Public Finance

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What is public finance?

Public finance is the study of the role of the government in the economy . It is the branch of economics that assesses the government revenue and government expenditure of the public authorities and the adjustment of one or the other to achieve desirable effects and avoid undesirable once. The study of how the government raises its income through different activities and how the government spends this collected income on the expenditure involved in the activities of the community is termed as Public finance. It is simply concerned with and deals with the revenue and expenses of the government.

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The government of every country has to perform some obligatory functions and optional functions .Defence of the country, maintenance of peace and security are some of the obligatory functions of the government. But the provision of education ,and the establishment of hospitals, building of parks ,etc, are optional functions of the government,To perform all these functions ,adequately & efficiently ,government needs funds from the public.

To perform these functions adequately and efficiently , govt. needs funds from the public.So publicfinance is that which deals with the income and expenditure of the government. **According of Findlay Shirras, ‘’ Public finance is the study of the principles underlying the spending and raising of the funds by public authorities**.

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The Nature And Scope Of Public Finance :

Nature of Public Finance

The Nature And Scope Of Public Finance : Public finance is a science as well as an art. It is a science because we study in it the various principles, problems and policies underlying the spending and raising of funds by the public authorities. It teaches how to collect taxes in the best way and how to maintain them economically and how to spend them properly.

As an art, public finance enables the concerned personnel to adopt the principles and policies in solving the financial problems of the Government in the best possible way to the maximum benefit of the society. The way to be adopted should be logical, suitable and proper according to the time. Application of various principles and policies depends much on the ability of the personnel in the Government how best he can extract from it in the public interest.

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Scope of Public Finance

The scope of public finance includes the following four types of activities-

1) **Public Revenues**. In this part of public finance, we study the various sources from which the Government collects revenues. Tax is the main source of revenue hence all principles of taxation and incidence of taxation are the subject matter of this part of public finance.

(2) **Public Expenditure.** In order to perform the various functions, the Government incurs expenditure out of the revenues collected by the state authorities from different sources. In this part of public expenditure, we study the main principles of public expenditure. Along with that we study the effects of expenditure on various sectors and also the ways and means through which the Government keeps a check on its expenditur

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(3) **Public Debt.** Like individuals, the Government also borrow funds from the public to meet its obligations and certain abnormal situations like war, famine, floods or natural calamities. The reason is that the Government expenditure exceeds its income in abnormal. times. The deficit in the budget is met by the Government by borrowing the funds from the public. Now, the Government borrows funds in normal situations for its promotional function i.e. for the economic development of the country. This part of public finance deals with the borrowing activities of the Government.

(4) **Financial Administration**. In this branch of public finance; we study how the Government controls its financial operations or in other words we study the problem of financial management. It covers matters like preparation of budget and its approval from the legislature, the audit of Government accounts etc. and other related matters.

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What are the objectives of Public Finance?

Price Stabilization

Equitable Distribution of Wealth

Satisfaction of Needs

Allocation of Resources

Provision of Full Employment

Maintaining Favourable Balance of Payments

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Government generates its incomes through the collection of taxes from the general public using various public amenities and government uses these funds in the development and betterment of these public amenities.

Some are the points on the Importance of Public Finance in Developing Countries .Importance of Public Finance in Developing Countries

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Public finance has importance for both developing and developed economies. It has a very important role in achieving objectives like full employment and price stability. Some of the importance of public finance are as follows-

Helps In Removing Inequalities In Terms Of Wealth And Income

In underdeveloped economies, there is a very serious problem regarding inequalities in the distribution of income and wealth. The rich are getting more and more while the poor are not getting enough and are thereby becoming poorer and poorer. So to promote equal distribution government need to invest in the development activities for the poor people

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Helps In Controlling Inflation & Deflation

Public finance is a very effective tool used by the government to control inflation and deflation like situations. In order to control inflation, the government increases the tax rate and capital expenditure. While during deflation government decreases the tax rate bringing down the prices thereby increasing the demand.

Helps In Attaining Economic Stability

Public finance is also used as a tool to stabilize the economy by the government. When there is more prosperity in the economy and the people are earning more and more, the government increase the tax rate and during deflation government reduces the tax rate thereby increasing the demand.

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Helps In Developing Well Structure & Infrastructure

Public finance helps the government in raising efficient funds for promoting the various infrastructural facilities in the economy like road, railways, medical and educational facilities, etc.

Helps In Increasing Export

It helps in promoting the export from the country and thereby earning the foreign exchange. Government reduces the tax rate or even exempt the products from the tax category that are exported. It imposes more and more tax rate on the import thereby disfavouring it.

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Helps In Encouraging Savings & Investment

A large category of the population invests their incomes on consumption due to which saving proportionate is very low leading to very low or nil investment. The government can use its finance to promote saving and investment habits in people by reducing the tax rate and providing some relief on product and services prices.

Helps In Allocating Resources Properly & Efficiently

It helps the government in proper allocation and utilization of man-made and natural resources. In order to allocate resources properly, the government imposes more and more taxes on the less demandable goods and imposes a low rate of taxes and even provides subsidies on more desirable products and services.

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Helps In Bringing Balanced Development In The Economy

It plays a very efficient role in helping the government in removing or erasing the gap between the rural and urban area, agricultural and industrial sector.

The government basically allocates an efficient amount from the fund raised through different sources for the infrastructural development in rural areas and provides direct benefits to the rural areas.

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Similarities between Public Finance and Private Finance:

The following are the points of similarities between public finance and private finance:

(a) Same Welfare Objective:

Both kinds of finances have broadly the same objective. Private finance is concerned with the maximization of individual welfare while public finance is concerned with the maximization of a community's welfare from given resources.

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Maximum advantage the objective of both to secure the maximum advantage out of expenditure . Just as private individual tries to secure maximum utility out of his expenditure ,in the same manner ,the government also wishes to obtain the maximum social advantage out of his expenditure(c) Scarcity of Resources:

(c)Scarcirty of resources

Both have limited resources at their disposal. Both public and private individuals are required to match their income and expenditures in such a way that both make the optimum use of resources which are scarce.

(d) Loans are Repayable:

Both private and public loans are required to be repaid. An individual borrows money from various sources to meet personal requirements. But that too cannot be unlimited. He has to repay his loans. Like individuals, government cannot live beyond its means. It can temporarily postpone repayment of loans, but it is obligatory to repay the loans..

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Differences between Public and Private Finance

1. Income and Expenditure Adjustment in Public and Private Finance

The government adjusts the income according to the expenditure budget. The private sector including individuals and private businesses adjust their expenditure according to the income or future estimates. The government first creates an outline for the expenditure then devices means of acquiring the monetary budget needed. Private finance involves cutting your coat according to your cloth.

2**. Borrowing in Public vs. Private Finance**

The government can borrow from itself, it can simply go back to the people to ask for loans in whichever financial asset e.g. bonds, when shortages arise. However, an individual can’t borrow from itself.

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3**. Currency ownership in Public vs. Private Finance**

The government is in charge of all aspects related to currency. This involves the creation, distribution and monitoring. No one in the private sector is allowed to create currency, this is illegal and most countries classify it as a capital offense.

4**. Present vs. future Income**

The public sector is more involved with future planning and making long-term decisions. The government makes decisions that will bear fruits in the long-term even ten years. These investments could include building of schools, hospitals and infrastructure. The private industry makes financial decisions on projects with a shorter returns waiting time.

5. Objective Difference in Public and Private Finance

The public sector’s main objective is to create social benefit in the economy. The private industry seeks to maximize on personal or profit benefits.

6. Coercion to Get Revenue

The government can use force to get revenue from individuals. This could involve the use of force to get taxes. The private sector however, doesn’t have this authority.

7. Ability to Make Huge and Deliberate Changes

The public finance sector has the ability to make huge decisions on income amount without much consequences. For example, it can effectively and deliberately increase or decrease the income amount instantly. Businesses and individuals can’t make these decisions and implement them immediately.

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8**. Surplus Budget Concept**

Excess income or surplus budgets is a great virtue in the private sector, this is however not the case in public finance. The government is expected to only raise what is needed for a fiscal year. Of what use would it be to have surplus budgets? It would be much easier to offer tax reliefs to the tax-payers so as to off-set the surplus.