Principle of Maximum Social Advantage

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Introduction

Modern states are welfare states whose main objective is to ensure maximum social welfare for the people. The fiscal operations of the government have significant effect on the economy as a whole. Government collects revenue through taxation and public expenditure brings out changes in consumption, production and distribution of national income. Public finance plays a key role in the determination of national income, employment, output and other parameters in the economy. Thus, it is desirable that some criterion or principle must guide operations of government. This guiding principle has been technically called the principle of maximum social advantage or principle of public finance. The principle of public finance has been named differently by different economists. Prof. Dalton has named it as 'Principle of Maximum Social Advantage' while Pigou calls it as 'Principle of Maximum Aggregate welfare'.

Dalton's View on Principle of Maximum Social Advantage

Principle of Maximum Social Advantage governs both operations of public finance, i.e. revenue and expenditure which act simultaneously to maximise the economic welfare of the society as a whole. The principle says that public authority should collect revenue and spend the money to maximise the welfare of the people as a whole. Imposition of taxes creates disutility among tax-payers while public expenditure provides utility. So, the state should adjust the revenue and expenditure in such a manner that utility is maximised and disutility is minimised. In other words income and expenditure of the state should be managed in such a way that there should be greatest net advantage to the society. The principle is well represented by a table followed by a graphical explanation.

In the table below we can see that as the rate of taxation increases, the marginal sacrifice of the community also increases while with increasing units of public expenditure marginal benefits accruing to the society decreases. A point is achieved where MSS becomes equal to MSB. Therefore, government will not impose any tax beyond fifth unit because marginal sacrifice due to taxation is equal to marginal benefit or utility due to public expenditure.

Table 1: Marginal Social Sacrifice and Marginal Social Benefit

Units of Taxation & Public Expenditure	Marginal Social Sacrifice (MSS)	Marginal Social Benefit (MSB)
1	10	90
2	20	75
3	30	65
4	40	55
5	**50**	**50**
6	60	35
7	70	25
8	80	15

Figure 1 : Dalton’s View

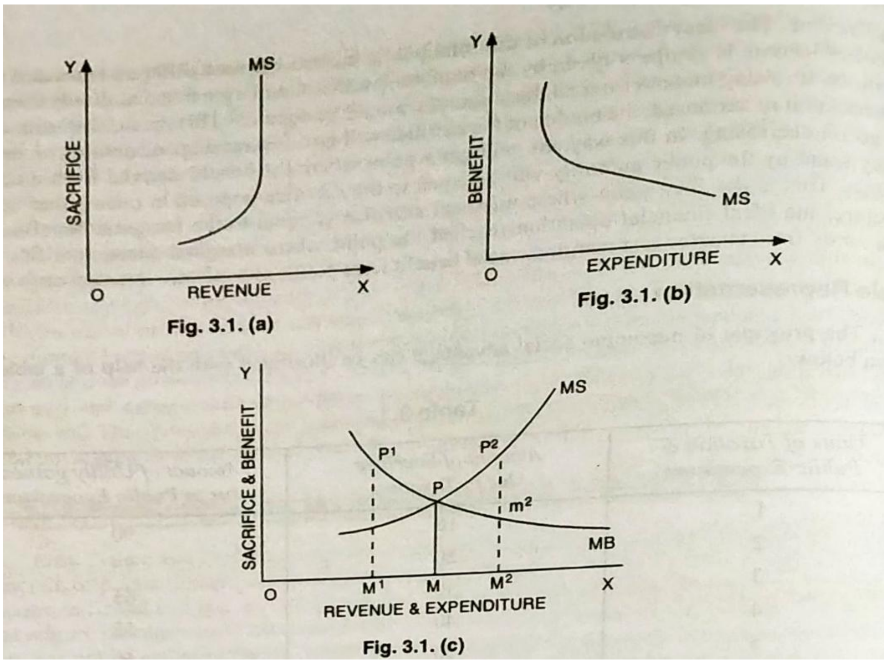


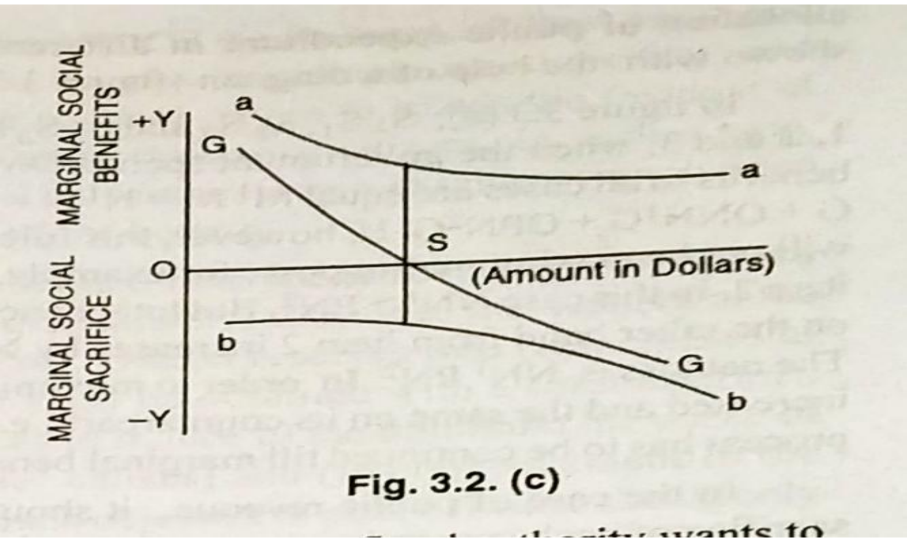
Fig. 3.1. (a)
Fig. 3.1. (b)
Fig. 3.1. (c)

The above graph represents Dalton’s view on Principle of Maximum Social Advantage. The curve in first graph (3.1a) represents marginal sacrifice which slopes upwards from left to right. The curve in second graph (3.1b) shows marginal utility of public expenditure having a negative slope. The last graph (3.1c) shows the interaction of the above two curves. It determines the optimum limit of public finance where MSS curve intersects MSB curve at point P showing OM level as the optimum. Therefore at point P welfare in terms of net benefits is maximised and society attains maximum social advantage.

Musgrave’s View

Musgrave has built his version on maximum social advantage on the lines of Prof. Pigou. Prof. Pigou says that public expenditure should be raised to the point where the utility derived from the last spent dollar equalises the utility lost by paying the last dollar as taxes. He also said that resources should be distributed among different uses so that the marginal return of benefit for each type of outlay should be equal. The explanation of Musgrave is depicted with the help of figure below:

Figure 2: Musgrave’s View



In the above figure, marginal utility of successive dollars of public expenditures allocated optimally between public uses is shown by line aa and marginal disutility of taxes imposed is shown by curve bb.

Line GG is obtained by deducting bb from aa and it measures the net benefits derived from successive addition to public budget. The optimum size of budget is determined at OS where marginal net benefits are zero. In this way minimum sacrifice approach to the allocation of taxes is matched by maximum benefit approach to the determination of public expenditure, and the two are combined in the general theory of budget planning.

Objective tests of Social Advantage

Following are listed some criteria of maximum social advantage:

- Political stability is the basic condition of attainment of maximum social advantage.
- Improvement in production is a necessary condition which requires increase in productive power in order to obtain large product with minimum effort and improvement in organisation of production

- Improvement in distribution which implies reduction in income inequality
- Economic stability indicating less fluctuations and a stable atmosphere for economic agents
- Attainment of full employment as it favours increase in production and promotes greater equality of income