

# **Promoting Transparency And Accountability of Local Public Finance in Korea**

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## **Abstract**

With very short history of local autonomy, her local fiscal system leaves much to be desired. In this paper, it is attempted to give policy suggestions to promote transparency and accountability of local governments.

Suggestions are as follows: First, use of the performance based budget should be expanded. For this, proper measure for the performance and the technique to analyze it should be developed. Besides, double entry bookkeeping system should be used and the accrual accounting is to be used in the long run. Second, monitoring system on local governments should be reformed. More emphasis of the government audit should be on the performance audit and redundancy of it should be avoided. Monitoring by citizens should be expanded with better access to information. Third, Maintaining fiscal soundness is important. Proper but not too strict control over local government bonds should be exercised and the regular review and evaluation of the fiscal soundness of local governments is necessary. Fourth, reform of the intergovernmental transfer system should be done. Particularly, special grant should be abolished, computing formula for the standard fiscal needs should be simplified, and the many expenditure programs carried out with subsidy should be transferred to local governments with matching funds. Finally, taxing and revenue mobilization power of local governments should be enhanced.

## **I. Introduction**

Fiscal decentralization is the trend that cannot be reversed in many countries, and Korea is not an exception. Decentralization, at the same time, requires the accountability. In other words, without securing accountability, attempt to decentralize power and function of the central government is likely to fail.

Unlike many OECD countries, Korea has a relatively short history of the local autonomy. Korea has been a highly centralized country for more than a thousand years, and may be one of those rare countries that have not experienced the feudal system. Since it is only recently that the full scale local autonomy is introduced, some degree of trial and error is unavoidable. As a consequence, there is much to be desired in current local fiscal system in Korea.

The purpose of this paper is to suggest possible solutions for such problems, focusing mainly on the accountability and transparency which are closely related each other. As Tanzi (2000) correctly put it, greater fiscal transparency induces greater accountability.

Needless to say, transparency and accountability are very important at both the local and national public finance. When it comes to the local level, there is a unique problem regarding the relationship with the central government. Substantial part of the control to secure the transparency and accountability is exercised by the central government. This kind of control by the higher level government generally take the form of such measures as limitation on setting local tax rates, control over borrowing power, and so on. These are the measures which generally tend to limit the degree of decentralization. Therefore, to solve such dilemma would be a main area of promoting transparency and accountability in local public finance.

In this paper, Reform measures to enhance transparency and accountability will be suggested in Korean context. Those measures include the wider application of performance based budget, maintaining fiscal soundness, reform on the intergovernmental transfer system, reform of the audit system and expansion of surveillance by citizens, and greater autonomy of revenue mobilization by local governments including greater taxing power. Although this paper deals with Korean case, policy suggestions made here could be applied to many other countries.

## **II. Reform Strategies**

### **1. Wider Use of Performance Based Budget**

#### **A. Performance Based Budget**

Lack of transparency is often caused by the fact that the outcome of the government expenditure is not defined and clearly shown. If this can be done well, then the accountability is also attained. This is why so many countries have tried to introduce performance based budget system in the last two decades.

Performance of the performance based budget system may not have been great, however. First of all, it is very hard to measure, and it may end up with huge file of documents and little results. Even if that is true, it is worthwhile to try to apply it particularly on the budget of the local government. Then, what makes us to believe that the performance based budget works better in local public finance? It is because that the local public good, in general, is closer to the private good than that provided by the central government so that it is easier to measure performance. Therefore, it is meaningful to introduce performance based budget system in the local fiscal system. For example, 30 state governments in the United States implemented performance-based budgeting under specific legislation, and 15 state governments did so without legislation in 1998.

Primordial Budgeting system concerned with performance was first developed just before World War I in USA. Then, under the auspices of the Hoover Commission of 1949, the designation performance budgeting was officially sanctioned as the preferred budgeting. The performance budget envisaged by the Commission consisted of these elements: (1) program and activity classification of government transactions, (2) performance measurements, and (3) performance

reporting. As is well-known, the most important factor in performance budgeting is “performance measurement.” It was derived from cost accounting and the approaches of scientific management and provided a basis for the use and the cost of manpower and other factors of production, the effectiveness with which they are used, and the accomplishments made in the process. Performance measurements implied the specification of yardsticks for efficiency that could be employed to set predetermined standards to observe performance over a period of time or make comparison with other similar organizations.

Under the traditional line-item budget, the focus was on the amounts needed to pay for things: personnel, equipment, supplies, etc. Such a presentation revealed little about what was accomplished as a result of such expenditures. Policies, programs, and activities of the spending units of government were not incorporated into the budget document. Performance budgeting, then, is an attempt to go beyond the money alone and the mere objects being bought and paid for to look at the services being provided and the activities being carried out. Further, it seeks to attach cost figures to those programs and activities. Budgeting takes on a different appearance in response to the need to present information in a different context. Tied to cost-accounting techniques, performance budgets presented manager and policymakers with detailed breakdowns of the unit costs of agency outputs.

This is the basic idea and it has been evolved with different names and programs such as Performance Budget System (by Hoover Commission above), Planning-Program Budget System (PPBS), Management By Objective (MBO), Zero Base Budget (ZBB), Output Budgeting, and Outcome Budgeting etc, and finally it has blown fully in the 80’s in most of OECD countries.

How then can we successfully introduce and operate the performance based

budget? It is well known that the development of the proper performance measure (or indicator) is most important. It is also well known that it is very hard to be developed. Since these measures must be different from program to program, there cannot be any a priori principle that can be used universally. It is not our purpose here to discuss details of such measures despite existence of long list of papers and articles on this matter. Instead, it should be emphasized again the well known fact that the outcome should not be confused with output. If that happens, true economic effect of certain expenditure programs will be distorted.

It is important to have proper documentation for the performance based budget. The document should be prepared on the basis of functions and objectives of the several agencies and departments of government rather than exclusively on the basis of objects of expenditure and organizational units. This presentation is especially important for those who give attention to the budget after it leaves the unit which originally prepares it. Thus, the format and presentation are vitally important to the legislative bodies that pass judgment on the merits of what is presented and that authorize funds for the administration of the substance, Also, the form of presentation is important for responsible citizens or groups of citizens who actively participate in the budget process.

Evaluation results of the performance should be linked to the allocation of the budget, promotion, salary decision as rewarding devices<sup>1</sup>. For example, the GPRA in U.S. requires that federal agencies submit the results of performance measurement for a given year with their budget request for the following year. Thus, originally, the performance measurement initiative was to be integrated with the budget process. It is very notable that many state governments actively

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<sup>1</sup> About details, see Y. Yun @ Y. W.on, "A Framework of Financial Performance Analysis Under the Accrual-Based Governmental Accounting 2002

integrated their budget system with their planning system between 1990 and 1995. Through this, the legislature is able to control not only budget input, but also the outcome of the budget at the same time.

Finally, for this system function well, related area should also be well developed. First, generally accepted accounting system including double-entry bookkeeping must be used in government accounting. It is also desirable for the governmental accounting system to be gradually changed to accrual basis. Next, development and wider application of the cost-benefit analysis with proper social discount rate is necessary<sup>2</sup>.

As indicated, every aspect of the performance based budget cannot be explained here. Instead, case of Seoul Metropolitan Government will be briefly explained so that we can get the idea of actual process currently going on. As a matter of fact, it was the central government of Korea that initiated performance based budgeting in 1999<sup>3</sup>. Under the direction of the central government, the SMG prepared the action plan of performance-based budgeting in 2000 and began to implement it in 2001.

#### B. Case of SMG<sup>4</sup>

Before the performance based budgeting is introduced, Management by Objectives (MBO) was already introduced as a means of assessing the degree of individual contribution to the achievement of organizations.

Strictly speaking the MBO of the SMG is not a means of measuring

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<sup>2</sup> See Jay-Hyung Kim, "The Emerging Performance Evaluation Architecture For Korea", 2002

<sup>3</sup> Pilot studies for several agencies are still going on.

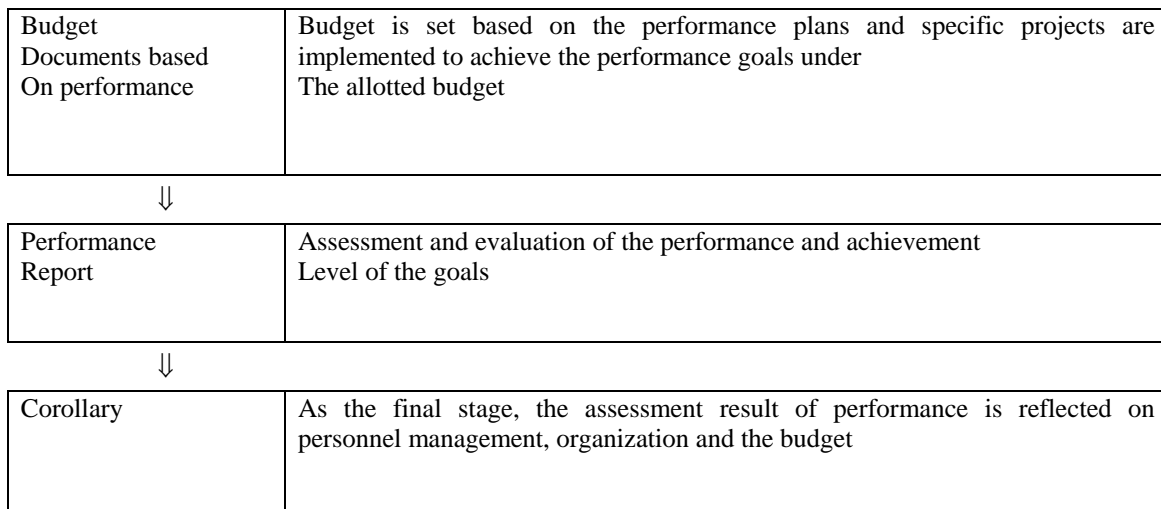
<sup>4</sup> This part is heavily drawn from Jong-Soon Kim & Hwang-Sun Kang, "Performance Measurement: A Status Report And Reflection" in ed. By M. Holzer & B. Kim, "Building Good Governance : Reforms in Seoul", 2002

organizational performance, but a control system over individual performance. MBO was a mandatory program directed by the central government of Korea. Under their guidance, but SMG has developed a more feasible model of MBO for the city administration. Under this model, the objectives for an individual for a given year are assigned; then, the achievement levels of the objectives are evaluated on a regular basis and reflected on his/her personnel records. The assessment of the operation of city administration based on performance and achievement is thus made possible under the system. The objectives of an individual are designated through consultation with the supervisor. The objectives set for an individual are the means of assessing the performance of the organization, which is more important.

Those involved in MBO play important roles in the performance-based budgeting process. As organizational objectives are determined by managers of each agency in consultation with the office of planning and budget and outside experts, the important task that links the budget with those objectives is given to them as well.

<Table 1> Procedures for Setting the Budget Based on Performance

Designation of Objectives	Based on the missions assigned to the unit, each office and bureau designates the strategic objectives, which are the priority goals, as well as performance goals, which are the specific measures to achieve the strategic goals
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Performance Plans	Specific business plans to achieve the said goals are established And the index to calculate the business expenses required and to assess the achievement level of the goals is formulated
↓	



In general, the budget system of SMG is operated under the following systems and procedures. In order to link Management by Objectives with the performance-based budget, the SMG came up with the following plans; first, to designate the priority strategic objectives as well as mid-to-low priority performance objectives for each office and bureau in the organization; second, to develop a performance index to facilitate the assessment and measurement on the goals achieved; and third, to establish a verification system to estimate and evaluate the performance achieved. Furthermore, in order to link the performance objectives for each office and bureau with the unit project for achieving the goals, the budget and performance plans were formulated so that the details and methods of assessing and evaluating the performance goals through the strategic objectives and unit projects are represented in the performance plans.

**<Table 2> Details on Improvement Following Changes in the Execution of the Budget**

Before	After
<ul style="list-style-type: none"> <li>· Ask for larger budget to secure more funding without having specific plans</li> </ul>	<ul style="list-style-type: none"> <li>· Balanced budget requests in consideration of the performance</li> </ul>
<ul style="list-style-type: none"> <li>· Routinely call for an increase of a certain percentage in the budget from the preceding year</li> </ul>	<ul style="list-style-type: none"> <li>· Deliberate on the budget planning in consideration of the performance goals and objective evaluation system</li> </ul>
<ul style="list-style-type: none"> <li>· Use up all of the budget allocated as a general practice</li> </ul>	<ul style="list-style-type: none"> <li>· Administer the budget with responsibility and make efforts to reduce wasteful use of the budget</li> </ul>
<ul style="list-style-type: none"> <li>· Focus on the legitimacy in administering the budget which calls for passive work behavior</li> </ul>	<ul style="list-style-type: none"> <li>· Induce active work behavior by considering the post evaluation result and linking to the budget allocation the following year</li> </ul>

Source: SMG(2001)

After 2002, it is strongly recommended that agency should be able to set up their own “mission vision statement” that is the source that organizational objectives are drawn from. In order to actively implement the responsible management system by each office and bureau, autonomy was granted in designating the objectives, namely formulating the business plans and setting up the budget. Responsibilities of the offices and bureaus for the outcome of operating the budget were thus strengthened. Under the system, each department administers the budget for the unit’s business in order to achieve the goals for each stage. Achievement level and performance level of the goals area assessed through inspections and analysis by evaluating the performance of the business. The results are reflected in personnel appraisal, and a system of incentives to individuals or units for cost saving has been formulated, leading to a more

efficient operation of finances.

MBO and performance-based budgeting are similar managerial tools in that both utilize performance measurement. Both need performance indicators with which to measure organizational goals. Thus, using performance indicators as a link, MBO and performance-based budgeting can be integrated. Now, the SMG tries to integrate those systems within a performance management system. Through the integrated system, it is expected that each department can use the same indicators in order to measure both organizational performance and personnel job performance so that a lot of administrative time and cost might be reduced. Under an explicit mission vision, employees are clearly aware of what they are expected to do in order to achieve their organizational goals.

<Table 3> Basic Structure of the Performance-Based Budget in SMG

The mission and strategic objectives of each department	Designation of the mission, strategic objectives and performance objectives for each department
Objective for each project	Designation of the performance index and the Evaluation method for each project
Drawing up and administering the budget	Reflection of the performance objectives and evaluation Results in drawing up and implementing the budget
Assessment and evaluation of performance	Making public the evaluation result and the feedback

Source: SMG(2001)

## 2. Monitoring of Local Governments

### A. Audit

Traditionally, the audit has been in the center of monitoring various levels of government. Therefore, it has been one of the major functions of the government. In Korea, overall audit is carried out by the Board of Audit and Inspection (BAI) which is a constitutional institution. It carries out periodic audits and inspections every year of central and local government agencies as well as of government-financed institutions. The BAI is responsible for investigation of whether the budget has been allocated as originally planned, whether budget expenditure has been executed legally, and whether excess expenditure exists.

The BAI is legally responsible for both financial and performance audit, but, in Korea, its function is limited to financial audit. This is because the BAI is required by the Constitutional Law to report the result of financial audit to the National Assembly and the President. But the performance audit is not given, by the Law, the importance as much as financial audit.

There are two types of financial audit: compulsory and elective audit. The BAI is required to audit every year the central and local government agencies, government-financed institutions, and all other agencies that are stipulated to be audited by the BAI. But the BAI also, by the request from the Prime Minister, can audit finance or many other institutions to which the central and local government agencies subsidize or make financial contribution. The BAI can audit before and after government expenditure is made. But, in Korea, financial audits of the BAI are performed usually after government expenditure is completed; therefore, the audit can be only an ex post review of government budget expenditure.

The BAI, through financial auditing, usually confirms whether the information related to budget execution is recorded by established accounting guidelines; looks into whether information includes any error or wrongdoing; and then reports true information. The purpose of a financial auditing is to investigate whether budget expenditure is legally executed or not. Of course, confirming whether budget account is recorded by accounting guidelines is a broader concept than just judging whether the information included in budget account is true or not. But, in Korea, a financial auditing without accounting guidelines takes the latter form and therefore, it can be classified as a narrow concept of auditing.

Beside the audit by the BAI, National Assembly also conducts special audit<sup>5</sup> during the general session in Fall. This audit concentrates more on the performance audit. Besides, central government, local congress all conduct audit and inspection over local governments. Thus, this might be regarded as the overlap or redundancy of audits.

This phenomenon may have a bright side because the more is audit, the more transparent is the government. On the other hand, too much audit is problematic because of two reasons; first, it keeps local civil servants to the pitfall of the unnecessary burden and second, it discourages them to engage in “meaningful and important, but risky” programs. Therefore, it is necessary to reduce the number of agencies conducting audit and inspection.

In sum, as for the government audit, it is suggested here that the focus should be more on performance audit than the traditional financial audit. For this,

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<sup>5</sup> Although the term “audit” is used in both cases, their emphases are slightly different. The audit by the Board of Audit and Inspection is concentrated on checking legality and lawfulness, while that of the latter is relatively more

expertise of inspectors are to be enhanced which in turn requires more training and education and less circulation of the position. Redundancy of audit should be avoided.

#### B. Monitor by Citizens

Recently, direct surveillance by citizens, as one important part of the participatory democracy, becomes more and more popular throughout the world. This is actually a major part of the “Open Government”. One of the main factors which makes it possible is the rapid development of the IT (Information Technology) and as a consequence, it is quite related with the development of “e-Government” as well. Obviously, this cannot be a direct substitute but rather a complement of the government audit. Therefore, its use must be expanded.

There are several ways to monitor local governments. These include Public Hearing on the budget by citizens, Petition of Audit by Citizens, Lawsuit filed by Taxpayers on improper usage of the budget. Indeed, some of them are already codified in Korea. It is not so frequently used as intended, however, partly because governments are reluctant to cooperate and partly because prerequisites for the implementation are too restrictive<sup>6</sup>. Therefore, amendment of related Law is necessary.

It goes without saying that greater access to information is a key to the success of monitoring by citizens. It is, in fact, the second principle of “Code of Good Practices on Fiscal Transparency” by Tanzi (2000). Although it is a legal right to have the full access to information except for exceptional cases, it is sometimes hard to have that. It should be changed.

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on the performance.

<sup>6</sup> For example, number of petitioners are to be decided by decree within one fiftieth of total residents in locality

There is a case in Korea closely related with monitoring by citizens. City of Seoul (Seoul Metropolitan Government : SMG) recently introduced a new system which is called the “The Seoul Metropolitan Government’s Online Procedures Enhancement System (OPEN system)”. This system was developed with the purpose of “preventing corruption in those administrative procedures, which handle citizen’s applications for municipal permits, licenses and other documents”. Thus, the area it covers is not the whole of the functions of Seoul Metropolitan Government but a part of it. However, this limited area is where corruption is most likely to occur. List of those functions are presented in table A1.

It is believed that this system has performed fairly well. Transparency can be achieved by preventing unnecessary delays, arbitrary decisions because citizens (not applicants only) can monitor progress in the processing of applications. Data shows that the SMG employee’s bribery case has been drastically decreased from 1999. In 2001, city officials’ involvement in bribery charges are only 39.5% of that of 1999. Besides, all the survey results conducted to evaluate its performance do show that this has been successful.

If it was successful, what are the factors behind it? Knowing them would be important so that they can be used in the process of reforms in other local governments. Park (2003) points out five factors like the following; 1) leadership, 2) corporation between Audit and Inspection Bureau and Information System Planning Bureau, 3) high level of information disclosed, 4) voluntary acceptance / compliance of the employees, 5) public relations. What draws our attention most among them are 2) and 3). Since the environment and conditions that each local government is situated is different, it is not proper to argue that they should follow exactly same paths. But adoption of the system similar to “OPEN” is desirable, and local governments should consider abovementioned factors in

doing so.

Some argue that NGO's should directly participate in the audit and inspection processes. This is not proper, however, because NGO's cannot legitimately represent general public. It is fine to give them better access to information and expand channels to enable them to express their views and opinions. But their role should be limited there.

Besides, there is an argument that citizens should actually participate in the process of formulating and in-year control of the budget. This is not appropriate either because people who would participate do not have a mandate. If it is necessary, these people should be through election process. Members of local parliament are enough to do it. Again, having greater access to the actual budget and more opportunity to express their opinions and let them reflected in the budget process is desirable and should be encouraged. But, they cannot replace elected officials in this area.

### 3. Maintaining Fiscal Soundness of the Local Government

As Bahl (1999) put it, Ministry of Finance, as one of the major detractors of the decentralization policy, tries to control the borrowing powers of local governments. This was a major concern in Korea when local autonomy started. Therefore Korean government also put strict control on the issuance of local government bond. Currently, local government bond can be issued only with the permission of the Ministry of the Government Administration and Home Affairs, case by case. Once the proposal to issue new bonds to fund certain expenditure program is submitted to MOGAHA, that proposal is reviewed thoroughly particularly on the terms, conditions, repayment schedules and so on. Only if the

review result is affirmative, bond issue is permitted.

This is not totally irrational considering tendency of local governments to expend without securing proper fund. Indeed, Japan has experienced serious problem regarding this. Even if a certain degree of control over the borrowing power of local governments for the sake of accountability, too strict a control as in Korea is criticized because it puts too much limit on the control of the expenditure by local governments.

Whether it is desirable or not, central government of Korea seems to have succeeded in curbing debt of local governments. As can be seen in table 3, proportion of the local government in total expenditure has decreased after 1996 which is right after the first election of governors and mayors, although the absolute amount of new bonds keeps increasing.

<Table 4> Trend of Local Government Bond

**Change of Local Bonds Issue**

	Local Bonds Issue	Local Bonds/Expenditure
1981	397836	13.5
1982	579727	16.1
1983	777458	17.1
1984	692699	13
1985	616479	10.6
1986	791701	12.1
1987	755272	10.1
1988	870043	9.8
1989	1130225	10
1990	2256235	14
1991	3193046	14.6
1992	2795065	10.5
1993	3201615	11.1
1994	3609828	11.1
1995	n.a.	n.a.
1996	4049761	9.1
1997	4458041	8.8
1998	4618519	9
1999	5293697	9.8

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

This is certainly a different phenomenon from cases of Latin America or Japan. Thus, it is suggested that the control must be on total amount bases. In other words, central government put some ceiling on the total amount of new local government bonds, and let local governments decide the size of bond for each program.

Although it is a progress as long as the discretion of local governments is concerned, critiques still believe that it is not enough and argue that such control should be abolished entirely. We oppose such proposal simply because it is too

early to conclude that the “spending without properly securing fund” tendency cannot be found. Once that control device is totally lifted, it is very likely that the local debt will snowball.

Besides, together with this modification, it is suggested here that the regular check and evaluation of the fiscal soundness should be conducted. Organization which carries out such function may have the form of board or committee, members of which consist of outside experts, bureaucrats of both levels of government. Regular check as such will enhance the accountability of local government expenditures.

#### 4. Intergovernmental Transfer System

Like many other countries in the world, Korean grant system (Tax Share System) is a formula-based one. There is, however, an ad-hoc grant which captures one eleventh of the total grant. This is ad-hoc because its distribution is not based on the formula but on the discretion of the Minister of the Government Administration and the Home Affairs. It is believed that the political concern is behind such distribution. This, in terms of Bahl (1999), is one of the major detractors of fiscal decentralization and a serious blow on the transparency of the local Public Finance. Thus, it must be abolished.

Another problem of Korean Tax Share system is caused by the improper computation formula of the so-called standard fiscal needs (or basic financial needs). These needs are supposed to be equal to the actual expenditure needs by the local governments necessary to provide basic services. This system, however, is criticized because computing process based on formula is not transparent at all. This formula is based on 31 variables, the weight of each is

not known with many modifying factors (see Table 5).<sup>7</sup> Because of this, standard fiscal needs have fluctuated erratically (See Table 6).

<Table 6> Trend of standard fiscal needs (Million Won, %)

	2000	2001	2002	%change	
				2001	2002
Total	16,275,441	20,355,528	22,442,447	25.1	10.3
Metro	3,288,488	3,798,522	3,989,355	15.5	5.0
Provinces	2,537,058	3,074,411	3,304,529	21.2	7.5
Cities	5,912,898	7,064,565	8,160,671	19.5	14.8
Counties	4,536,997	6,418,030	7,041,892	41.5	9.7

source: MOGAHA, "Manual for local share tax", 2000, 2001, 2002

What’s really serious about this lack of transparency is unpredictability of the revenue of each local government. This is harmful to accountability of the local governments because they cannot properly plan the expenditure. Also, there are variables used for the computation of the basic needs which are regarded as encouraging unnecessary expenditures by local governments. For example, local governments with larger number of civil servants are supposed to have greater standard fiscal needs (in turn, receive more grant) because number of civil servants is one of the variables for calculating standard fiscal needs.

<sup>7</sup> About details please see Yong-Seong Kim, “Intergovernmental Fiscal Transfer in Korea” July, 2003

As a result, officials of local governments tend rather to lobby central government officials or congressmen to get bigger budget than to increase tax effort or reduce expenditures. This is obviously neither accountable nor efficient.

Next, there are problems related with subsidy from the central government. Among many problems, the most serious one is too much interference by ministries of the central government, admitting that certain degree of control by the central government is necessary. Clearly, too much interference and control is against enhancing the accountability. Especially, it is observed that the share of the subsidy among three transfer mechanisms has increased recently (see figure 1). This trend may be interpreted as “disguised centralization”.

<Figure 1>

To correct this problem, it would be most desirable if we could find means to minimize control by ministries. It is, however, very hard to implement. As a second best solution, drastic reduction of the subsidized programs is suggested here. Such programs should be carried out by own budget of local governments.

## 5. Enhancement of Local Government Taxing Power

Unless enough fund is secured, local autonomy cannot persist. Currently, share of national tax revenue in Korea is around 80% of total tax revenue while expenditure of the central government captures around a half of total expenditure. It is somewhat natural for the relationship between two levels of government, and that is the reason why there exists intergovernmental transfer system.

The story is different, however, taxing power of local governments are seriously limited. In that case, not only autonomy but also accountability is damaged because local governments cannot but rely either on borrowing or transfer from the central government. If necessary, local governments should be able to raise tax rates or levy new taxes. As Bahl (1999) pointed out, voters will hold their elected officials more accountable if local public services are financed to a significant extent from locally imposed taxes, as opposed to the case where financing is primarily by central government transfers. He also argues that the tax must be visible to local voters, large enough to impose noticeable burden.

Currently in Korea, the tax base and rate are required to be legislated in law which should be passed in the National Assembly. To overcome this problem, local governments are allowed to use the elastic tax rates and their tax base as “extra law tax item”. The latter means that the some local taxes can be levied under the decree instead of law. It is seldom used however.

Therefore, it should be allowed that local governments could set their own tax rates and introduce new taxes depending upon the environment and situation of each local government. For that, we first determine which could be good tax bases.

Probably local Value Added Tax (VAT) is an appropriate candidate. Under Bahl’s argument, Korea is good case to have local VAT because there is a strong, well-administered VAT with a uniform base. As he correctly pointed out, this condition is not met in most developing countries. Hur (2003) suggests that it should take the form of tax sharing like the case of Japan for interim periods before the final decision about perfect switch to local VAT is made.

It is well known that the property tax is a most appropriate source of local

government revenue, so that it is indeed an important revenue source of local governments in many countries including Korea. As Bahl (1999) correctly summarized, it is good as a revenue source for local governments because of the following reasons: First, local government services tend to benefit property owners and occupants, hence it is a kind of benefit tax. Second, the burden of tax is not easily exported. Third, it is highly visible in the local area because it is a tax on wealth. Finally, local assessors have a comparative advantage in identifying local property wealth. There is, however, a weakness of the property tax as a local revenue source. It is administratively difficult and expensive, and politically unpopular mainly because there can be disagreement on the assessed value of the property between tax payer and the tax authority. This is why the effective tax rates tend to be kept low, and share of the property tax revenue is low.

With regard to the first reason, an important policy implication can be drawn. Currently in Korea, it is hard to find a linkage between benefit of the property owners and the burden of the property tax. In that case, the property tax is likely to induce tax resistance because of the abovementioned reason. Thus, it is strongly recommended that the burden of the property tax should be directly linked to the benefit of the expenditure. One way must be linking property tax with the education as in America.

Finally, local governments should be allowed to introduce new taxes which are appropriate regarding economic and social situation of the region. For example, tourism tax can be introduced in Gangwon province.

### **III. Concluding Remarks**

Considering very short history of local autonomy and lack of experience, it is natural to expect that much to be desired in current local fiscal system in Korea. In this regard, following policy measures to promote accountability and transparency of local governments are suggested here.

First, use of the performance based budget should be expanded. For this, proper measure for the performance and the technique to analyze it should be developed. Also, evaluation results of performance measures should be used in the allocation of the budget, promotion, salary decision as rewarding devices. There should be an improvement in related areas. For example, generally accepted accounting system including double-entry bookkeeping must be used in government accounting. It is also desirable for the governmental accounting system to be gradually changed to accrual basis. Well-developed cost-benefit analysis should be actively used as well.

Second, monitoring system on local governments should be reformed. More emphasis of the government audit should be on the performance audit and redundancy of it should be avoided. Expertise of inspectors are to be enhanced which in turn requires more training and education and less circulation of the position. Monitoring by citizens should be expanded with better access to information.

Third, Maintaining fiscal soundness is important. Proper but not too strict control over local government bonds should be exercised and the regular review and evaluation of the fiscal soundness of local governments is necessary.

Fourth, the reform of the intergovernmental transfer system should be carried out.

First of all, special grant should be abolished, and computing formula for the standard fiscal needs should be simplified. Many expenditure programs carried out with subsidy should be transferred to local governments with matching funds.

Finally, taxing power of local governments should be enhanced. For this, local VAT can be introduced and the property tax should be linked to the public education. Local governments should be allowed to levy new taxes which are appropriate regarding the economic and social situation of the region.

Policies suggested here contribute not only to the promotion of transparency and accountability but also to other goals such as efficiency, regional balance, and finally to decentralization. Since Korea is still at the early stage of the decentralization, design of detailed action plans to implement suggested measures should be started now.

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<Table 5> Frequency of Measuring Units

Measuring unit	Frequency	Needs Categories
Number of Local congress Member	1	Legislation and Election administration expenses
Number of Election District	1	Legislation and Election administration expenses
Regular staff of Public service personnel	3	Gernal administration expenses
Number of Households	3	Gernal administration expenses Improvement expenses for health and life environment
Size of Population	10	Education and culture expenses Improvement expenses for Health and life environment Social security expenses Development expenses for House and Local society Development expenses for Local economy Preservation-development expenses for Country resources
Number of Workers in specially designated fields	3	Improvement expenses for health and life environment Development expenses for Agricultural-marine products Development expenses for Local economy
Size of Area	7	Improvement expenses for health and life environment Development expenses for House and Local society Development expenses for Agricultural-marine products Preservation-development expenses for Country resources
Number of Automobile	1	Traffic management expense
Number of Civil defense corps member	1	Civil defense management expenses

<Table A1> Civil Applications Available on the Web

	Services		Services
Industry & Economy	<ul style="list-style-type: none"> <li>- Adjustment of gas consumer rates</li> <li>- Registration of of large-scale shops</li> <li>- Financial assistance small and medium enterprises</li> <li>- Factory approval and registration</li> <li>- Permit and sanction of gas business</li> <li>- Permit of livestock-related business</li> <li>- Registration and sanction of petroleum sales(gas station)</li> </ul>	Culture & Tourism	<ul style="list-style-type: none"> <li>- Review of compulsory installment of art objects</li> <li>- Registration of sports facilities</li> <li>- Contract for operation of community sports centers</li> <li>- Distribution business</li> <li>- Approval for tourism business</li> <li>- Registration of tourism business</li> <li>- Hosting of local culture events</li> </ul>
Transportation	<ul style="list-style-type: none"> <li>- Assessment of influence on traffic</li> <li>- Adjustment of taxi fares</li> <li>- Installment and adjustment of village shuttle bus routes</li> <li>- Pricing criteria and bus fares</li> <li>- Settlement of intra-city bus routes</li> <li>- Approval for express bus and intercity bus terminal operation</li> <li>- Registration and sanction of automobile management business</li> <li>- Truck freight business registration</li> <li>- Sanction on mover business</li> <li>- Sanction on business vehicles</li> <li>- Approval for license transfer for owner-driven taxis</li> </ul>	Environment	<ul style="list-style-type: none"> <li>- Purchase of land for parks</li> <li>- Approval and agency contracts for waste disposal business</li> <li>- Approval and sanction of excreta-related business</li> <li>- Permit and sanction of air pollutant exhausting facilities</li> <li>- Registration and sanction of vehicle inspection agencies</li> <li>- Registration of noise- or vibration-producing facilities</li> <li>- Registration and sanction of dust-dispersing business sites</li> <li>- Registration and sanction of toxic substance handling</li> </ul>
Housing	<ul style="list-style-type: none"> <li>- Housing construction projects</li> <li>- Building permits and inspection</li> <li>- Hosing redevelopment projects</li> <li>- City center redevelopment</li> <li>- Improvement of residential areas</li> <li>- Sanction on architects</li> <li>- Permit or outdoor advertisement</li> </ul>	Urban Planning	<ul style="list-style-type: none"> <li>- Approval for acts of chancing topography and soil</li> <li>- Decision and change of urban development plans</li> <li>- Approval of topography and soil changes in limited development districts</li> </ul>
Construction	<ul style="list-style-type: none"> <li>- Compensation</li> <li>- Facility construction</li> <li>- Construction technology services</li> <li>- Contract for facility maintenance</li> <li>- Construction business registration</li> <li>- Approval for use of rivers</li> </ul>	Firefighting	<ul style="list-style-type: none"> <li>- Inspection on completion of firefighting facilities</li> <li>- Approval and sanction of establishment of dangerous article factories</li> </ul>
Sanction	<ul style="list-style-type: none"> <li>- Contact for social welfare facilities operation</li> <li>- Approval and sanction of entertainment establishments and song bus</li> </ul>	Administration	<ul style="list-style-type: none"> <li>- Purchase of government supplies</li> </ul>