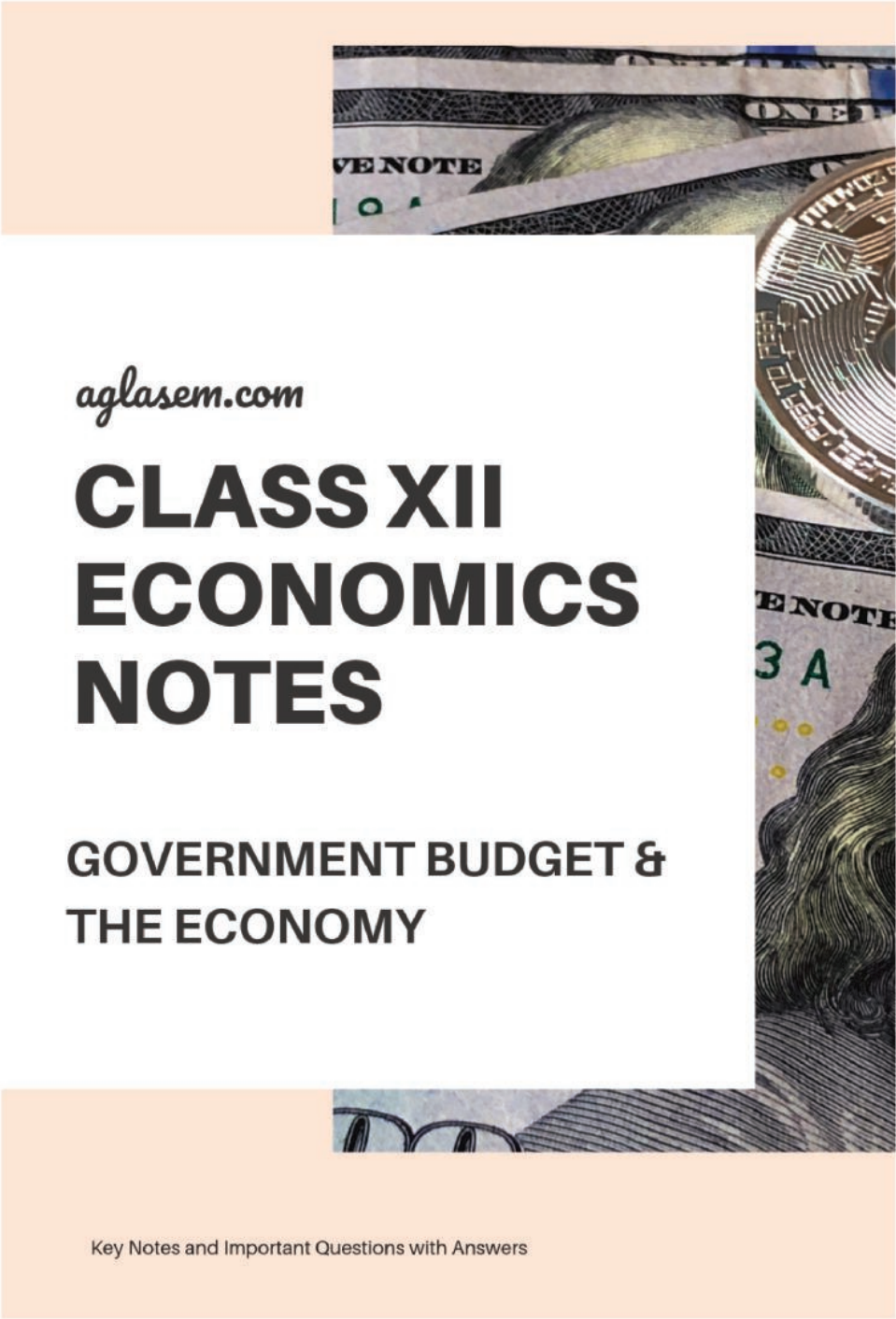


The background of the page features a collage of US currency. On the right side, there is a vertical strip showing a close-up of a dollar bill with the text 'ONE DOLLAR' and 'FEDERAL RESERVE NOTE' visible. Below this, another section shows a '3 A' serial number. At the bottom right, a portion of a coin is visible. The left side of the page has a solid light orange background.

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CLASS XII ECONOMICS NOTES

GOVERNMENT BUDGET & THE ECONOMY

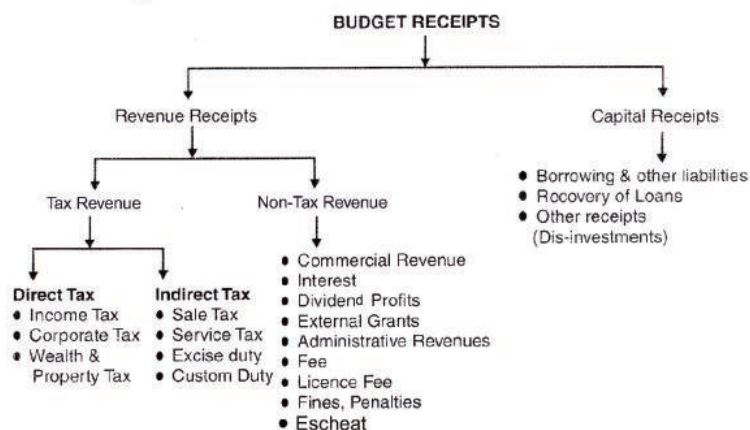
Key Notes and Important Questions with Answers

UNIT VIII

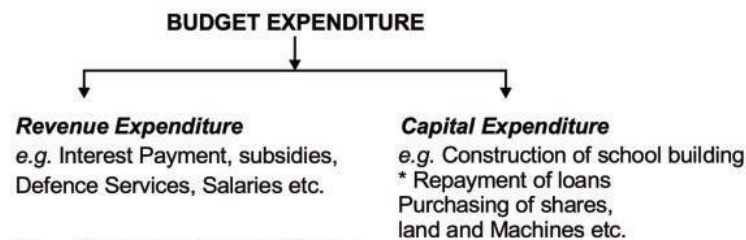
GOVERNMENT BUDGET AND THE ECONOMY

Points to Remember

- ❑ **Budget** is a financial statement showing the expected receipt and expenditure of Govt. for the coming fiscal or financial year.
- ❑ **Main objectives of budget** are :
 - (i) Reallocation of resources.
 - (ii) Redistribution of income and wealth
 - (iii) Economic Stability
 - (iv) Management of Public enterprises.
- ❑ There are two components of budget :
 - (a) Revenue budget
 - (b) Capital budget
- ❑ **Revenue Budget** consists of revenue receipt and revenue expenditure of the government.
- ❑ **Capital budget** consists of capital receipts and capital expenditure of the government.



- ❑ **Direct Tax** : When Government imposes a tax on a person and paid by the same person is called direct tax. Its burden cannot be shifted to others. For example : Income Tax, Property Tax.
- ❑ **Indirect Tax** : When Government imposes a tax on a person but partially or wholly paid by other person is called indirect tax. Its burden can be shifted to others. For example : Sales Tax, Excise duty VAT, GST.
- ❑ **Revenue Receipts** :
 - (i) Neither creates liabilities for government.
 - (ii) Nor causes any reduction in assets.
 - (iii) Recurring in nature.
- ❑ **Capital Receipts** :
 - (i) Either creates liabilities of the government.
 - (ii) or reduces assets of the government.
 - (iii) Non-recurring in nature.



- ❑ **Revenue Expenditure** :
 - (i) Neither creates assets (ii) Nor reduces liabilities
 - (iii) Recurring
- ❑ **Capital Expenditure** :
 - (i) Either creates assets (ii) or reduces liabilities.
 - (iii) Non-recurring
- ❑ Revenue deficit is the excess of total revenue expenditure over total revenue receipts of the government.
- ❑ **Revenue Deficit** : Total revenue expenditure > Total revenue receipts
- ❑ **Implications of Revenue Deficit are** :
 - (i) It leads to repayment burden in future without investment.
 - (ii) It shows wasteful expenditures of Govt. on administration.
 - (iii) It increase the burden of taxes.

- ❑ **Fiscal Deficit** : Total expenditures – Total Receipts excluding borrowing.
- ❑ **Fiscal Deficit** : Fiscal deficit is the excess of the government total expenditure over total receipts excluding borrowing.
- ❑ **Implications of Fiscal Deficits are :**
 - (i) It leads to inflationary pressure.
 - (ii) A country has to face debt trap.
 - (iii) It reduces future growth and development.
- ❑ **Primary Deficit** : By deducting Interest payment from fiscal deficit we get primary deficit.
- ❑ **Primary Deficit** : Fiscal deficit – Interest payments.

Exam. Oriented Questions with Answer

**VERY SHORT ANSWER QUESTION
(1 MARK)**

- Q. 1.** Why is recovery of loans treated as a capital receipts?
Ans. Because it reduces assets of the government.
- Q. 2.** Why are borrowing a capital receipt?
Ans. Because they create a liability for the government.
- Q. 3.** Give two examples of revenue receipts?
Ans. (i) Tax receipts (ii) Income from Public enterprises
- Q. 4.** Define Government Budget.
Ans. Government Budget is an annual statement of estimated receipts and expenditure during a fiscal year.
- Q. 5.** Define revenue Budget.
Ans. Revenue Budget is the statement of estimated revenue receipts and estimated revenue expenditure during a year.
- Q. 6.** Define disinvestment.
Ans. It refers to the selling of shares of PSU held by the government.

Q. 7. What is capital budget.

Ans. Capital Budget shows estimated capital receipts and capital expenditure during a fiscal year.

Q. 8. What is direct tax? Give an example.

Ans. A direct tax is one final burden of which falls on that very person who is liable to pay it to the government. Example : Income tax.

Q. 9. What is Indirect tax? Give two examples.

Ans. An Indirect tax is that tax which is initially imposed on and paid by one individual, but the burden of which is passed over to some other person who ultimately bears it.

Example : (i) Sales tax (ii) VAT.

QUESTIONS WITH ANSWERS 3-4 MARKS

Q. 1. Explain the 'redistribution of income' objective of a government budget.

OR

Explain how the government budget can help in a fair distribution of income in the economy.

Ans. Budgetary policies are useful medium to reduce inequalities of income or the fair distribution of income. Government can use tax policy and public expenditure as a tool. Government can reduce the disposable income and wealth of Rich by imposing heavy tax and can spend more on providing free services to the poor. It raises the disposable income and welfare of the poor.

Q. 2. Explain the "Reallocation of resources" objective of a government budget.

Ans. Through its Budgetary policy the government directs the allocation of resources in a manner such that there is a balance between the goal of profit maximisation and social welfare. Government can provide subsidy and reduction in tax rate to

motivate investment into areas where private sector initiative is not coming.

Q. 3. Distinguish between revenue receipts and capital receipts with the help of example :

Ans.	<u>Revenue Receipts</u>	<u>Capital Receipts</u>
	1. These receipt do not create any liability for government.	1. These receipt create liability for the Govt.
	2. These receipts do not cause any reduction in assets.	2. These receipts cause a reduction in assets of the Govt.
	3. Example : Tax receipts	3. Example : Loan by Govt., disinvestment.

Q. 4. Distinguish between Revenue Expenditure and Capital Expenditure with the help of example :

Ans.	<u>Revenue Expenditure</u>	<u>Capital Expenditure</u>
	1. These expenditure do increase govt. assets	1. These expenditure increase not the govt. assets.
	2. These expenditure do not cause any reduction in govt. liability	2. These expenditure cause reduction in govt. liability.
	3. Example : Transfer pay-ment by government.	3. Example : Repayment of loan by government.

Q. 5. Distinguish between Direct and Indirect Tax :

Ans.	<u>Direct Tax</u>	<u>Indirect Tax</u>
	1. Direct tax is a tax whose liability to pay and incidence lie on the same person.	1. The liability to pay and incidence liability of indirect tax do not lie on the same person.

2. Its incidence can not be shifted to some other person.
2. Its incidence can be shifted to some other person.
3. Example : Income Tax
3. Excise duty, VAT

Q. 6. What is meant by fiscal deficit. Write its implications.

Ans. Fiscal deficit is equal to excess of total expenditure over the sum of revenue receipts and capital receipts excluding borrowings i.e., Fiscal deficit means borrowing of the government.

$\text{Fiscal Deficit} = \text{Total expenditure} - \text{Total receipts net of borrowings.}$

Implication of Fiscal Deficit :

1. It increases the supply of money in the economy.
2. It increases financial burden for future generation.
3. It is cause of inflation.

Q. 7. What is revenue deficit? State its implications.

Ans. Revenue deficit is the excess of total revenue expenditure over total revenue receipts.

Implication : 1. It implies that government is dis-saving.

2. It implies that the government is spending more than the current income.

3. A high revenue deficit gives a warning signal to the government to either curtail its expenditure or increase its revenue.

Q. 8. Calculate (1) Revenue deficit (2) Fiscal Deficit (3) Primary Deficit by following Data : (Rs. Crore)

1. Capital Receipts other than borrowings	95
2. Revenue Expenditure	100
3. Interest payment	10
4. Revenue Receipts	80
5. Capital Expenditure	110

- Ans.**
1. Revenue deficit = Revenue expenditure – Revenue Receipts
 $= 100 - 80 = \text{Rs. 20 Crore.}$
 2. Fiscal Deficit = (Revenue Expenditure + Capital Expenditure) – Revenue Receipts – Capital receipts net of borrowings
 $= 100 + 110 - 80 - 95 = \text{Rs. 35 Crore.}$
 3. Primary deficit = Fiscal Deficit – Interest Payment
 $= 35 - 10 = \text{Rs. 25 Crore.}$