Comprehensive Urban Studies No.71 2000

# Globalization of Local Public Finance in Japan

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## 1. Financing the Tokyo Metropolitan Government

Collapse of Japan's "Bubble Economy" by 1991 and prolonged depression since then have directly hit the budget of the Tokyo Metropolitan Government (TMG). The major revenue source of TMG is metropolitan taxes, which account for nearly two-thirds (65.5% in 1997) of its general account budget. Of the metropolitan taxes, taxes imposed on corporations (corporation inhabitant tax and corporation enterprise tax) are important revenue sources but their amounts are affected by changing business conditions. In 1989, the year when the bubble peaked, the total amount of these two corporation-related taxes reached 2,680.1 billion yen, accounting for 56.1% of TMG's tax revenue. By 1998 however, that amount dropped to 1,627.7 billion yen, or to only 38.2% of the total tax revenue. Accordingly TMG's total amount of tax revenue decreased from 4,849.4 billion yen in 1991 to 3,860.1 billion yen in 1994 and continued on to either decline or showing little increase.

Contrary to this trend of tax revenue decline, basic financial needs continued to grow. One factor contributing to this increase is "graying" of Tokyo. The proportion of senior citizens aged 65 and over to the total population is rapidly increasing from only 4.0% in 1962 to 13.3% in 1996. It is expected to reach 25.2% by 2025.

Another factor is a rising unemployment caused by prolonged recession (rate of unemployment in Tokyo was 3.1% in 1990, 4.9% in1995 and estimated 5.6% in the mid 1999) and increasing corporate bankruptcies (2,876 cases in 1996 and 3,406 cases in 1998). As the employment system of Japanese corporations has been based on life-long employment and seniority system, it is almost impossible for middle-aged workers to get new jobs once they are fired.

These factors have urged TMG to increase various kinds of social welfare programs including construction of homes for senior citizens and shelters for homeless people.

In addition, the central government encouraged (or say rather forced) local governments to increase their public works spending to stimulate regional economies. The rationale was, "Don't worry about the financial resource for issuing local bonds. We the central government will pay for the necessary expenditure (payment of interest and principal redemption) by supplying additional Local Allocation Tax (LAT)". LAT is a fund reserved to secure equitable distribution of financial resources among local governments, and to guarantee execution of nationally standardized administration even by "poorer" governments (both prefectures and municipalities). At present a certain

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percentage of national tax revenues (32.0-32.5% of personal and corporate income tax and liquor tax; 24% of consumption tax; and 25% of tobacco tax) are earmarked for this fund.

The LAT system was started in 1950 based on recommendations made a year earlier by a group of American tax experts led by Professor Carl Sumner Shoup of Columbia University ("Shoup mission"). The system continued to expand and at present all prefectures, except TMG, have come to receive a fair amount of LAT.

TMG has not been entitled to receive LAT as the central government has long regarded it a "rich" local government where headquaters of large corporations have concentrated. So long as Japan could enjoy high economic growth, this arrangement of not granting LAT worked fine for Tokyo. Because of rapidly shrinking tax revenue mentioned earlier however, TMG, who cannot cover the shortage by LAT, was forced to issue additional bonds to cover expanding public works expenditure.

During the boom period, TMG did accumulate some reserve funds for rainy days, but after exhausting them it kept issuing metropolitan bonds every year to cover deficits. Table 1 shows "Outstanding Amount of Metropolitan Bonds" from 1983 to 1997. The rate of increase was low until 1992 (total annual increase of a little over 0.1 trillion yen in the first six years, and a little over annual 0.3 trillion yen in the next three-year period). However, since 1992 until 1997, that pace accelerated to record a one-trillion-yen increase in a single year.

Table 1 also shows the underwriters of inflating metropolitan bonds. The Trust Fund Bureau is a government fund consisting of the deposits of Postal Savings Account, Employees' and People's Pension and others which will be explained later. "Finance Corp. for Public Enterprises" in Table 2 is also considered a part of government fund. Private financial institutions have had confidence in

Table 1 Outstanding Amount of Metropolitan Bonds

(in billion yen, %; at the end of fiscal year)

| | 1983(S58) | 89(H.1) | 92(H.4) | 93(H.5) | 94(H.6) | 95(H.7) | 96(H.8) | 97(H.9) |
|---|---|---|---|---|---|---|---|---|
| Total | 5,9523 | 6,6093 | 7,773.1 | 8,966.1 | 9,897.8 | 10,970.9 | 11,612.7 | 12,112.1 |
| | (100.0) | (100.0) | (100.0) | (100.0) | (100.0) | (100.0) | (100.0) | (100.0) |
| by Loaner | | | | | | | | |
| Trust Fund | 1,122.9 | 1,593.1 | 1,720.2 | 1,972.2 | 2,007.9 | 2,572.4 | 2,689.6 | 2,741.8 |
| Bureau | (16.8) | (24.1) | (22.1) | (22.0) | (20.3) | (23.5) | (23.2) | (22.6) |
| Public Sub- | 1,927.5 | 2,624.4 | 2,770.1 | 2,928.4 | 3,205.0 | 3,489.8 | 3,737.2 | 3,985.4 |
| scription | (32.4) | (39.7) | (35.8) | (32.7) | (32.4) | (31.8) | (32.2) | (32.9) |
| City Banks | 2,376.5 | 1,429.6 | 2,028.3 | 2,863.0 | 3,468.6 | 4,032.4 | 4,319.7 | 4,500.1 |
| | (39.9) | (21.7 ) | (26.2) | (31.9) | (36.8) | (36.8) | (37.2) | (37.2) |
| Others | — | — | — | — | — | — | — | — |
| Average interest rate(%) | 7.56 | 6.39 | 5.87 | 5.49 | 5.27 | 4.90 | 4.64 | 4.40 |

Note: (1) The total includes a small amount of short term bonds in addition to the items listed.
(2) 1 billion yen = roughly US$ 9.5 million S: Showa H: Heisei
(3) Others include Postal Life Insurance, Finance Corp. for Public Enterprises, Mutual Aid Society.
(4) Average interest rate for metropolitan bonds
(5) sources"Tosei Yoran"(Tokyo Statistical Yearbook)

TMG's financial power that major lenders (almost three-fourths) include city banks, insurance companies, and Employees' Mutual Aid Society. It should be noted that the average interest rate of metropolitan bonds was very high before the 1990s (7.56% in 1980 and 6.39% in 1989). Consequently, there will be a heavy financial burden of interest payment for the bonds maturing between 2010 and 2020.

Before finding an answer to question whether TMG can continue on its deficit finance by bond issuance, we shall first examine the financial condition of other municipal governments.

## 2. Local Public Finance is Falling into Debt

### (a)Municipal bonds

As of the end of March 1998, Japan had in total 3,232 municipalities (670 cities and 2,562 towns/ villages). Table 2 shows the outstanding amount of municipal bonds. Generally speaking, their financial power and credibility in the country's public loan market is not so strong like TMG, and have to depend heavily on government funds (e.g. Trust Fund Bureau and Postal Life Insurance), and the Japan Finance Corporation for Municipal Enterprises (Finance Corp. for Public Enterprises in Table 2). This corporation is empowered to issue bond to furnish long-term (usually 20 to 28 years) loans for local public enterprises such as water supply and sewage works, urban transportation facilities,and others.

The outstanding amount of municipal bonds totaled 54,089.3 billion yen at the end of March 1998 (the end of fiscal year 1997). As Table 2 shows, until 1990 this outstanding amount increased around one trillion yen annually, but since then, between 2 to 4 trillion yen every year. Since the Japan Finance Corporation for Municipal Enterprises is a government organization, the national

Table 2 Outstanding Amount of Municipal Bonds and Their Loaners

(in billion yen)

| | 1988(S63) | 89(H.1) | 90(H.2) | 91(H.3) | 92(H.4) | 93(H.5) | 94(H.6) | 95(H.7) | 96(H.8) |
|---|---|---|---|---|---|---|---|---|---|
| Total | 26,256.6 | 27,248.5 | 28,606.4 | 30,461.2 | 33,382.8 | 36,843.1 | 41,071.8 | 46.360.0 | 50,981.9 |
| by Loaner | | | | | | | | | |
| 1. Government | 17,728.0 | 18,187.0 | 18,698.1 | 19,339.9 | 20,421.2 | 21,915.9 | 24,141.6 | 26 857.9 | 29,274.1 |
| Funds | (67.5) | (66.7) | (65.4) | (63.5) | (61.4) | (59.5) | (58.7) | (57.9) | (57.4) |
| a) Trust Fund | 10,792.5 | 10,991.0 | 11,258.1 | 11,664.2 | 12,539.1 | 13,843.0 | 15,793.2 | 18,267.9 | 20,521.9 |
| Bureau | (41.1) | (40.3) | (39.4) | (38.3) | (37.6) | (37.6) | (38.5) | (39.4) | (40.3) |
| b) Postal | 6,933.5 | 7,196.0 | 7,440.0 | 7,675.7 | 7,882.1 | 8,072.9 | 8,348.4 | 8.589.9 | 8,752.2 |
| Insurance | (26.4) | (26.4) | (26.0) | (25.2) | (23.7) | (21.9) | (20.3) | (18.5) | (17.2) |
| 2. Financial Corp. | | | | | | | | | |
| for Public | 2,253.5 | 2,310.1 | 2,327.9 | 2,389.1 | 2,624.1 | 2,954.8 | 3,195.1 | 3,534.6 | 3,951.0 |
| Enterprises | (11.7) | (8.5) | (8.1) | (7.8) | (7.9) | (8.0) | (7.8) | (7.6) | (7.7) |
| 3. City Banks | 2,852.6 | 3,006.2 | 3,360.7 | 3,970.4 | 5,486.9 | 6,555.2 | 7,990.7 | 9,444.6 | 10,562.0 |
| | (10.9) | (11.0) | (11.7) | (13.0) | (16.4) | (17.8) | (19.4) | (20.4) | (20.7) |
| 4. Public | 967.3 | 1,015.0 | 1,070.3 | 1,142.0 | 1,256.5 | 1,415.9 | 1,647.4 | 1,955.0 | 2,248.6 |
| Subscription | (3.7) | (3.7) | (3.7) | (3.7) | (3.8) | (3.8) | (4.0) | (4.2) | (4.4) |

Note: Total include others.

Source: "Chihô Zaisei Tôkei Nempô"(Annual Statistics on Local Public Finance) government has actually paid for almost two-thirds of this outstanding amount.

### (b) Prefectural bonds

Local governments of Japan consist of municipalities and 47 prefectures (including TMG), and the total outstanding amount of bonds issued by both municipalities and prefectures can be seen in Table 3. Again we see that a major part (51.2% in 1997) has been financed by the national government (undertaken by funds of the government and the Japan Finance Corporation for Municipal Enterprises). This outstanding amount has more than doubled within the past 8 years, from 50.0 trillion yen in 1988 to 111.5 trillion yen in 1997. The sharp increase tells that the local public finance is falling into debt.

Table 3 Outstanding Amount of Local Bonds and Their Loaners

(in billion yen)

| | 1988(S63) | 89(H.1) | 90(H.2) | 91(H.3) | 92(H.4) | 93(H.5) | 94(H.6) | 95(H.7) | 96(H.8) | 97(H.9) |
|---|---|---|---|---|---|---|---|---|---|---|
| Total | 50,042.6 | 52,300.8 | 55,098.1 | 58,689.9 | 65,045.2 | 72,304.2 | 80,461.2 | 94.447.0 | 104,916.6 | 111,496.4 |
| by Loaners | | | | | | | | | | |
| 1. Government | 26,537.3 | 27,784.8 | 29,997.0 | 30,339.4 | 32,508.0 | 35,494.8 | 38,331.4 | 43,447.0 | 47,646.8 | 49,722.5 |
| Funds | (53.0) | (53.1) | (52.6) | (51.7) | (50.0) | (50.4) | (47.6) | (46.1) | (45.4) | (44.6) |
| a) Trust Fund | 18,580.7 | 19,473.5 | 20,363.6 | 21,404.4 | 23,276.8 | 26,003.0 | 28,489.9 | 32,971.7 | 36,718.5 | 38,715.0 |
| Bureau | (37.1) | (37.2) | (37.0) | (36.5) | (35.8) | (36.9) | (35.4) | (35.0) | (35.0) | (34.7) |
| b) Postal Life | 7,956.7 | 8,311.3 | 8,633.4 | 8,935.0 | 9,231.2 | 9,491.7 | 9,841.5 | 10.475.2 | 10,928.3 | 11,007.5 |
| Insurance | (15.9) | (15.9) | (15.7) | (15.2) | (14.2) | (13.5) | (12.2) | (11.1) | (10.4) | (9.9) |
| 2. Japan Finance | 3,876.3 | 3,990.4 | 4,089.0 | 4,215.0 | 4,641.4 | 5,197.0 | 5,500.1 | 6,057.9 | 6,779.0 | 7,342.2 |
| Co. | (7.7) | (7.6) | (7.4) | (7.2) | (7.1) | (7.4) | (6.8) | (6.5) | (6.6) | (6.6) |
| 3. City Bank | 10,451.5 | 10,208.1 | 10,363.5 | 11,032.5 | 13,741.9 | 18,204.1 | 23,267.7 | 289,966.3 | 33,060.8 | 36,085.1 |
| | (20.9) | (19.5) | (18.8) | (18.8) | (21.1) | (25.8) | (28.9) | (31.2) | (32.0) | (32.4) |
| 4. Public | 3,790.4 | 3,951.9 | 4,128.3 | 4,297.1 | 4,714.6 | 5,287.6 | 6,255.2 | 7,245.6 | 8,184.5 | 9,067.5 |
| Subscription | (7.6) | (7.6) | (7.5) | (7.37) | (7.2) | (7.5) | (7.7) | (7.8) | (7.9) | (8.1) |

Note: Total include(5) others. As for others, refer to Table 1 and 2 its note (3);
Municipal Bonds exclude those of Special Ward (ku) in Tokyo.
Source: Ministry of Local Affairs "Chihô Zaisei Tôkei Nempô"
( Statistical Data of Local Public Finance)

### (c) The overall picture of local debts

The 1999 version of "The White Paper on Local Public Finance" published by the Ministry of Home Affairs warned the trend of increasing local debt (Chapter 1, Section 2 "Future Financial Burden"). It explains that the total amount of local debt is not equal to that of local bonds but in addition includes debts related: i) LAT's borrowed money from the national government's Trust Fund Bureau; ii) contract authorization (official premise for future payment); iii) deficit financing of local public corporations (Chiho Kosha); and iv) the so-called "third sector companies (Third Sector)".

i)LAT's borrowed money

The first item, or LAT's borrowed money from the national government's Trust Fund Bureau, is shown in Table 4 ("Net Debt of Local Governments"). As explained before, the national government encouraged local governments to increase their public works spending by promising to sup-

Table 4 Net Debt of Local Governments

(Ordinary Account ; in trillion -1,000 billion-yen)

| | 1990 | 1991 | 1992 | 1993 | 1994 | 1996 | 1997 |
|---|---|---|---|---|---|---|---|
| (1) Outstanding Amount of local bonds | 52.2 | 54.9 | 61.1 | 70.5 | 80.5 | 103.3 | 111.5 |
| (2) LAT* Account borrowed from FILP** | 1.5 | 0.7 | 2.2 | 3.8 | 7.4 | 14.4 | 15.2 |
| (3) Public enterprise debt (covered by the ordinary account) | 13.3 | 14.4 | 15.8 | 17.0 | 18.4 | 21.4 | 23.0 |
| Total*** | 67.0 | 70.0 | 79.1 | 91.3 | 106.3 | 139.3 | 150.0 |

*LAT: Local Allocation Tax or national equalization fund

**FILT: the Fiscal Investment and Loan Program

***In addition to the total given here, there are debts related to public enterprises and third sector companies

Source of the "Total" : Chihou Zaisei no Joukyou 1999(Conditions of local finance), Ministry of Home Affairs

port their financing with additional LAT. The amount of LAT account however has become too small to supply the necessary fund which forced the national government and obliged to borrow from the Trust Fund Bureau. It is expected that the amount of this borrowed money may reach 30.03 trillion yen at the end of fiscal year 1999.

ii) Contract Authorization

In addition to debt shown in Table 4, we must add items ii) to iv) listed above (i.e. Contract Authorization with 17.3 trillion yen debt at the end of fiscal year 1997, "Chiho Kosha" and "Third Sectors".) plus local public enterprises debt not covered by the ordinary account (29.4 trillion yen in 1997) and loan by the Japan Finance Corporation for Municipal Enterprises (the gross amount of 29.0 trillion yen in 1997).

iii) Chihô Kôsha

Following the example of "public or government corporation" in the U.S., local governments in Japan introduced this system in the mid-1960s by investing their necessary capital, and hiring employees who were treated as semi-government officials. Based on three acts, local governments set up three kinds of local public corporations under the name "Chihô Kôsha" since the 1970s for supplying or developing (1) local public housing,(2) local public road and (3) public land . At first local governments invested 100% of their capital, but later certain amount of private (such as bank, utility or railway company) money was introduced. As of the beginning of 1996, the number of Chihô Kôsha to which local governments invested 100% of their capital was 4,125 (770 by prefectures, 219 by designated cities -- major cities with population more than 1 million and were allowed a certain extent of autonomy, and 3,136 municipalities ). In addition, there were 5,219 Kôshas financed partly by private money.

iv) The "Third Sector"

Since the mid-1980s, the Japanese economy enjoyed high rate of economic expansion ( called the stage of "Bubble Economy") and local governments themselves tried to expand their activities efficiently (or say rather speculatively) by inviting private capital and civilian know-how. Thus they set up semi-public corporations under the name of the "3rd Sectors." After the promulgation of "Comprehensive Law to Arrange Health Resort Areas" in 1987, many Third Sectors engaged in regional development works in holiday resort areas, and we find many Third Sector type hotels accessible by scenic railways or sightseeing roads across the country. Also because of deficit financing of the national railway system (the system was privatized in 1987 with 25.5-trillion-yen accumulated deficit and this amount with interest eventually reached to 28 trillion yen without paying out), many local railways in depopulated area went bankrupt and they were transferred to the Third Sectors with financial support from local governments and regional private corporations.

After Japan's Bubble Economy burst at the beginning of the 1990s, many Third Sectors have gone into the red. One example --both City and Prefecture of Miyazaki (located in southern Kyushu) jointly established the Phoenix Resort Company (PRC) with 300 million yen capital (each government invested 25% of this capital and the remaining amount was financed by the Dai-ichi Kangyo Bank and other private regional enterprises). This PRC constructed a 43 -floor high-rise beautiful hotel with 750 rooms and many amusement facilities in the 135-hectare (almost 340 acres) pine forest. The PRC as well as the City and the Prefecture expected to have 5.5 million annual visitors. While the construction works were going on, the general economic condition worsened and, after its opening in 1994, the hotel had only 3.0 million visitors annually which caused 20-billion-yen deficit. PRC's accumulated debt including the construction cost has now reached 260 billion yen. In 1999 Miyazaki Prefecture decided to spend 6 billion yen out of its budget to cover the deficit, but what should be done for the remaining deficit?

On Dec.28, 1999 Ministry of Local Affairs reported that the total number of the "Third Sectors" was 8,395 and, as of July 1st of that year, out of 3,475 set up to do businesses, 1,436 (41.3% of total) were in the red with a total loss of 220.6 billion yen. Of these deficit-operating sectors 33.6% engage in sightseeing or leisure business, 14.2% in agricultural special home product, 12.2% in transportation and 7.6% in regional or urban development. The Ministry warns that, since many local governments guaranteed financing to these Third Sectors, they should have some responsibility in case any of them go bankrupt.

## 3. Trust Fund Bureau and Postal Savings System

As Table 3 shows, the major sources of financing local bonds are "Funds of Trust Fund Bureau" and "Postal Life Insurance". In 1997 these two sources covered 44.6% of the outstanding amount of local bonds. Table 5 shows that the deposit of postal savings covers the major part of "Fund of the Trust Fund Bureau" (238.8trillion yen out of 418.3 trillion yen or 57.1% in 1997).

Post offices handle both postal savings and postal life insurance business in Japan. Compared with other countries, Japanese post offices are responsible for a surprisingly huge amount of saving money. Total 24,638 post offices (as of March 31, 1997) all over the country form the biggest financial institution in the world. There are, as we know, similar financial institutions such as "Sparkasse" in Germany or "Caisse d'Épargne" in France, but they are a kind of saving or thrift

Table 5 Deposits to Fund of the Trust Fund Bureau(Yokinbu Shikin)

in trillion(1,000 billion) yen

| | 1986(S.61) | 89(H.1) | 93(H.5) | 94(H.6) | 95(H.7) | 97(H.9) |
|---|---|---|---|---|---|---|
| (1) Postal savings | 101.3 | 131.3 | 181.5 | 195.2 | 211.6 | 238.8 |
| (2) Postal life Insurance & Annuity | 2.6 | 4.1 | 8.0 | 7.4 | 8.5 | 6.0 |
| (3) Employees' Pension | 50.3 | 67.7 | 96.7 | 103.0 | 107.4 | 124.0 |
| (4) People's Pension | 2.5 | 4.5 | 7.5 | 8.2 | 8.6 | 9.9 |
| (5) Total | 167.1 | 230.1 | 326.3 | 346.7 | 373.9 | 418.3 |

Note: "Total include other miscellaneous items.

Source: "Ministry of Finance Statistics Monthly" July 1999

institutions for promoting or supporting home ownership or purchasing consumer durable goods.

In Germany, "Postbank" has 14, 703 offices taking care of people's saving, but their deposited money is mainly used for information technology facilities.

Even a large bank can open maximum 400 or 500 branch offices, and those only in urbanized area. But one of 24,638 post offices over Japan are located in your neighborhood, wherever you live. It is quite easy for rural villagers to deposit their daily cash income in neighboring post office.

There is a historical background to this notable financial features of post office in Japan. In 1868 the new Meiji Emperor Government replaced the Tokugawa feudal regime to start modernization, and attached special importance to constructing and improving nationwide transportation and communication systems. In 1872 the national government constructed the country's first railway between Tokyo and Yokohama, set up a modern-style post office system almost in the same year and joined in the Universal Postal Union in 1877. The government appointed its officials to the head of regional higher-ranking post offices, but selected influential community leaders as heads of local (called the third class) post offices which were located even in small isolated islands.

In 1861 England opened the first postal saving system in the world, and Japan adopted this system in 1875. Since the Meiji Restoration, the goal of the national government was to catch up with advanced European countries by accumulating large amount of capital. This postal savings money served as an important financial source for its industrial and military development.

To encourage people to be thrift and diligent, the government advocated the campaign "Work harder and put your saved money in the neighboring post office". In unison with the government, masters of local post office shouted "No poverty can overtake industry. For your future happiness, save your money to put in post office. Your deposit will be guaranteed by our government". "Many a little makes a mickle" came true and the postal savings section of the Bureau of Communication (organized in 1878) collected farmers' and workers' daily cash income to build up a mighty public fund.

In 1885 this fund was transferred to "Yokinbu" (section of postal savings) of the Ministry of Finance. Before the 20th century, "Yokinbu" fund was used only to secure national bonds, but in 1907 that function was expanded to include loans to the general and special accounts and collateral for local bonds. In the late 1920s, the worldwide great depression spread to Japan and many corporations went into bankruptcy. Small savers (e.g. farmers, workers and owners of small enterprises) feared defaults by private banks. In spite of post office offering interest rates lower than those in the private sector, these savers put their money into postal savings account for security reason, which was then used by the government for industrial and military development.

After the 2nd World War ( in 1951), "Yokinbu" was reorgsanized and renamed "Trust Fund Bureau" (Shikin Unyoubu). Table 5 shows the deposits to this Fund of the Trust Fund Bureau, and Table 6 shows the Postal Savings Account. In Table 6, "Ordinary" is equivalent to a demand deposit of commercial banks while "Installment" means monthly fixed amount deposit (unit 1,000 yen). The rate of interest fluctuates based on market conditions. "Fixed" means deposits in postal savings for a fixed period (maximum ten years) at compound interest, and when they mature depositors receive the principal with interest on it. The rate of interest is fixed when initial deposits are made. Anyone who deposited money before 1990 when the interest rate was over 6% (see Table 1 column "Average interest rate" which is roughly the same as the rate applied to postal savings) could later expect to receive a significant amount of interest (Note: the average interest rate further declined to below 3% after 1989).

Table 6 Postal Saving Account (Deposited at the end of fiscal year)

(in trillion yen ; concluded)

| | 1984(S.59) | 88(S.63) | 92(H.4) | 93(H.5) | 95(H.7) | 97(H.9) |
|---|---|---|---|---|---|---|
| 1) Ordinary | 7.75 | 8.76 | 12.48 | 13.93 | 15.80 | 25.60 |
| 2) Installment | 0.81 | 0.78 | 0.81 | 0.86 | 0.85 | 0.76 |
| 3) Fixed | 84.31 | 116.33 | 156.78 | 168.74 | 180.93 | 214.17 |
| Total | 93.30 | 128.11 | 173.33 | 186.90 | 201.22 | 247.25 |

Note: Total includes others ; (Savings for home building, for children' education, etc.) S=Showa, H=Heisei
Source: Special issue on FILP in "Ministry of Finance Statistics Monthly" July 1999 (p.59)

## 4. Postal Savings Account in Crisis

Deposited amount of postal savings, guaranteed by the national government, increased to 254 trillion yen (around US$ 2,500 billion) in September 1999. The money served as "a mallet of luck" or "Santa Claus bag," and whenever politicians wanted to promote public works (highway, air port, bridge, dam...) in their constituencies, they could draw money out of this huge bag (officially taking the form of long-term borrowing money -- usually 20 to 40 years -- through "Ministry of Construction", "Ministry of Home Affairs",or other ministries).

However, new crisis is approaching this Postal Savings Account. In September 1990, people deposited large amount of money to postal savings – for a ten year period with fixed compound rate of 6.33% and they will mature in September 2000 amounting to total 58 trillion yen principal and interest. Similar amount was deposited with 6.0% fixed interest rate in July 1991 which will mature in July 2001 with total 48 trillion yen principal and interest.

Total 106 trillion yen (almost US$ 1,000 billion) will fall due within a year or so. After deducting 20% as interest tax imposed at the source, we expect (or fear) that roughly 81 trillion yen might be withdrawn from their postal savings.

Optimistic post offices expect around 70% of this 81 trillion yen may be redeposited to their savings. But would people be generous enough to redeposit such a huge amount of money to the post office again even with current interest rate, say 0.2% for a three year period? If you deposit 1 million yen at compound interest rate of 6%, you can receive 0.76 million yen of interest after ten years, but in case of 0.2%, you get only 0.016 million (16 thousand) yen within the same period.

If a half, or even one-third of postal deposited money is withdrawn from the postal savings account, there will be a tremendous impact on the country's local bond market.

## 5. Toward the Globalization of Local Public Finance

In order to solve the deficit financing of local public finance, we must search for the ways of "Globalization." From the viewpoint of international standard, we find it necessary to correct some of country's key systems as follows:

### (1) Easy Access to Local Bonds

As Table 2 and 3 show, the national government fund and banks undertake most of local bonds and very few individuals or foreign investors own them. If many people invest their saved money in local bonds or, as we see in many advanced countries, foreign investors buy our local bonds, the situation might be quite changed. However, we must solve several problems to achieve this goal.

### (2) Strengthen Local Autonomy by Decentralizing Financial Power

In 1997 net total amount of government expenditure (gross total of national general account plus those of local governments without duplications) was 148.7 trillion yen. Out of this total amount, national government net expenditure was 52.3 trillion yen (35.2%) and that of local governments was 96.4 trillion yen (64.8%). The local governments spend twice as much and thus work twice as much as the central government.

However, when we turn to taxes, fundamental independent revenue source of public administration, the national vs. local ratio reverses. Out of total 91.8 trillion yen tax paid, national taxes accounted for 60.6% or 55.6 trillion yen, while the rest, or 39.4% (36.2 trillion yen) was paid as local taxes. Thus local governments have to rely heavily on national financial support, in the form of transfers and grants, to execute their duties.

At present our national government is implementing a program to decentralize administrative functions. Even though many functions carried out by the national government are being transferred to local governments, financial resources are still being controlled at the central level. Local governments cannot handle larger amount of works and services without money and thus have to rely more on the national financial support.

We must admit the fact that Japan's local autonomous power is still weak and precarious. People do not pay much attention to local affairs and they are not accustomed to invest their saved money into local bonds. Similarly, Japan's local bonds are not a main target for foreign investors at present.

### (3) Globalization of Local Budgetary System

From now on Japan's local public finance should be fully understandable not only for domestic people, but also for international investors. International standards are being applied to our business accounting systems – from the ones based on acquisition price to market price and others. Similarly, our local budgetary system should introduce a form of balance sheet showing the whole picture of local government financial conditions. The existing system based on cash (not accrual) tells only a part of borrowed money and does not clarify assessed value of public facilities (fixed assets).The relation among different accounts --general, public enterprises, Chihô Kôsha and the Third Sector companies, and how much the total deficit a local government has, are not clear under the current annual financial reports. It might be necessary to introduce a concept of "consolidated balance sheet" to public finance. Just like "consolidated statement of shareholders' equity" published by private companies, local governments can prepare "consolidated statement of taxpayers' equity". These reports should also help foreign people, investors in particular, to get a clearer picture of Japan's local finance.

One item that has long been neglected in local public finance is "depreciation reserves." This is due to the historical background that most of public infrastructure and facilities in major cities (except ancient capital cities of Kyoto and Nara) were bombed and destroyed during the Second World War. Many of them were rebuilt during the period of high economic growth and there has been no or little need to worry about renewing or maintaining brand-new city halls, highways, bridges, sewer pipes or public concert halls.

However, many of these facilities and buildings have been used for over 30 years and a need to supply maintenance and repair costs for them is arising. The ordinary accounts of local public finance does have "Maintenance Cost" item whose amount occupies 1.1% of the total expenditure in 1997 but not "Depreciation Expenses." According to the Ministry of Local Affairs' "The White Paper on Local Public Finance", depreciation expenses are included in "Reserve Funds" together with local bonds sinking fund, retirement allowances and others, but the amount of Reserve Funds has decreased from 20.7 trillion yen in 1992 to 16.5 trillion yen in 1997.

We should introduce a global standard to our local budgetary system and in doing so the reports (based on Mr.Fudeya's Report) published by the following organizations might be suggestive:

International Federation of Accountants; Public Sector Committee
Governmental Accounting Standards Boards (U.S.)
Certified Institutes of Public Finance and Accountancy (U.K.)
Public Sector Accounting Standards Boards (Australia)
Accounting Research Standards Boards (New Zealand)
Canadian Institutes of Chartered Accountants (Canada)

At the same time our local finance experts should examine and develop methods to properly assess the value of public infrastructure, and to forecast interest rates to properly accumulate depreciation reserves, annuity and retirement allowances and others. By referring to reports published by the above institutes, we should make our local budgetary system a global one. At the same time, it is necessary for our local finance experts to discuss proper ways of assessing public road, a virgin forest or forecasting the interest rate in case of accumulating depreciation reserves, annuity and retirement allowances,etc.

### (4) Citizens' Participation in Local Affairs

The global budgetary system of our local public finance would make it easier for both community residents and foreign investors to better understand the local finance.

If more and better-to-understand information is provided, citizens will be more interested in, and will be willing to participate in local affairs. Local autonomy can only be strengthened through citizens' active involvement. It should be noted that efficient and competitive local government can only be created through a collective effort of the government itself and the citizens.