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WEEKLY ARTICLE:

OBJECTIVES OF TAXATION IN MODERN PUBLIC FINANCE

INTRODUCTION

The primary purpose of taxation is to raise revenue to meet huge public expenditure. Most governmental activities must be financed by taxation. But that is not the only goal. In other words, taxation policy has some non-revenue objectives. Sincerely speaking, in the modern world, taxation is used as an instrument of economic policy. It affects the total volume of production, consumption, investment, choice of industrial location and techniques, balance of payments, distribution of income, e.t.c.

Here we will discuss the objectives of taxation in modern public finance:

1. Economic Development
2. Full Employment
3. Price Stability
4. Control of Cyclical Fluctuations
5. Reduction of BOP Difficulties
6. Non-Revenue Objective

ECONOMIC DEVELOPMENT

One of the important objectives of taxation is economic development. Economic development of any country is largely conditioned by the growth of capital formation. It is said that capital formation is the kingpin of economic development. But Least Developing Countries usually suffer from the shortage of capital.

To overcome the scarcity of capital, governments of these countries mobilize resources so that a rapid capital accumulation takes place. To step up both public and private investment, government taps tax revenues. Through proper tax planning, the ratio of savings to national income can be raised.

FULL EMPLOYMENT

Second objective is the full employment. Since the level of employment depends on effective demand, a country desirous of achieving the goal of full employment must cut down the rate of taxes. Consequently, disposable income will rise and, hence, demand for goods and services will rise. Increased demand will stimulate investment leading to a rise in income and employment through the multiplier mechanism.

PRICE STABILITY

Thirdly, taxation can be used to ensure price stability—a short run objective of taxation. Taxes are regarded as an effective means of controlling inflation. By raising the rate of direct taxes, private spending can be controlled. Naturally, the pressure on the commodity market is reduced.

But indirect taxes imposed on commodities can lead to inflationary tendencies. High commodity prices, on one hand, discourage consumption and, on the other hand, encourage saving. Opposite effect will occur when taxes are lowered down during deflation.

CONTROL OF CYCLICAL FLUCTUATIONS

Fourthly, control of cyclical fluctuations—periods of boom and depression—is considered to be another objective of taxation. During depression, taxes are lowered down while during boom taxes are increased so that cyclical fluctuations are tamed.

REDUCTION OF BOP DIFFICULTIES

Taxes like custom duties are also used to control imports of certain goods with the objective of reducing the intensity of balance of payments difficulties and encouraging domestic production of import substitutes.

NON-REVENUE OBJECTIVE

Finally, another extra-revenue or non-revenue objective of taxation is the reduction of inequalities in income and wealth. This can be done by taxing the rich at higher rate than the poor or by introducing a system of progressive taxation.

CONTACT

Office Address

- 17, Olumoroti Jaiyesinmi Street, Gbagada Phase II, Lagos, Nigeria.
- 21, Lord Emmanuel Drive, Off Jogunomi Street, Akpasak Estate, Uyo, Akwa Ibom, Nigeria

Online Address

07038254989

08152451523

@sowprofessional.com

@sowprofessionaltd

www.sowprofessional.com

care@sowprofessional.com

THANK YOU!