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PECULIARITIES IN LOCAL FINANCE

By Dr. Masao KAMBE*

The matter of local finance has rarely attracted public attention like that of state finance; hence its studies were not satisfactory. But as its importance has increased gradually and many examples of poor administration have been uncovered, more attention has been given to it. This tendency was very favorable for furthering the study of the subject. Now, since this local finance is also a sort of finance, it may be considered, so far, that it is enough to apply to it the general principles of state finance, but the truth is that it differs from state finance in its nature and, consequently, in its principles. To try a mere application of state finance without paying much attention to this fact, therefore, will do little good to a successful operation of local finance. Such being the case, I am trying to point out in this paper the fact that there are some differences between the two. Now then, what differences can be found there?

(1) Extent of Jurisdiction of two bodies

At first, the extent that the influence of a political body reaches is different. It is smaller in case of the local government while it is wider in case of the state. A local community stands as a part of the whole

* The author is emeritus professor at Kyoto University

in relation to the state. Therefore, the sphere of the influence of the state government is far wider than that of the local government, and is fertile in complex resources within it, which, if utilized wisely, will enable the state to carry on vigorous financial activities. On the contrary, the local government has smaller jurisdiction, the narrowness of which may differ according to localities. A local government may have crowds of people and things within its narrow boundary and be rich in economic resources which enable it to do a large scale financial activity if made best use of them, while another government, and perhaps most of local governments, may be poorly endowed with both people and materials, and their industries are primitive in most cases. With all means they have, even the ordinary administration does not go smoothly, not to speak of emergencies when they are visited by natural calamity or disaster, in which case, they can do nothing for themselves, but are obliged to depend upon the state subsidies. The necessity of the state subsidies for them is not confined to the time of emergency alone. Even in ordinary times, it is unavoidable for them to have recourse to the state subsidies, to the financial counterpoise subsidy or to the bounty tax and the concession tax which were recently adopted in Japan. Of course, the independence of local finance is desirable, but due to the reasons aforementioned, in some part of the state at least, the local finance does not enjoy a perfect autonomy and has the weakness of too much dependence. Nevertheless, the local community with weak financial autonomy must not take it for granted to draw the national subsidies and to rely too much upon the state, neglecting to exert its own power to the fullest, while at the same time the state govenment should make the surveillance strict not to have local finance indulge in depending upon it too much.

(2) Limitations upon the Free Action of the Bodies

In case of state finance, it can dispose of anything at its own discretion. Of course, there might be some limitations in actual practice. Moreover, it is also possible that the state bounds itself at its own will. But anyway it can manage affairs quite freely without being subject to any restriction of other political bodies. Local finance, on the other hand, is subject to state-stipulated laws from the very beginning, and is predestined to follow the directions thereof. It is needless to say that local finance has also ample room left to handle matters by its own judgment. Still, regarding certain matters, it cannot but obey state directions if the latter should instruct the former by laws to deal with the revenue or the expenditure in a certain way. If the state government orders to do certain administration and to defray certain expenses incurred by the administration out of certain resources, or not to turn public loans in certain cases, or, with regard to taxation, not to levy certain taxes, and certain taxes must not go beyond a certain amount, etc., local finance cannot but bow to the orders. No matter how much autonomy state government permits to local government as a matter of principle, it will result in detrimental impairment of the interest of the state as a whole should it allow local government to do the administration without any restriction. It is inevitable for state government to impose upon local governments various restrictions in order to avoid this result. It is feasible, indeed, that in some countries the decentralization of power prevails so extenssively that a decisively powerful local government is not obedient to state directions and takes its own course, but, of course, it isn't desirable at all. On the contrary, it is also feasible that the centralization of power is exercised so extremely, that the rules of state control over local governments are too complicated and the free action of these governments is checked unduly thereby. It has little to recommend it, neither. It is rather preferable in a democratic country that the autonomy of local finance is admitted as far as possible and is encouraged to extend. For this purpose, it is desirable that in the matter of expenditure the obligatory expenditure will be lessened to the minimum while the voluntary expenditure be extended to the maximum, and limitations upon the issuance of bonds will be relaxed as much as possible, and that in the matter of taxation the independent taxes will be expanded while taxes like the surtax, the bounty tax or the concession tax be lessened as far as possible.

(3) Expenditure

(A) Items of Expenditure

First of all, it must be conceded that since the scope and varieties of the administration from which state or local expenditure accrues are stipulated by state laws, the items of expenditure are provided in the laws. Then by what criterion is the administration decided? In the light of principles of the division of administration between state and local governments in a most advanced country, the following three principles are to be adopted : namely, the principle of clear-cut responsibility (the principle to specify partial charge to respective organizations and to have them assume the responsibility of their own), the principle of efficiency (the principle to put an organization of the best possible efficiency in charge) and the principle of local preference (the principle to give a local government a priority of taking in charge of those affairs which could be managed by it rather than by the state). According to these principles, the state government should be trusted such affairs as those which are essential for the existence of the state, the national overall programs, those which must be handled by state government from the view point of state control, those which go beyond the local limits and could not be disposed of by each of specific local governments quite efficiently, those which have nothing to do with local limits, and those which may promote the benefit of the nation, but could only be managed very inefficiently or improperly should they be done by each of specific local governments, while the local governments should be allowed to manage those affairs which can be done for themselves, with the above exceptions. At any rate, if follows that different divisions of admi nistration between state and local governments are established according to the laws stipulated by respective states, and that in compliance with these divisions some differences in items of expenditure between state and local governments are to be found. Of course, there exist items of the same nature in both for all of that. But there are such expenditures that the state government may have while the local government may not. For example, those items such as the national defense expenditure or the judicial expenditures are proper to state government and are not found in local government. In Japan, the constitution declares the abandonment of warfare, and naturally she has not the national defense expenditure in due form. In the face of this fact, a sort of expenditure corresponding to the national defense expenditure remains just as before since it is inevitable for her to defend herself at least so long as she exists. In actual practice, she has the self-defense army in place of the army and has the expenditures to cover the expenses incurred thereby as well as the partial expenses of the U. S. army which is stationed here to protect Japan. In any case, such item as the national defense expenditure is to be found in state finance and not in local finance. And that local government can do without such a huge and yet inflexible expenditure as the national defense expenditure, makes local finance much easier to dispose of, and reveals itself as one of the remarkable differences between state and local finances.

(B) Elasticity of Expenditure

The problem of great or small range of elasticity is found in state and local finances. The expenditure of the state government has little elasticity either to increase or decrease, and has such a huge amount of expenditures that cannot be cut down very drastically or that must be expended at any cost in a certain length of period for a certain item of expenditure.

In particular, the national defense expenditures can be mentioned as such in any country. This item takes a large proportion of the whole expenditure, and cannot be curtailed very much. Even in ordinary times, the state government may be obliged to spend fairly large amounts, making some degree of sacrifice, to keep a good balance with other countries in the then prevailing circumstances. It is of course unavoidable for the state government to spend extravagantly, particularly when a war begins. On the contrary, however, local government has little occasion for such an enormous and excessive expenditure as this. Those items which come under the category of obligatory expenditures may sometimes be called excessive in comparison with the power of a certain local community, but those which fall under the category of voluntary expenditures are quite flexible either to expand or to contract. If local government is financially powerful enough, it can afford to spend a large amount, and if it is not so powerful, it may still be content with a small expenditure. It is feasible sometimes that a local government has unduly large obligatory expenditures for its own financial power and that it may be obliged to spend disproportionately the emergency and relief expenditures in case of calamiy and disaster. But eventually this sort of expenditure must be considered by the state government and helped by state subsidy, grant or bounty tax, which are usually stipulated for by state laws. Except this, the expenditure of the local government has a wide range of elasticity, and its free expansion and contraction depends upon the financial capability of the said government.

(4) Revenue

(A) Items of Revenue

Speaking of the items of revenue, they are also divided between state and local finances in accordance with state-stipulated laws. From their nature, there are such items that may apply to both state and local finances while there are others that suit state finance but not local finance or that suit local finance but not state finance. It is, above all, a very important problem to decide what categories of taxes are appropriate to state government and what are to local government. As a matter of principle, those taxes which are endowed with the local divisibility of object of taxation (such property of object of taxation that makes it possible to divide it between a district and others, and to discriminate clearly that part belongs to A district and that to B for taxation purposes) are allowed to local government while those which, being lacking in this property, could not be easily assigned to one district, and which are rather fit to be taxed collectively are left to state government. For example, land tax, house tax, fixed assets tax; business tax (business tax is open to the charge of lacking slightly in local divisibility, but still devices can be found for its solution for all of that), immovable property transactions tax, direct consumption tax, and retail consumption tax are endowed with local divisibility of object of taxation, and tnerefore fit for local tax while income tax, corporation tax, property tax, most of circulation taxes, various kinds of consumption taxes, and monopoly revenue must be brought to the state government, though it is also possible as a matter of fact that the state government may apportion taxes in a different way on the score of a policy to its advantage. At any rate, respective items of revenue are divided between state and local governments in accordance with state stipulated laws in actual practice. In consequence, differences in the items result in state and local revenue.

(B) Elasticity of Revenue

The elasticity of revenue is large in state finance while it is small in local finance. The state government can decide at liberty the items of revenue at its own discretion, if necessary, and it is even possible for it to deprive the local govenment of those items once apportioned. It can raise the tariff of an established tax, too. On the other hand, the assessment that the state government imposes upon the people is not the whole of their income, but just a certain proportion of it, hence they still have enough to meet the rise of tariffs to some extent if necessitated by state finance. The state government may have recourse to a public loan or to brrowings at its option if need be. Such being the case, it is able to increase or decrease the revenue quite freely. Of course, it is natural in actual practice that there is a limit beyond which it should not attempt to do too much. And yet, fairly ample room is left over for it to increase or decrease the revenue. On the contrary, however, it is the case with local government that the sphere of its influence is pretty small, the resources derivable therefrom are limited (and this limits local government before everything) and moreover the categories of taxes and the rates are regulated by state-stipulated laws. In addition to that, even the floating of a public loan may require the permission of the state government each occasion, and it is not easy for the local government to avail itself of a public loan because of its small credit. Therefore, there is a difference in the degree of elasticity of revenue between state and local finances. It is not easy for local govenment to increase the revenue in case of emergency, and so, state government usually takes an expedient means to extend a helping hand to local government when the latter is really in needy circumstances. Of course, there is a practical limit of the financial power beyond which the state government cannot meet even its own need. But if one compares the state with the local government, he must find that there is a great difference in the relative difficulty of increasing or decreasing the revenue of respective governments.

(C) Principles of Revenue

As for the state tax, the capacity principle is devotedly observed in order to maintain the impartial incidence, while as for the local tax, the benefit principle may be taken into consideration besides the above principle. Of course, it may be conceded that principles adopted by different states are not absolutely the same, and that taxes may be collected according to the capacity principle alone without distinction of state and local taxes. However, quite a number of scholars support that as for the local tax, the benefit principle must be incorporated, and actually not a few local governments follow the above opinion in their financial management. What is meant by this principle is that since there can be recognized a wide difference in the benefit each member of the local organization derives from the local administration, taxes must be imposed proportionately to the degree of difference. It also implies that unlike the state admidistration, the local administration is performed closely to the people, and therefore, it is possible to detect the degree of benefit the people derive therefrom and to impose taxes proportionatlely to that degree so that larger incidence may fall upon those who enjoy larger benefit. This, of course, does not mean that the benefit principle is the main principle of local taxation. As far as taxation is concerned, the capacity principle remains the major principle, and the said principle must be considered to some extent in addition. Now, admitting that the benefit principle is applied as a supplementary principle to the local taxation, it is usually advisable to choose land, house and business taxes as those to whch this principle suits the purpose best, and to add as the basis of assessment some external criterion to some extent.

(5) Relation of Revenue to Expenditure

As a matter of principle, three differences can be noticed in the relation between revenue and expenditure.

(A) Equilibrium Principle and Surplus Principle

In state finance, the equilibrium principle of revenue and expenditure (the principle to square revenue with expenditure) is observed, while in local finance, efforts are, of course, made to attain the same effect, but greater contrast is that the surplus principle (the principle to leave some surplus after expenditure is satisfied with revenue) is also taken into consideration and every effort is made to avoid deficiency even if surplus be made. It must be acknowledged, however, that local finance does not look to make surplus as much as private economy. As for private economy, it is obviously a virtue to strive to leave a surplus, and that as much as possible. But if the local finance labors for the equilibrium of revenue and expenditure alone, it will be pinched by hard times very badly (even if not as badly as private economy) should it meet some deficiency which is feasible to be produced unavoidably, and which might be disposed of fairly easily if it were the state government. In such a case, it is more difficult for it to rely upon a public loan for lack of its credit than for the state government if compared. Such being the case, caution must be taken against this, and in the execution of budget the appropriation should be made in such a manner as to expend as little as possible, thus making it possible to leave some surplus, which, if ever made, will be saved and put to good use so that it may be used to meet any future need as the occasion calls without recourse to the floating of a loan. Maybe it is not necessary for local finance to do the same as private economy which anticipates from the very beginning to create some surplus with which it builds a fortune and tries to improve its economic standing. Nevertheless, it is highly desirable for local finance to provide for the future and to strive always to produce as much surplus as possible in executing the budget so as to meet without difficulty any need which may otherwise call for a public loan.

(B) Principle of Controlling Income after Measuring Outgo, and Principle of Controlling Outgo after Measuring Income

In private economy, the principle of controlling the outgo after measuring the income must be observed. Here, the outgo is controlled within the limits of the income. Heavy expenses should not be made when the income is low. In this manner, the private economy strives for economic independence and improvement of its economic standing. On the other hand, in atate finance the necessary amount for expenditure is determined at first, and then the revenue sufficient enough to cover it will be raised. If a certain amount is found indispensable, the revenue sufficient enough to cover it must be raised by some way or other through every possible device and contrivance. Since the state administration is very important, it is quite natural to make such a shift. Besides, the expenditure of the state is, as was mentioned already, lacking in elasticity, and is hard to be curtailed while its revenue is very elastic and could be relatively easily reduced if the need is over or could be increased as occasion arises, and thus these operations become possible. But in local finance, however important the expenditure might be, it is not of such nature that could never be retrenched as is the case with the state finance, and to speak of its revenue, being restricted both legally and actually instead, it cannot be increased very easily. Such being the case, it must be conceded that local finance has to depend at first upon the principle of controlling the income after measuring the outgo like the state finance in formal respect, but at the same time it should also pay attention to the rule of private economy or the principle of controlling the outgo after measuring the income. Here, local finance adopts partly the principle of of private economy, and does not follow the principle of state finance alone. Thus you have seen that there was a difference between state and local finances in this respect.

(C) Allowances to be made for the Application of the Principle that the Ordinary Expenditure must be Covered by Ordinary Revenue while the Extraordinary Expenditure may be Met by Extraordinary Revenue

The principle concerning the relation of ordinary and extraordinary income and outgo is applicable to all economies no matter whether it is state finance, local finance or private economy. According to this principle, ordinary expenditure should not be met by extraordinary revenue but by ordinary revenue in any circumstance, whereas it is a common guide-post to all economies that extraordinary expenditure may be covered not by ordinary but by extraordinary revenue (typically by borrowing) although we have to notice that there is difference between three economies in the degree of how strictly this principle is applicable to each. That is, state finance is the only economy, indeed, to which this principle can be applied in the strict sense of the word. If it is state finance, it is not so difficult in these days to have recourse to borrowing, a form of extraordinary revenue, as occasion arises. So it is quite all right for it to meet the need by such extraordinary revenue as a public loan or borrowing. But if it is private economy, a simple application of this principle to it may imperil its economic independence and improvement. Here, borrowings are no light task in most cases. Property may be disposed of to tide over the pending difficulty, but it is feasible that it has little property to part with. Therefore, it is safer for private economy to contrive to disburse not only ordinary expenses but also extraordinary expenses out of ordinary receipts without recourse to extraordinary receipts. as much as possible. It is ideal if it is at all possible that all extraordinary expenses could be met by ordinary receipts alone. As for local finance, even though it does not go so far as private economy, you should not readily conclude that extraordinary expenditures may be covered by extraordinary revenue because here it is possible to rely upon borrowings. Still it should try to manage well to disburse extraordinary expenses out of ordinary revenue as much as possible. Most of those extraordinary expenses which may arise in ordinary circumstances are paid out of ordinary revenue while such a huge extraordinary expense as might be caused by a disaster may alone be covered by extraordinary revenue such as state subsidy or the borrowings from the finance section of the treasury under certain circumstances, or by some extraordinary revenue of more autonomous nature such as the borrowings from the outside or the market on its own credit or from depositories (banks) by dint of the power of the confederation of local organizations, or disposal by sale of government property should there be any permanent property of its own. Or it will make doubly sure that in anticipation of such occasions some amount of surplus is produced and saved annually through utmost economy in the execution of the budget, and is increased devotedly in ordinary time so as to be appropriated to the need when a heavy disaster necessitates an extraordinary disbursement.