the public authorities.

DEFINITIONS

- **Adam Smith** - "Public finance is an investigation into the nature and principles of the state revenue and expenditure"
- **Prof. Dalton** - "Public finance is concerned with income and expenditure of public authorities and with the mutual adjustment of one another."

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- **C.F. Bastable** - "Public Finance deals with expenditure and income of public authorities of the state and their mutual relation as also with the financial administration and control"

Private Finance and Public Finance

- Private Finance is the study of Income and Expenditure of an private Individual or Private institutions
- Private Finance can be classified into two categories the personal finance and business finance.
- Personal finance deals with the process of optimizing finances by individuals such as people, families and single consumers.
- Business Finance involves the process of optimizing

Similarities Between Private Finance And Public Finance

1. Maximum Advantage

2. Precedence of Income

3. Scarcity of resources

4. Borrowings

5. Adjustment of Income and Expenditure

1. **Maximum Advantage**

- The objective of the both is to secure the maximum advantage out of the expenditure.
- Private individual tries to maximum Utility out of his expenditure and Government Wishes to achieve maximum social Advantage out of its Expenditure

2. **Precedence of Income**

- In private finance, the Income must precede expenditure.
- In public finance as well, the revenue has to be raised before the expenditure can be met.

3. Scarcity of resources

- Scarcity of resources in relation to ends is a factor common to both.
- The private individuals as well as the state have to adjust their scarce resources to meet multiple ends.

4. Borrowings

- Both the private individuals as well as the state have to resort to borrowing when expenditure exceeds revenue.

5. Adjustment of Income and Expenditure

- Both the public and private finance always face the same problem, i.e., the problem of adjustment of income and expenditure.

Dissimilarities/Differences Between Private Finance and Public Finance

1. Determination of Expenditure
2. Differences in credit status
3. Right to print currency
4. The law of Equi - marginal utility
5. Nature of Budget
6. Compulsory character
8. Secrecy of the budget
9. Elasticity of finance
10. Pattern of Expenditure
11. Time Duration
12. Differences in objective
13. Effect on Economy

1. Determination of Expenditure

- Government first determines the volume of expenditure that it has to incur on different heads to perform their obligations and then tries to find out the resources to meet this expenditure

- Individual first considers his income and then determines the volume of expenditure, it has to incur on different heads or items of consumption

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2. Differences in credit status

- The credit of a private individual is, at best, limited.
- He can borrow a limited sum of Money for a limited source
- Private individuals can rise credit only within the economy
- It means that the private finance has a limited source
- The government enjoys a very high degree of credit in the market
- It can borrow large amounts not only from its citizens but also from the foreigners

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3. Right to print the currency

- The government has a source of income which is not available to the private individual
- The government can print notes which are legal tender within the country
- The government often resorts to the printing press to cover the deficit in the budget engendered by war or an economic crisis
- The private individual enjoys no such right of printing the currency

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4. The Law of Equi – Marginal utility

- The private individual arranges his Expenditure in accordance with the law of Equi-Marginal Utility
- A Private Individual distributes his income between consumption and savings in such a manner as to equalize their marginal utility
- A Private individual tries, as far as possible, to apply the law of Equi – Marginal Utility to his Expenditure
- The government does not give as much importance this law as a private individual does
- Modern governments sometimes incur certain types of expenditure from which they do not derive any advantage
- They do incur this type of expenditure to satisfy certain sections of the community

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5. Nature of Budget

- Surplus budget is always god for a Private Individual
- Private individual spend less than his income and save something
- The government generally Prefer deficit budget
- Government spends more than its income

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6. Compulsory Character

- Public finance is known for its compulsory Character
- The public authorities cannot avoid or postpone certain expenditure
- Eg; Expenditure on Defence public administration, maintenance of law etc.
- Private finance is voluntary in nature
- Individuals can plan to postpone their expenditure

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7. Coercive Method

- The government can use coercive methods to collect revenue
- For example government can raise non repayable loans
- No citizen can refuse to pay taxes if he is liable to pay them
- Private individuals cannot use force to get their income
- Individuals have to earn their income by their own efforts.

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8. Secrecy of the Budget

- The budget of an individual is shrouded in mystery
- Secrecy is maintained in budget of the private private finance
- But in the case of government budget there is no secrecy is maintained
- In a democratic country , the government presents its budget before the parliament where it is widely discussed and subjected to criticism

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9. Elasticity of Finance

- Public Finance is more elastic/flexible than private finance
- There is no much scope for changes in private finance
- In Public finance drastic changes can be done
- Example – A private individual cannot effect any special increase in his income nor he can bring about any special changes in his expenditure
- But, the government can increase its income imposing new taxes. Likewise it is also in a position to make the necessary changes in its expenditure

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10.Pattern of Expenditure

- The Public expenditure is governed by deliberate economic policy of the government
- The economic, social and political requirements Of the country are considered while planning the public expenditure
- Private finance is influenced by habits, fashion, customs, status and personal needs of the individual
- Immediate objective of the private finance is maximization of their satisfaction

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11. Time Duration

- In public finance state allocate resources on various projects which yield return only in the future. Example investment in education
- It means public finance has a long term perspective.
- In private finance private individuals tries to satisfy their present needs and are interested in obtaining quick returns
- It shows that private finance has a short term consideration

- The objective of private finance is to fulfill private interest
- The objective of Public finance is to secure the maximum social advantage to the society
- The motive of private expenditure is personal benefit

- The motive of public Expenditure is social Benefit

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13. Effect on Economy

- Private expenditure, being small in relation to public expenditure, has only a marginal effect on the economy

- Public expenditure being in gigantic size has a tremendous impact on the economy

Objectives of Public Finance

1. To Secure adjustments in allocation of Resources
2. To maintain economic stability
3. To accelerate economic development
4. To secure distributive justice
5. To reduce economic inequalities
6. To achieve full employment
7. To achieve optimum utilisation of resources
8. To increase rate ~~of capital formation by~~ increasing the rate of saving and investment

COMPONENTS OF PUBLIC FINANCE

1. Public Revenue

2. Public Expenditure

3. Public Debt

4. Financial Administration

PUBLIC REVENUE

- The income of the government through all sources is known as public revenue
- This component deals with the different sources and methods of raising the revenue to the government
- It also studies about the classification of taxes, burden of taxes~~, effects, taxable~~ capacity etc.

PUBLIC EXPENDITURE

- Public expenditure refers to the expenditure incurred by the public authorities
- This component deals with the principles and problems related to the allocation of government spending
- It also studies about the classification of public expenditure, its effect, public expenditure policies of the government, and trends in public expenditure

PUBLIC DEBT

- ✓ Public debt refers to the loans raised by the government both internally and externally
- ✓ This component of public finance studies the need for and methods of raising public debt and problems related to raising and repayment of public debt

FINANCIAL ADMINISTRATION

- Financial administration refers to the study of different aspects of public budget
- It deals with the organizing and disbursing of the finances of the state
- The objective of framing budget, the methods of framing it, sanctioning and audit etc., are studied under this

ECONOMIC STABILIZATION

- this component of public finance studies the use of public revenue and public expenditure to secure economic stability and growth.
- It includes various economic policies and measures of the government that are used to achieve full employment, balanced growth and optimum use of resources

Thank you