IV- 2° The Principle Of Maximum Social Advantage

Q:1 Explain Dalton's Principle of Maximum Social Advantage.
OR "Social advantage in maximum when marginal social benefit equals marginal sacrifice" - Discuss.

(A) Principle of Maximum Social Advantage :-

Working of Public finance bring have great effect on the economic Lives of People. Government Collect funds through taxation. which result in Sacrifice of Purchasing Power. On other side government spend collected revenue to satisfy Collective wants of economy which result in benefits to People.

According to Hugh Dalton -
"The best system of Public finance is that which bring maximum social advantage from the working of Govt."

(B) Meaning :- Hugh Dalton -

"The Principle of MSA explain that - Public finance bring Economic welfare when Marginal Social Benefit of Public Expenditure is Equal to Marginal Social Sacrifice of Taxation."

Symbolically **MSA = MSB = MSS**

(C) Assumptions of MSA :-

1. The Government must follows Balanced Budget.
2. Public Revenue Consists of only Taxes and no other sources of Revenue
3. All Taxes are result in Sacrifice

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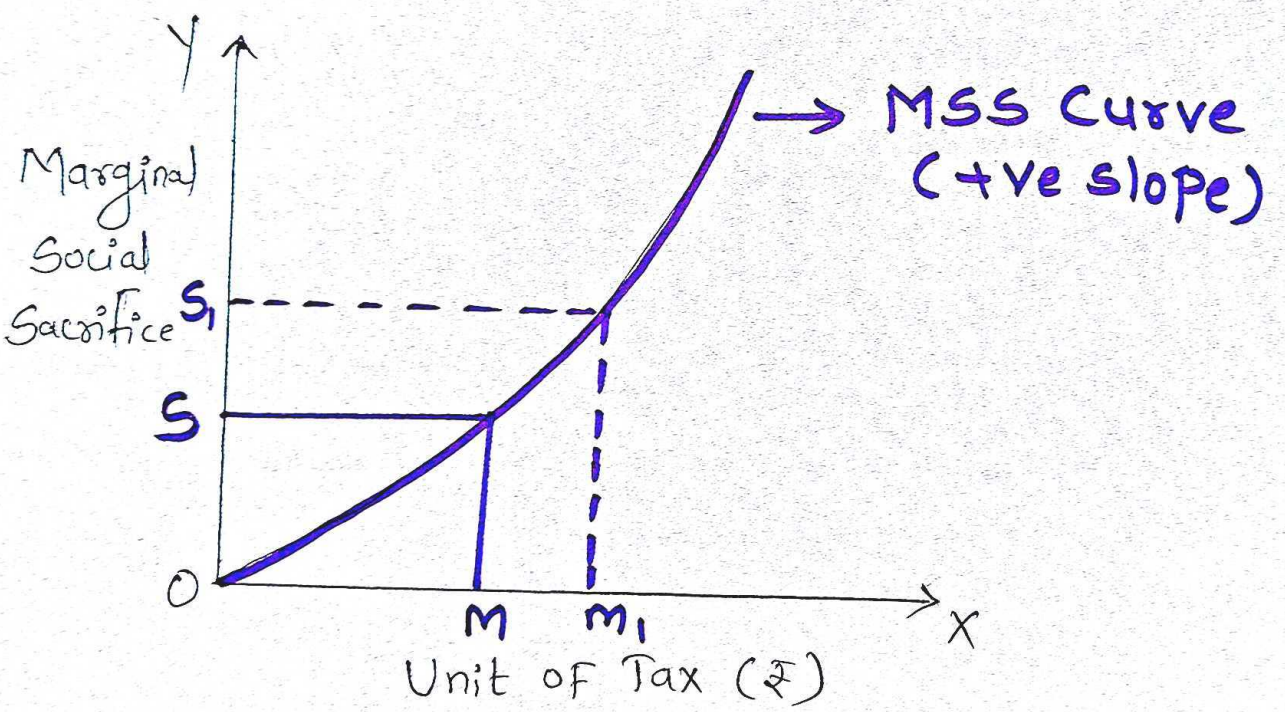
4. All Taxes are subject to Increasing marginal social Sacrifice (MSS)
5. All Public Expenditure of Government Leads to benefits.
6. Public Expenditure is subject to Diminishing Marginal Social Benefit (MSB)

(D) Marginal Social Sacrifice :-(MSS) :- when People

Pay taxes, it results in Sacrifice or Dis Utility. As revenue increase, the marginal Sacrifice also increases. Thus Taxes are subject to Increasing Marginal Sacrifice. It is shown in following diagram—



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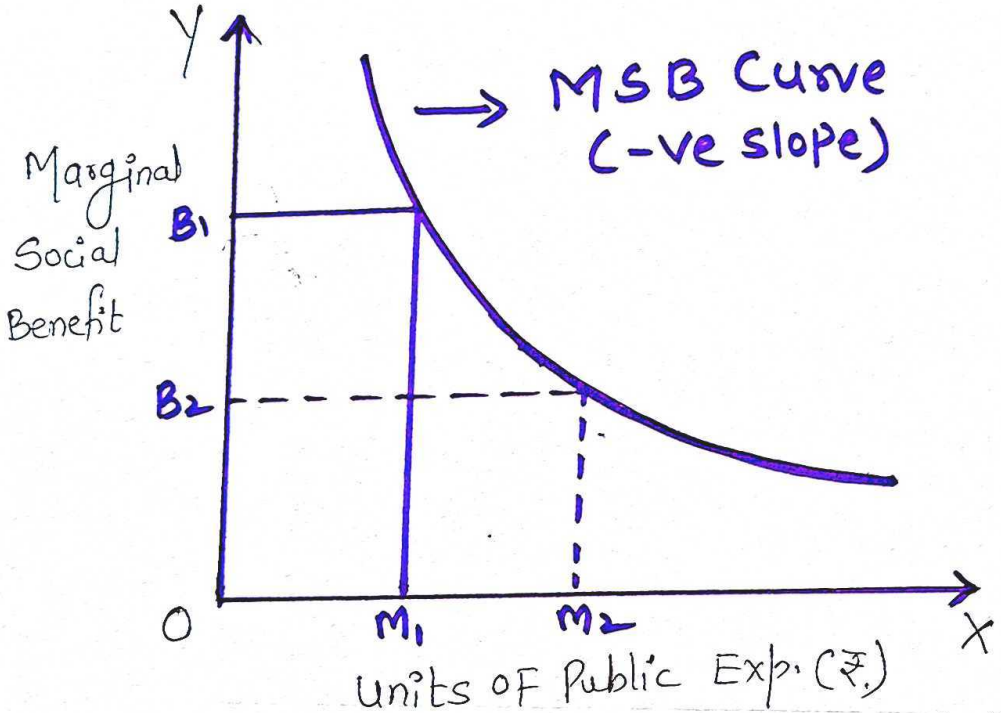
1) MSS Curve is sloping upward from Left to right.
2) When Tax increase from OM to OM1, Sacrifice of People also increase from OS to OS1.
3) Thus Taxes are subject to increasing marginal Sacrifice which shows Positive slope.

(E) Marginal Social Benefit (MSB) :-

Government Spent Public Expenditure for growth and development of a country. It increase income, employment, out put and Productivity of economy. Thus public expenditure result in benefits to the society. But the benefits derived from each additional public Expenditure will go on diminishing with increase in Public Expenditure. Thus Public Expenditure is subject to diminishing Marginal benefits shown in following diagram —



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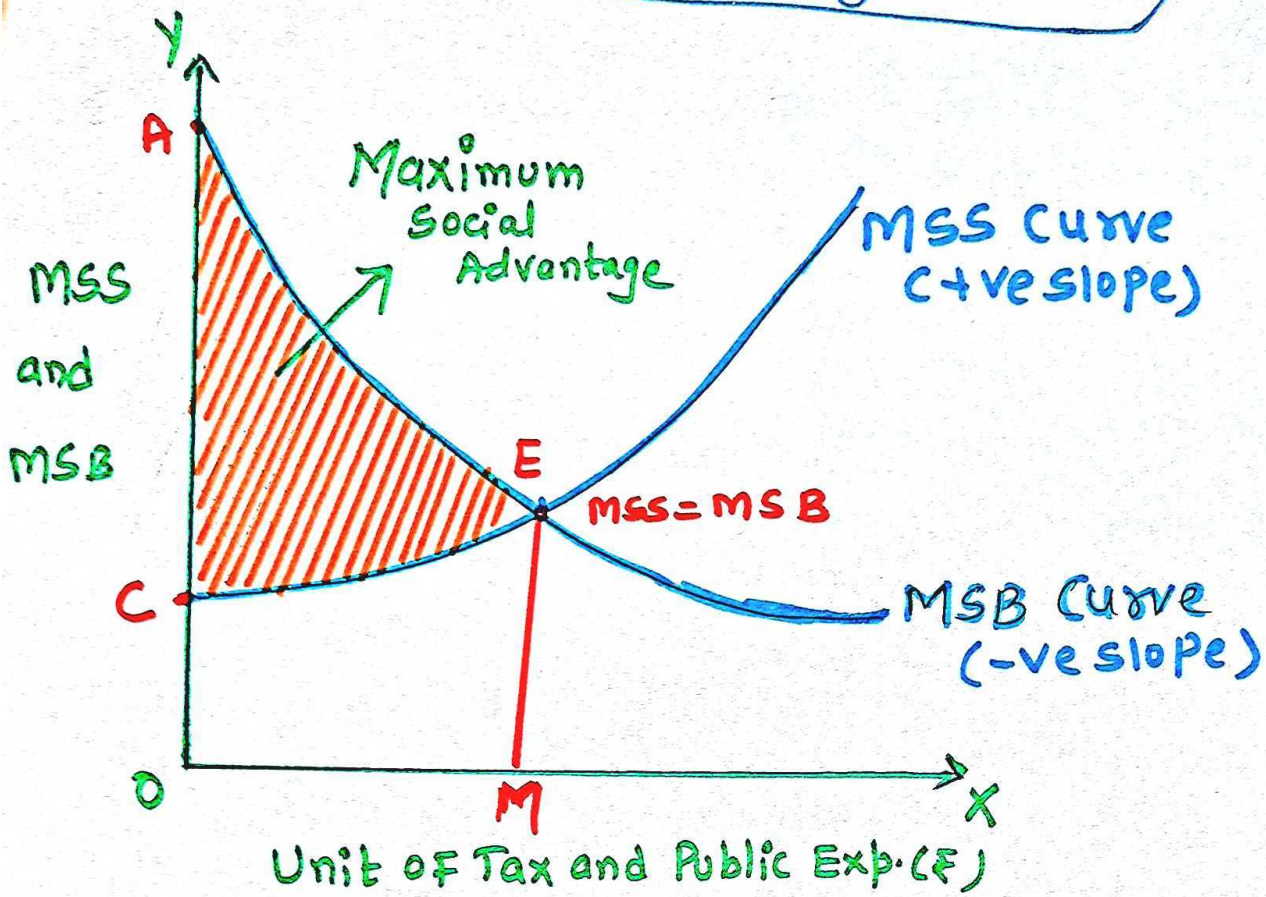
1) MSB Curve is sloping Downward from Left to right
2) As Public Expenditure increase From OM_1 to OM_2, Marginal social Benefit goes on diminishing From OB_1 to OB_2.
3) Thus Public Expenditure are subject to Diminishing marginal benefits which has Negative slope.

(F) Net Social Benefit / Maximum Social Advantage

" The Difference between. MSB due to Public Expenditure and MSS due to Taxation is Known as Net Social Benefit "



1) MSS Curve is Marginal Social Sacrifice Curve sloping Upward from Left to right. It shows that increase in unit of Tax, Sacrifice of People also increase.

2) MSB Curve is Marginal Social Benefit Curve sloping Downward from Left to right. It shows that increase in Unit of Public Expenditure, Benefit will go on diminishing.

3) MSS Curve intersect MSB Curve at Point E. This is known as Point of Maximum Social advantage where MSS = MSB.

4) The Shaded area ACE in diagram shows — Quantity of Maximum Social Advantage.

Q:2 Illustrate Musgrave's Interpretations of the Principle of MSA or Net Social Benefits ?

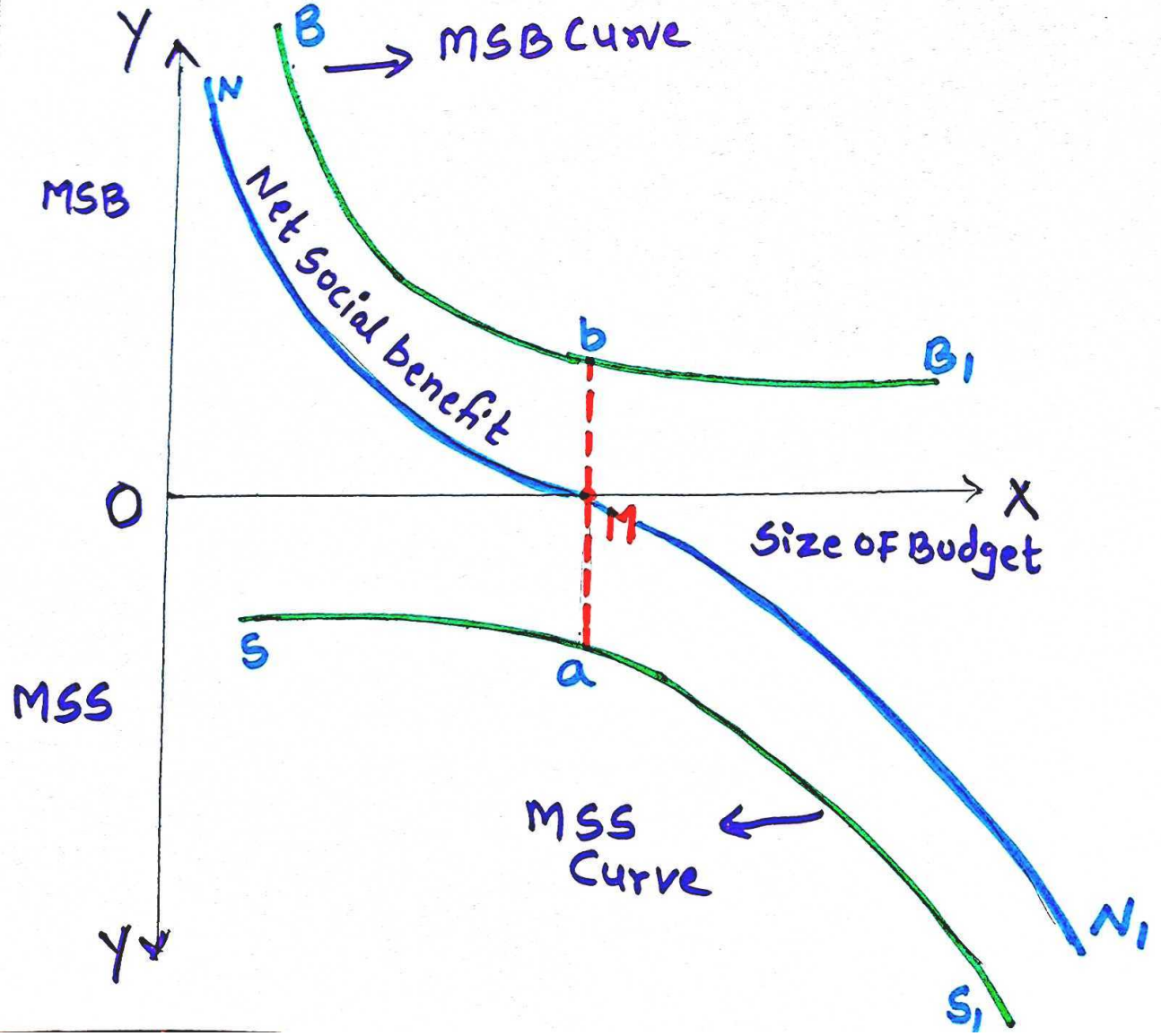
OR Explain Musgrave's Maximum Welfare Principle of Budget determination ?

(A) Musgrave's Principle of MSA :-

Dalton Principle of Maximum social advantage is termed by Musgrave as — 'Maximum Welfare Principle of Budget determination'

According to Musgrave- "Optimum size of the budget is determined where MSB to society by Fiscal Operation is zero."

The difference between MSB due to Public Expenditure and MSS due to Taxation is known as Net Social benefits



1) On X-axis, Size of government's budget and Y-axis shows Welfare of society due to Public Expenditure
2) The Upper Part of diagram shows Social benefit of Society due to Public Expenditure.
3) BB_1 is MSB curve sloping downward from Left to right. It shows that benefit from each additional Unit of Public Expenditure is diminishing. Thus MSB Curve has Negative slope.
4) The Lower Part of diagram shows Sacrifice of Purchasing Power due to Taxation.
5) SS_1 is MSS curve sloping Downward which shows that Large amount of funds are taken away from Public through Taxation. Each additional unit of Tax increase Sacrifice Level of People.
6) **Net Social Benefit = MSB − MSS**

Net Social Benefit is Calculated by deducting Net sacrifice of Taxation From Social benefit of Public Exp.

7) According to Musgrave, NN_1 is Net Social Benefit Curve which is Calculated by deducting SS_1 From BB_1.
8) OM is the optimum size of Budget where Community get Maximum Social Benefit from Public Expenditure
9) Before OM Level of Budget **MSB > MSS** and after OM Level of Budget **MSS > MSB**

10) Thus Optimum Size of Budget should be at OM where Community enjoy maximum social Benefits.

Q:3 Explain the Limitations of Principle of Maximum Social Advantage.

(A) Principle of Maximum social Advantage } same from Q:1
(B) Meaning
(C) **Criticism / Limitations / Drawbacks of the Principle of MSA :-**

1. **Unrealistic Assumption :-** Dalton assumed that every unit of Tax Paid will result in Sacrifice or burden on society. It is also assumed that government Expenditure is always beneficial these assumptions are unrealistic.

Example :- Taxes on Cigarettes or Liquor provide benefits to society. But Tax on Education and on Essential Commodities is harmful for the interest of society.

2. **Non-Tax Revenue Sources are Ignored :-** The Principle of MSA assumed that Public Revenue Collects From Tax only. However, the government have other non-Tax Revenue sources like- Fines and Penalties, Fees, Profit of Public Sector enterprises, Marketing borrowing etc. These Non-Tax revenue sources are Ignored.

3. **Lack of Objectivity :-** According to Critics, it is not possible to measure MSS due to Taxation and MSB due to Public Expenditure. so it is difficult to

Compare the Sacrifice and benefit of people because MSS and MSB are also affected by Non-economic Factors, Political and Social Factors.

4) **Methodological Imbalance :-** The benefit of Public Expenditure to the Society is a Macro Concept and the Sacrifice due to Taxation to individual Tax Payer is a Micro Problem. Thus there is methodological Imbalance to Compare the MSS and MSB.

5) **Lack of Divisibility :-** As Per Dalton View, when MSS and MSB are calculated, then government resources are required to be divided into smaller Parts. It will measure Sacrifice Per unit of Tax Paid and Benefit Per unit of Public Expenditure.

But according to modern economist Public Expenditure and Taxes cannot be divided into small units.

6) **Ignores Spill-over effect of Public Expenditure:-** The Principle OF MSA ignores Spill-over effect OF Public Expenditure i.e Long Term benefits OF Public Expenditure.

Example :- Development Expenditure or Expenditure on Infrastructure will Provide benefits not only for one year but for many Subsequent years.

7) **Contra-cyclical Measures :-** The Principle of MSA is not Useful to Control Trade Cycles. The government

has to follow Various Contra-Cyclical measures to control inflation, recession, to reduce Poverty and Unemployment.

Example :- During Recession, government has to reduce Taxation and increase Public Expenditure to increase demand in economy.

⑧ **No Disutility in Public Borrowings :-** Disutility arises in Case of Taxation but not in Case of Public borrowings. Hence government incurr more Public Expenditure through Public borrowings. So it is difficult to bring Equality between MSS & MSB.

⑨ **Differences in Area :-** According to modern economist, It is not possible to compare MSS due to Taxation of One Place to MSB due to Public Expenditure of other Place.

Example :- People of Big Cities Like- Mumbai, Kolkatta Pay a good amount of taxes and such taxes are Spend by government in developing backward areas. Thus it is difficult to compare Sacrifice of Taxpayer in Cities with benefits enjoyed by rural people.

⑩ **Misuse of Government Funds :-** The Principle of MSA is based on assumption that government funds are used in most effective manner to provide more benefits to economy

But it is observed that Large share of govt. funds are misused for unproductive purposes which do not create any benefits.

(11) **Large Budget Size** :- Dalton Principle of MSA measures sacrifice Per unit of Tax paid and benefit enjoyed Per unit of Public Expenditure. But Practically it is not Possible because the Government and Follows Large size of Budget. In Large Budget all transactions OF Collecting funds, and Allocation of Resources are involved. Thus it is difficult to compare small amounts of transactions with Large Size of Budget

(12) **Change in Conditions** :- In an economy Conditions are changing Continuously. So Principle of MSA is not Possible to follow in all Circumstances.
Example :- During war, Public Expenditure of government increases but it is difficult to measure benefit at that time.

CQ:4 How the Principle OF MSA is Used in Practice?

(A) Principle of MSA } Same From CQ:1
(B) meaning

(C) **The Principle OF MSA in Practice** :- It is not Possible to measure MSS due to taxation & MSB due to Public Expenditure hence the Principle of MSA has no Practical application.
But according to some economist, the Principle of MSA is Used in Fiscal operation by Public authority. According to Dalton they are →

1. **Preservation of the Society :-** According to Dalton, Public finance operation should be performed in such a way that society must be protected from internal problems and external attacks.

2. **To Increase Production :-** The government should incurr Public Expenditure to increase goods and services. Even Tax Revenues are utilised to grow infrastructure facilities in rural areas.

3. **To Improve Distribution :-** The Progressive Tax system helps to reduce Income Inequalities. However, Progressive Taxation should not badly affect on desire to work, save and Investment etc.
Thus government should maintain Equal Distribution of Income and wealth.

4. **To achieve Economic Stability :-** Government Follows Fiscal Policy to maintain Price stability in the economy. It will try to control trade cycles like- inflation or recession.

5. **Growth and Full Employment :-** Main Objectives of Fiscal Policy is to achieve Economic growth and Full-employment with optimum Utilisation of Resources.

6. **Provision of Future :-** According to Dalton - Life time of an Individual is Limited but State Never dies. It is a permanent system. Thus Public Finance Operation helps our Government to secure future of our economy for Long time.