

Non-tax Revenue and Expenditure Structure of Local Governments in the ROK (Summary)

Joong-Ho Kook

Associate Professor, Faculty of Economics and Business Administration, Yokohama City University

Jung-Wook Shim

Graduate School of Economics, Hitotsubashi University

1. Non-tax Revenue

Looking at a breakdown of local government revenue in the ROK, we can see that the share of non-tax revenue is very high: for example, 40.9% of local revenues in 2000. However, local governments in the ROK do not obtain high revenues from non-tax revenues, such as users' fees, charges, and interest revenues.

Non-tax revenue in the ROK has the distinguishing feature that it includes a very high share of surplus revenue not used that year, which is carried over to the next. This surplus reaches 60.5% of net non-tax revenues. In contrast,

the sum of property rent revenue, revenue from rents, revenue from fees, business revenue, and interest revenue remains at best 17.6% of net non-tax revenues.

Why is the surplus so high? There are a number of reasons for this. Firstly, local governments in the ROK cannot make outlays from transfers received that year. This is because the central government makes a large number of transfers near the end of the year. It should also be noted, however, that not all of the surplus originates from the transfers not used that year.

Revenue from the previous year amounted to 69.3% in

2000, in the case of the general account. Of course, this figure denotes the surplus from 1999. However, carrying over a large surplus from 2000 to the following year could also not be avoided. For example, the share of revenue from the previous year carried over in 1998 amounted to 68.1% of the surplus, in the case of the general account.

Secondly, local governments tend not to make concrete estimates of the increase in local revenue resulting from policy changes, such as local tax reform. In the ROK, it is usual for the central government uniformly to decide policy reforms in order to increase local tax revenue. This deprives local governments of an incentive actively to estimate the effect of policy reforms on their revenue.

Thirdly, there is a political reason. Until 1995, the central government of the ROK appointed local government executives itself. Local government executives had a tendency to implement surplus budgets, which were praised more highly than deficit budgets. Even under the present direct election system, a large amount of local revenue is carried over as a result of the influence of this custom.

Judging from such practices, it can be said that non-tax revenue actually includes, to some extent, tax revenue and transfer revenue from past years. This means that the real share of non-tax revenue could be much lower. In other words, the real share of transfer revenue or local tax revenue could be higher. Therefore, it would be wise to ensure that the points discussed above are taken into account in interpreting the non-tax revenue of the ROK.

2. Expenditure Structure in Brief

The expenditure structure at each level of local government differs somewhat from the revenue structure. In lower-level local government, the shares accounted for by expenditure are higher than those of revenues because of upper-level local government transfers to the lower level.

A major characteristic is that lower-level local government accounts for a relatively higher share of expenditure than of revenue. The share of lower-level government was 61.7% of total expenditure in 2000. This figure is much higher than that for revenue: 45.6% of total revenue. Transfers from the province to counties are particularly noticeable among the figures. The provinces accounted for 11.7% of total expenditure in 2000, but 23.6% of total revenue.

The expenditure structure of local government can be seen in Table 1.

Table 1: Expenditure Structure of Local Government (2000)

Expenditure Items I	%	Expenditure Items II	%
Personnel	11.0	General Administration	16.9
Articles	11.8	Social Development	45.2
Transfers	19.4	Economic Development	34.5
Capital Expenditure	48.8	Civil Defense	1.9
Loan & Investment	2.2	Support & Other	1.5
Financing	3.2		
In-Transaction	3.2		
Contingency & Other	0.3		
Total	100	Total	100

Source: Ministry of Government Administration and Home Affairs, *Financial Yearbook of Local Government 2001*.

As shown in the right-hand side of Table 1, when excluding local education finance, economic development and social development account for 45.2% and 34.5% of total expenditure in 2000, respectively. In order to investigate the expenditure structure of local government, however, it is

necessary to take into consideration the expenditure of the special account for local education as well. Local education finance expenditure, which is not shown in Table 1, is also high, as shown in our article in the previous issue of ERINA Report. Given this expenditure structure in the ROK, we can see that local governments mainly provide public services in the fields of social development, economic development, and education. In addition, as shown in the right-hand side of Table 1, the share of capital expenditure, which is closely related to economic development, is high.

3. Concluding Remarks on the Two Articles

This article has discussed the following characteristics of local public finance in the ROK. Firstly, local education finance is separate from 'ordinary' local finance, being operated as a special account under the control of the Ministry of Education. In contrast, 'ordinary' local finance is strongly controlled by the Ministry of Government Administration and Home Affairs. Local education finance is highly dependent on transfers from the central government.

Secondly, local governments have little power to decide their own tax rates and tax bases. In addition, local tax revenue accounts for a very low share of total revenue items, while there is also a severe imbalance between national tax and local tax revenues. For example, only 26.4% of local government revenue was collected from local taxes in 2000. Furthermore, the elasticity of local tax revenue to GRDP is not high because local taxes are heavily reliant upon property taxation.

On the other hand, the issue of bonds by local governments is extremely limited for two reasons: 1) when local governments want to issue new bonds, they have to obtain approval from the central government, and 2) the taxation power of local governments is severely restricted.

Thirdly, though non-tax revenue accounts for the highest share among all the local revenue items (40.9% of local revenues in 2000), it does not mean that the share of non-tax revenues, such as users' fees, charges, and interest revenues, is high in reality. In contrast to this, the share of surplus carried over is very high, and this surplus is classified as the one item of non-tax revenue. For example, the surplus has reached 69.3% of non-tax revenues in the general account. However, the sum of property rent revenue, revenue from rent, revenue of fees, business firm revenue, and interest revenue is at best 17.6% of net non-tax revenue.

Fourthly, there are large amounts carried over to the subsequent year that cannot be spent that year. The reasons for the large surpluses include: 1) the central government's tendency to carry out many transfers near the end of the year, 2) a tendency to underestimate the effects of policy reforms that will lead to an increase in local government revenue, because the central government is inclined to decide policy reforms uniformly, and 3) surplus budgets have historically been considered more desirable than deficit budgets, for political reasons.

Finally, on the expenditure side, local governments mainly provide local public services such as social development, economic development, and education. Moreover, capital expenditure accounts for the highest share, equal to 48.8% of local expenditure. Remembering that transfers are an essential part of local government revenue, it can be argued that capital expenditure plays an important role in regional economic policy.