

"Taxation: The Benefit Principle"

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Benefit Principle of Taxation:-

Introductory:-

Over the centuries, authors have developed two approaches to taxation, viz.; taxation according to benefits received and taxation according to ability-to-pay.

The benefit approach was initially developed by Knut Wicksell (1896) and Erik Lindahl (1919) two economists of the Stockholm School. Wicksell's near-unanimity formulation of the principle was premised on a just income distribution. The approach was extended in the work of Paul Samuelson, Richard Musgrave and others.

The benefit approach implies tax payment based on benefit received. Broadly speaking, the governmental services

Confer certain benefits on the Community and the cost of providing these benefits should be apportioned among individuals and private organisations on the basis of the relative benefit which they enjoy.

The benefit approach has two implications: first benefit is used as a justification for taxation and second, it serves as a standard for apportioning tax burdens. According to the benefit principle, the obligation to pay and also the amount to pay are individualised.

The benefit principle has two interpretations — the Cost of Service and the Value of Service Principle. According to the Cost of Service, every person should contribute in taxes the actual cost of the services of which he is the beneficiary. In other words, each should be charged for the expenses of the Govt. that he has caused. The Value of Service Principle on the other hand, states that every individual should pay in the form of taxes, according

to the worth of the services he has received from the government.

Towards the end of the 19th century, under the benefit principle, taxes came to be regarded as a price for public services and the determination of tax price in accordance with benefits received came to be looked upon as a condition of efficient allocation of resources. In modern benefit approaches, the basic idea is that the tax is like a price and that it should be designed to maximise the satisfaction which the consumer derives from his payment for public and private services.

Assessment of Benefit Principle:

The basic merit of the benefit approach is that it is based on the assumption that the benefit conferred by public services justify the imposition of taxes to pay for them. Secondly, the benefit approach combines both the income and expenditure sides of the budget processes and thus determines simultaneously both

the public services as well as tax shares.
Thirdly, benefit taxation is applicable to those cases where the benefit received by the individuals can be measured. For example, Petrol tax on the users of roads, local property taxes to finance police, fire protection and sewage services and special assessments to finance local public works. In spite of these merits, the benefit approach has so many drawbacks.

First, the benefit approach is based on the assumption that the activities of the Govt. can and should be calculated and assessed against each person on the basis of the individual benefits derived. This assumption is highly unrealistic and does not recognise the serious theoretical and practical difficulties.

Secondly, it is difficult to implement the benefit principle for most public services. There are certain services which the state provides for the general welfare and not for individual welfare. E.g. national defence, police, etc.

Thirdly, benefit approach, if applied rather blindly, will lead to great injustice rather than bring about justice in taxation. For example, the application of benefit approach will necessitate the curtailment of governmental outlay on such essential expenditure as education, public health etc.

Fourthly, The benefit principle cannot solve the problem of distribution and stabilisation which are important aspects of public economy.

Fifthly, The approach is not acceptable from the point of view of equity. It can have only a limited application, i.e. for special or direct services made available to individual on a voluntary basis.

To sum up, besides the limitations of the approach, a limited application of the benefit principle may be justified as an antidote to extreme application of the ability principle.
