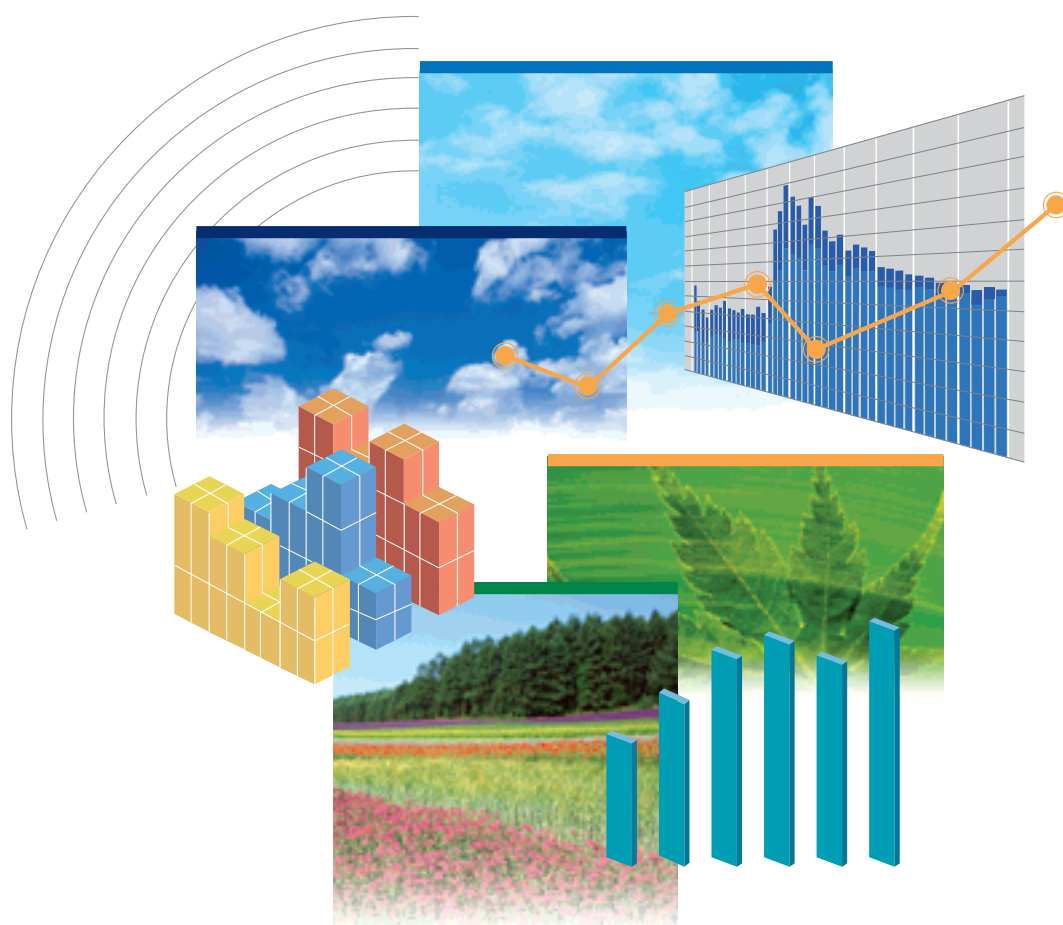


White Paper on Local Public Finance, 2005

Illustrated





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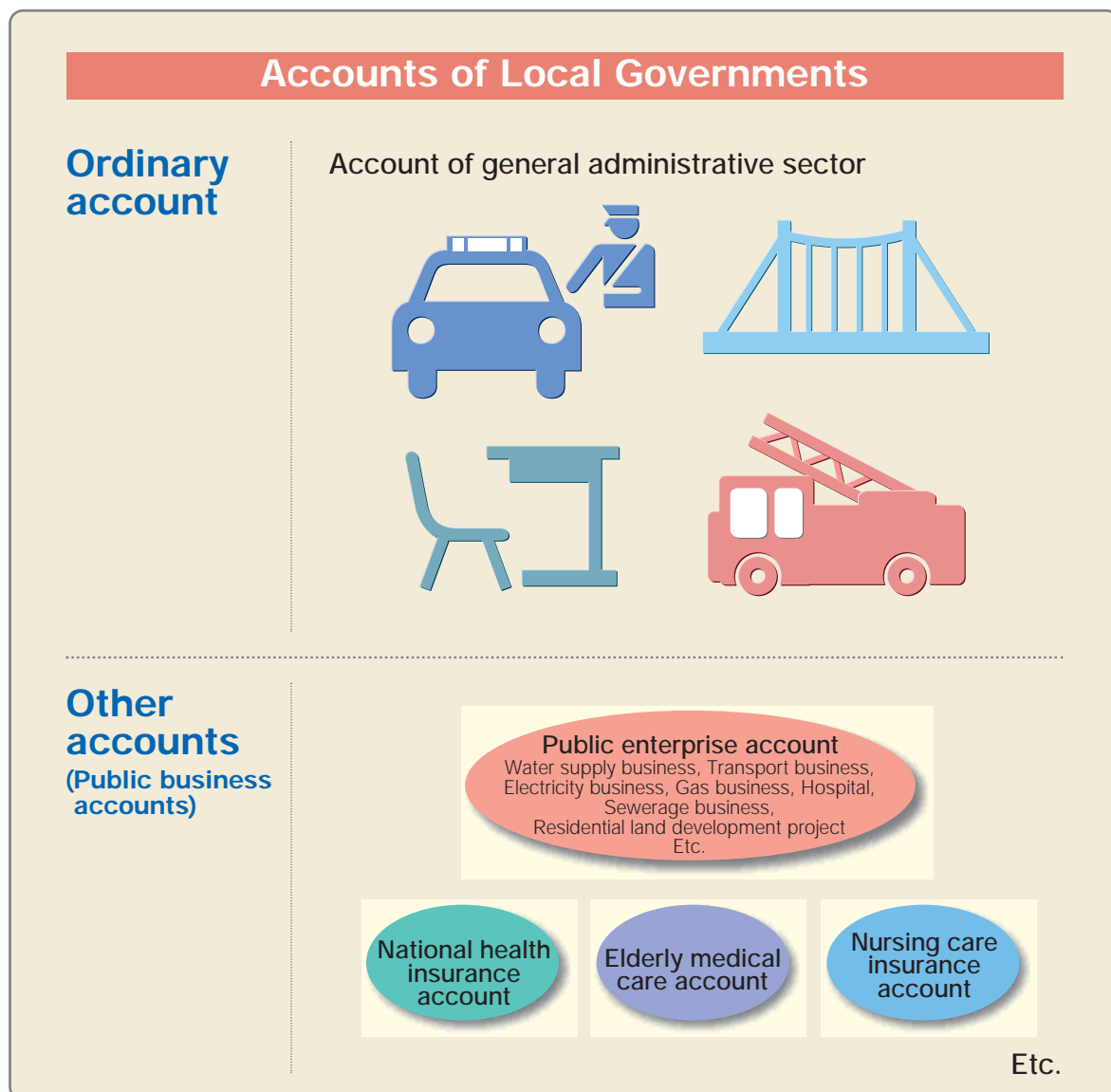
The Role of Local Public Finance

Prefectures and municipalities (cities, towns, and villages) are principal actors in various administrative areas, including school education, welfare and public health, police and fire services, and the construction of such public works as roads and sewerage systems. They play a major role in national life.

This brochure will introduce the state of local public finance, which is an assemblage of the finances of individual local governments, with particular focus on the state of settlements for fiscal 2003 and efforts toward financial soundness of the local public entities centered on the ordinary account.

Classification of the Accounting of Local Governments Applied in the Settlement Account Statistics

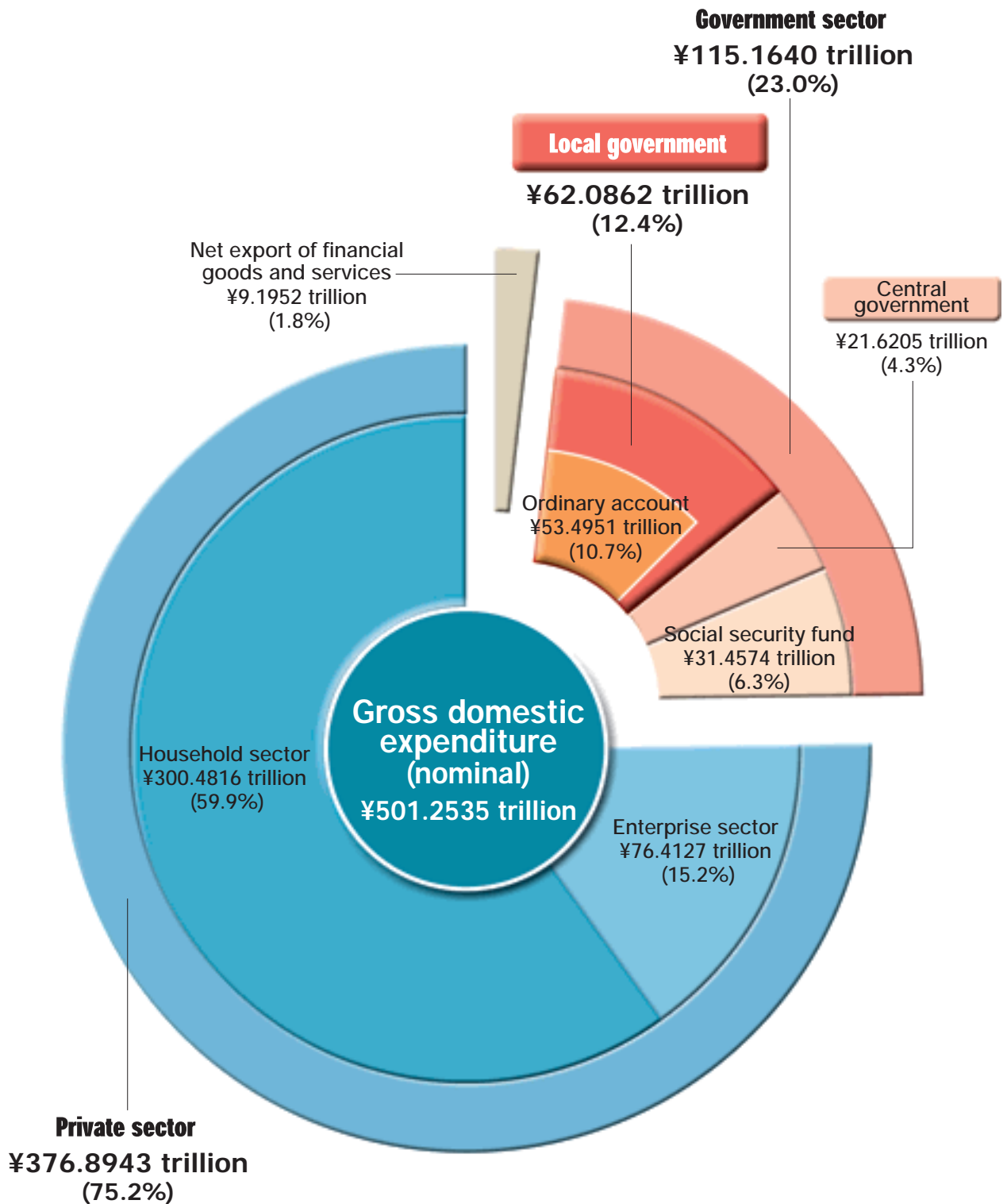
Although the accounts of local governments are divided into ordinary accounts and special accounts, the account classification of each local government is not uniform. Therefore, we have adopted a uniform method in the settlement account statistics by classifying accounts as an ordinary account, which covers the general administrative sector, and other accounts (public business accounts). This enables us to clarify the financial condition of local governments as a whole and to make a statistical comparison among local governments.



How large is local public finance compared with central government finance?

Looking at the scale of local public finance to gross domestic expenditure, we see that the ratio of the local government sector is 12.4%, which is about three times larger than the ratio of the central government.

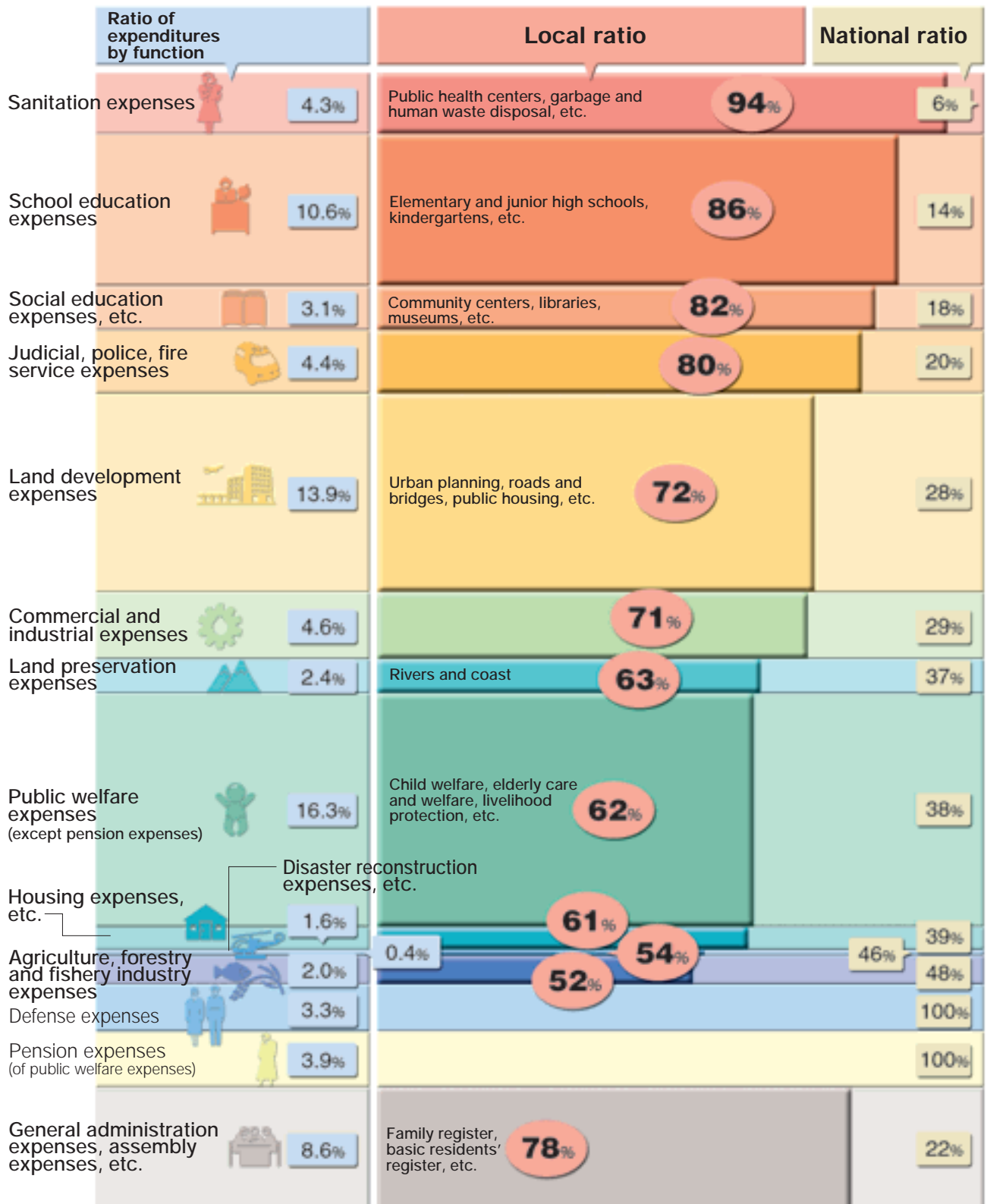
Gross Domestic Expenditure and Local Public Finance



In which fields are local expenditure ratios high?

Local expenditure ratios are higher in the areas that have a close relationship with our daily lives, such as public health and sanitation, school education, social education, and police and fire services.

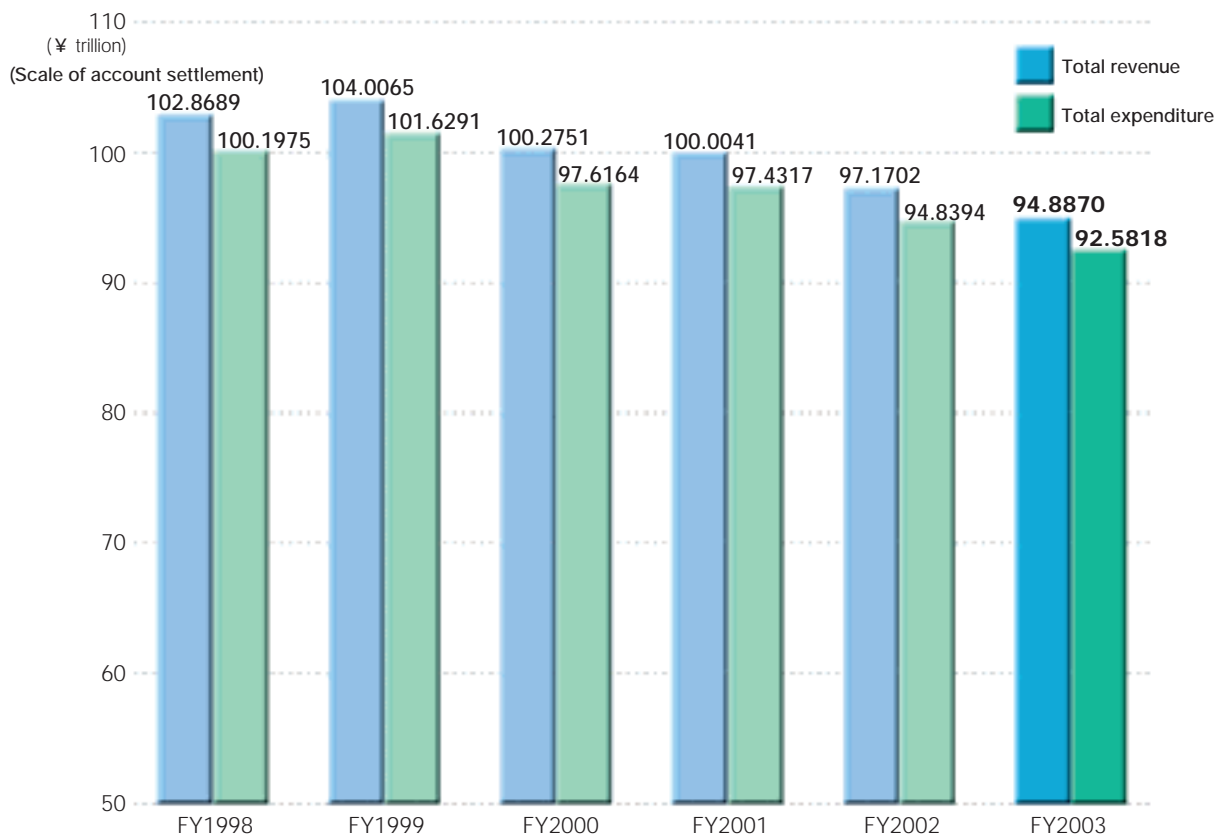
Shares of National and Local Governments in Main Expenditures by Function (final expenditure base)



The State of Local Public Finance (FY2003 Settlement)

Scale of Account Settlement

As a result of such factors as a decline in ordinary construction project spending and personnel expenses on the expenditure side and a decrease of local taxes and local allocation tax on the revenue side, both revenue and expenditure have shrunk for four consecutive years.



Revenue and Expenditure Settlement

Although both the single fiscal year balance and the real single fiscal year balance moved into the black, the number of local government bodies with a real balance deficit are increasing.

Category	Settlement figure		No. of deficit organizations	
	FY 2003	FY 2002	FY 2003	FY 2002
Real single FY balance	¥ 91.8 billion	- ¥ 97.8 billion	1,448 (2,435)	2,055 (2,932)
Single FY balance	¥ 139.7 billion	- ¥ 55.4 billion	1,347 (2,356)	1,949 (2,845)
Real balance	¥ 1204.6 billion	¥ 1078.3 billion	28	25

Notes:

- Real single FY balance:** Calculated by adding reserves to the fiscal adjustment fund and advanced redemption of local loans to the single FY balance and subtracting the used part of the fiscal adjustment fund.
Single FY balance: Calculated by subtracting the real balance of the previous fiscal year from the real balance of the fiscal year concerned.
Real balance: Calculated by subtracting the revenue resources that should be carried over to the next fiscal year from the income-expenditure balance.
- The number of organizations with real single FY balance deficits or single FY balance deficits does not include partial administrative associations and wide-area federations; the figures in parentheses are the number of organizations including partial administrative associations and wide-area federations.
- The number of organizations with a real balance deficit excludes entities with a deficit resulting from discontinued settlement (entities with no income or expenditure in the account settlement period because of a merger, etc.).

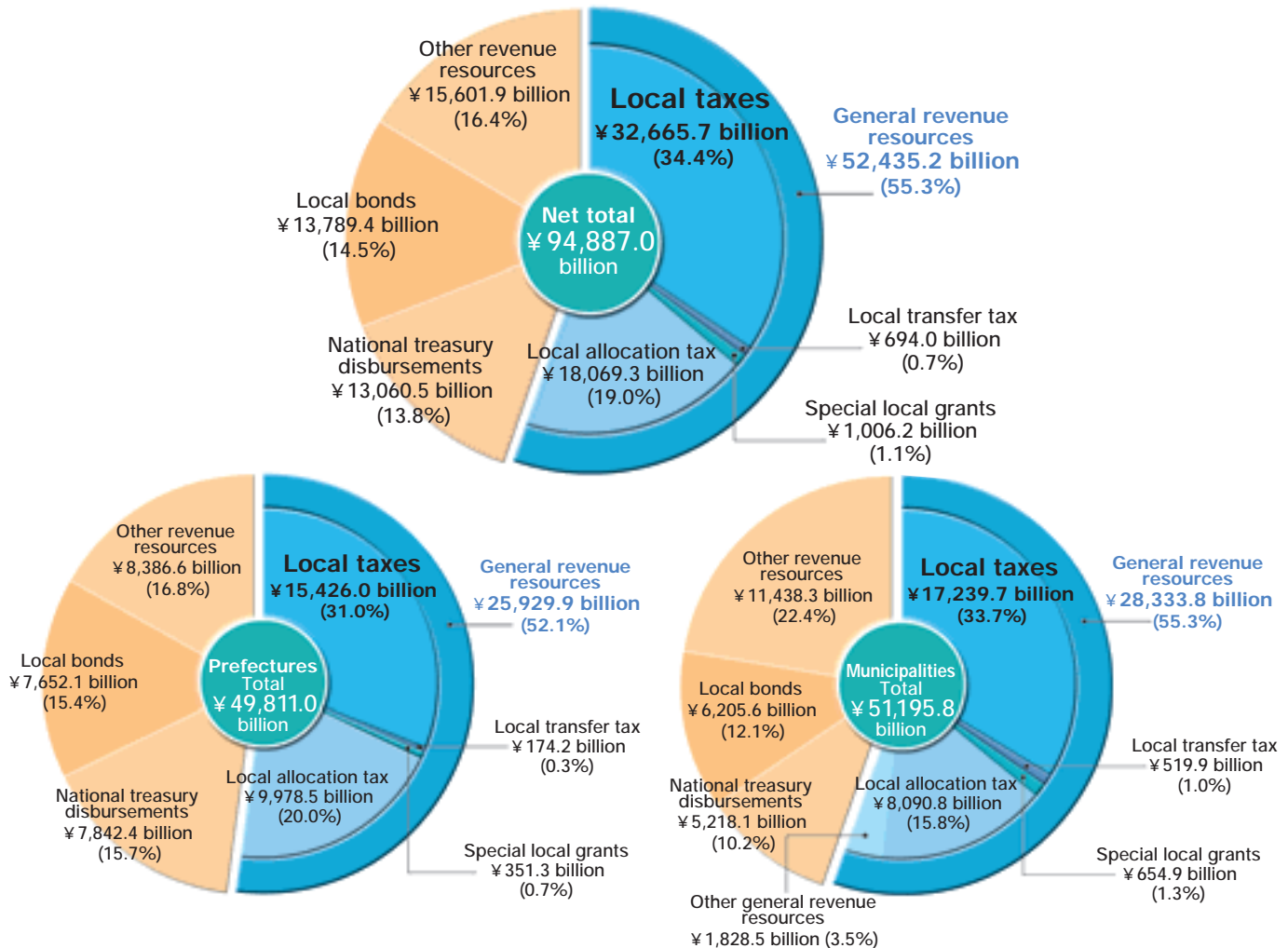
Revenue

Where does the funds for local government activities come from?

1 Revenue Breakdown

Local taxes account for about one-third of the revenue of local governments, followed by the local allocation tax, local bonds, and national treasury disbursements.

Revenue Breakdown (FY 2003)



General Revenue Resources

Revenue resources for which the use is not specified, like local taxes and the local allocation tax, are called general revenue resources. Here, the total of local taxes, local transfer tax, special local grants, the local allocation tax, and so on is treated as the general revenue resource. It is extremely important for local governments to ensure sufficient general revenue resources in order to handle various administrative needs properly.

Local transfer tax Collected as a national tax and transferred to local governments. Includes local road transfer tax, etc.

Special local grant A revenue source with the character of a substitute for local taxes, introduced to supplement a part of the decrease of local tax caused by a tax cut since FY 1999 and grants from the central government to local governments as a result of a revision of national treasury subsidies.

Local allocation tax An intrinsic revenue source shared by local governments in order to adjust imbalances in tax revenue among local governments and to guarantee revenue sources so that local governments in whatever region can provide a certain level of administrative services. Calculated as a certain ratio of five national taxes. (See page 9 for details.)

National treasury disbursements A general name for funds disbursed from the central government to local governments for specified uses.

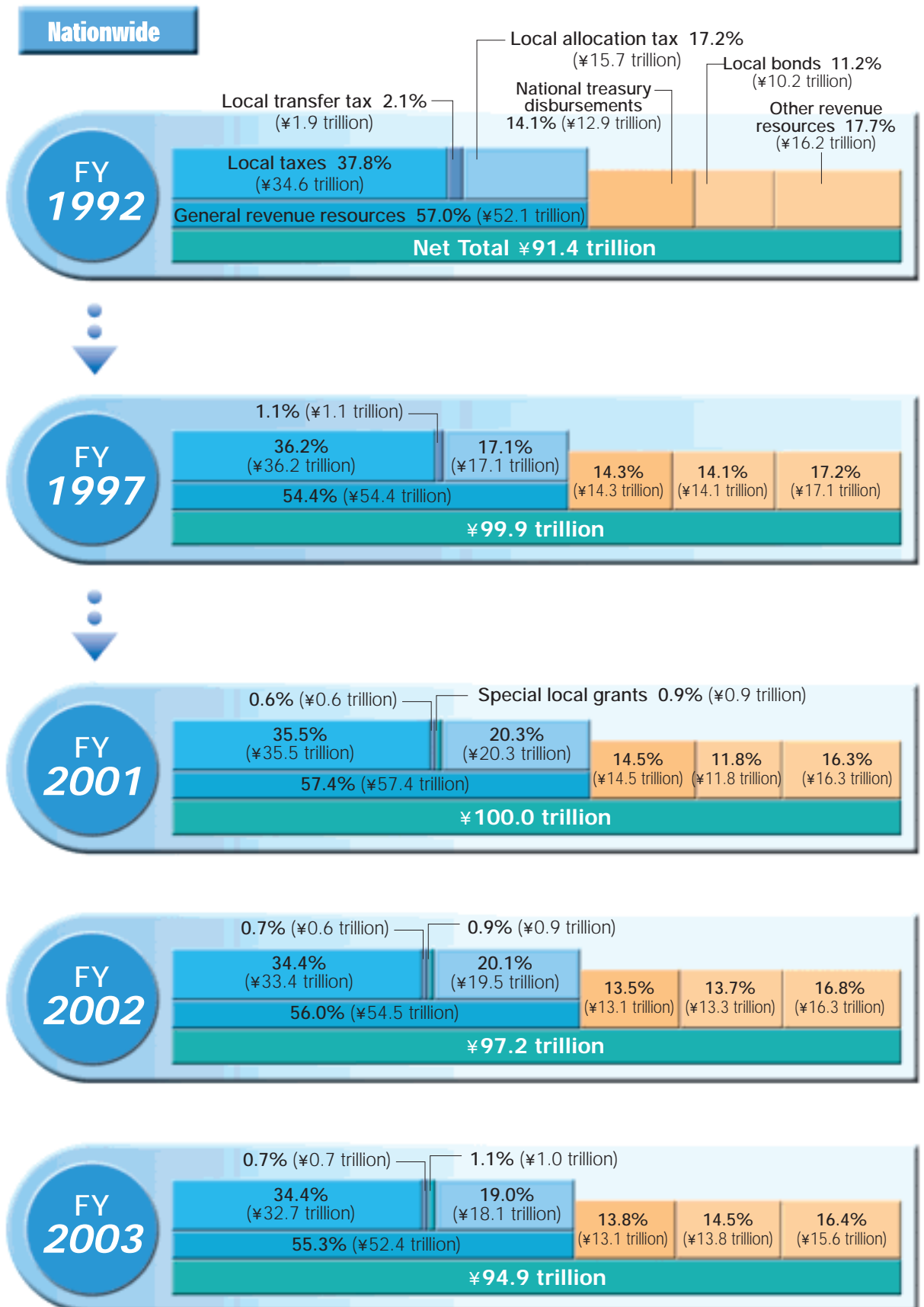
Local bonds These refer to the debts of local governments for which fulfillment continues for more than one fiscal year.

Notes:

1. The figures here are mainly for the ordinary account. (For the accounts of public enterprises, such as water supply and sewerage businesses, transportation businesses, and hospitals, see page 21.)
2. The figures for each item are rounded off under the given unit. Therefore, they do not necessarily add up exactly to the total.

2 Revenue Trends

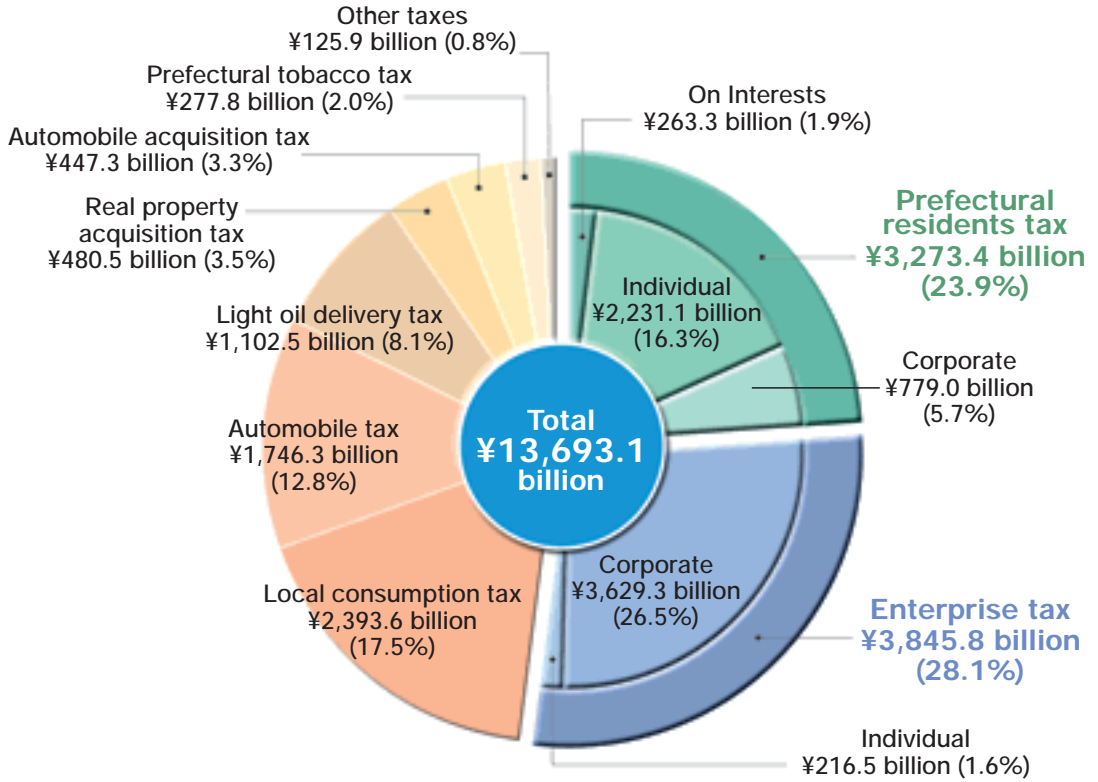
In recent years, while the ratios of local taxes and local allocation tax in total revenue are on a downward trend, the ratio of local bonds is increasing.



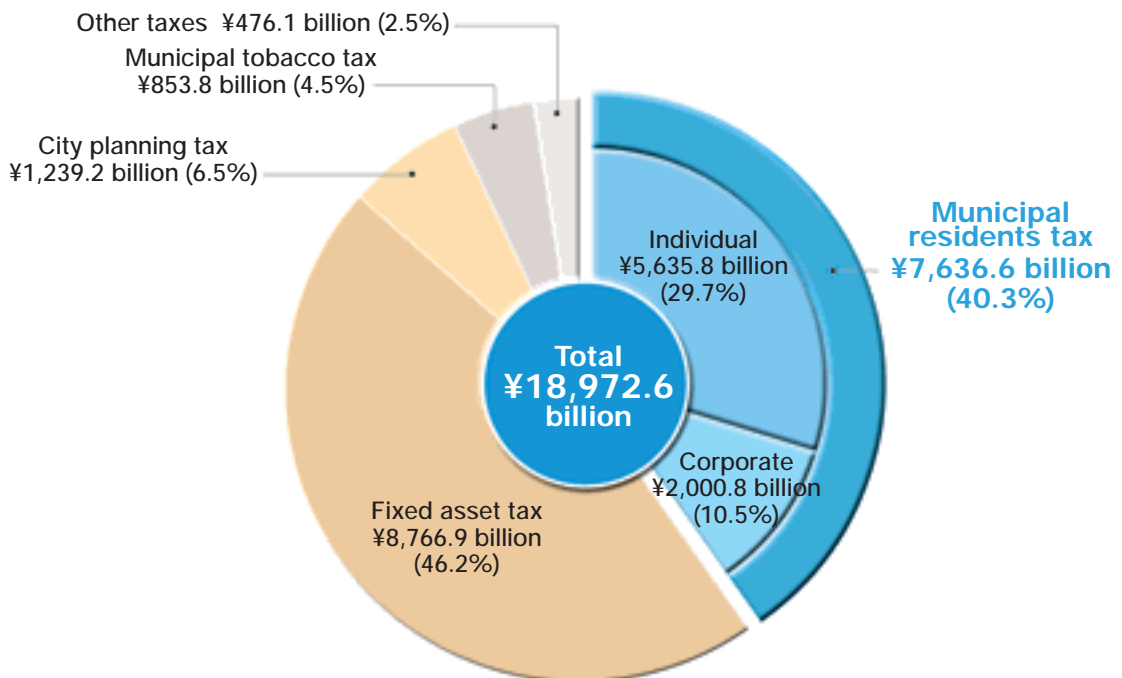
3 Local Taxes

Local taxes consist of prefectural taxes and municipal taxes. (In the case of the special wards of Tokyo, the Tokyo Metropolitan Government collects some municipal taxes.)

Composition of Revenue from Prefectural Taxes (FY 2003 settlement)



Composition of Revenue from Municipal Taxes (FY 2003 settlement)

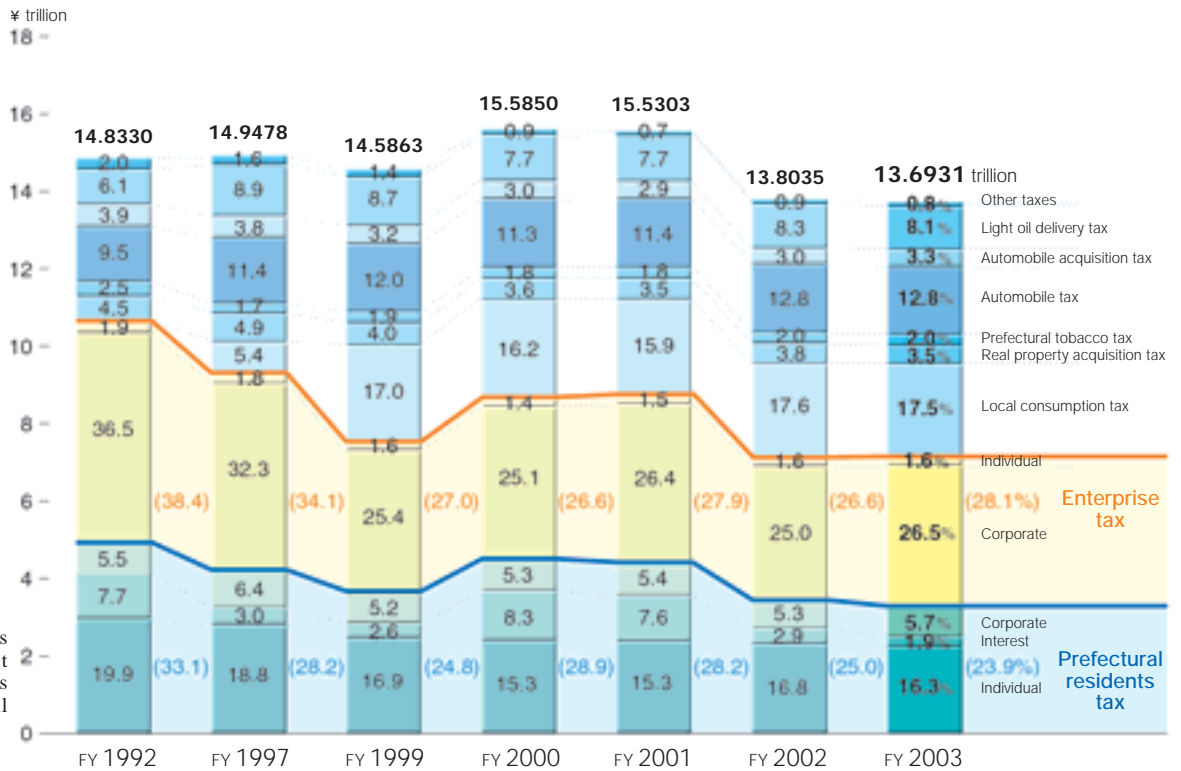


Among prefectural taxes, the ratios of the two corporate taxes (corporate business tax and corporate prefectural residents tax) are high. Among municipal taxes, the ratios of the fixed asset tax and individual municipal residents tax are high.

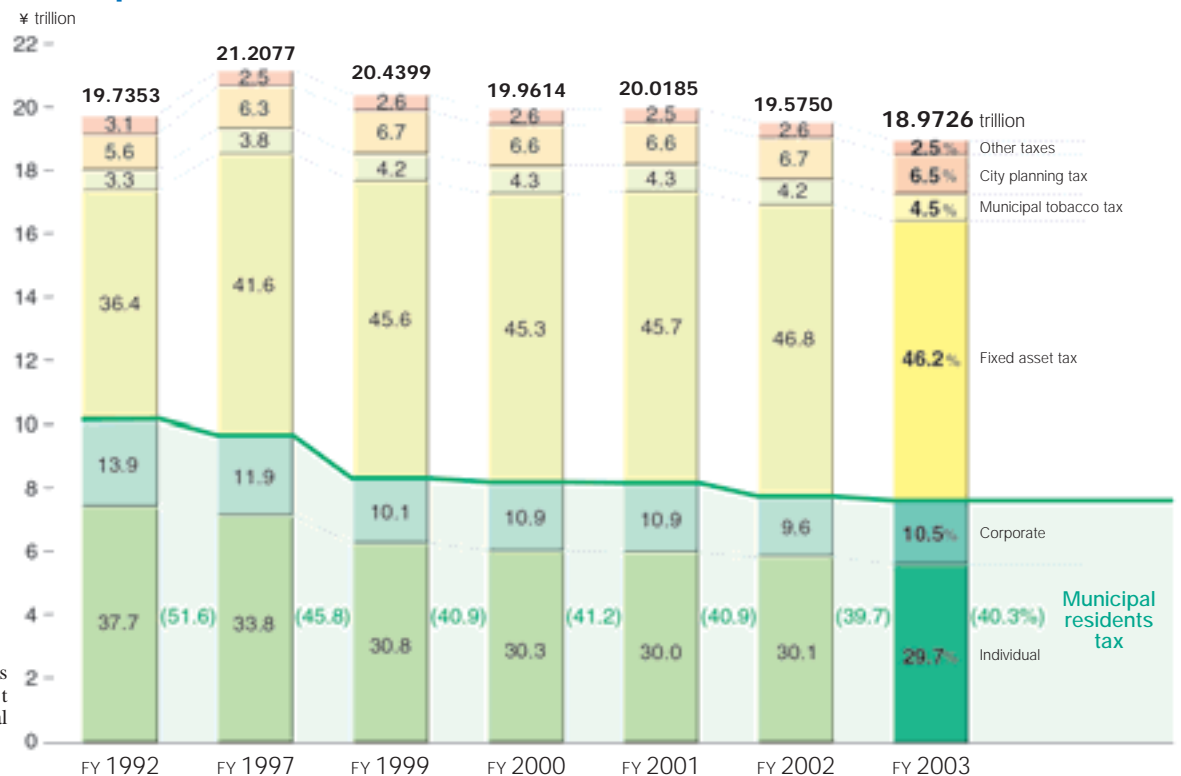
The two corporate taxes are impacted by the business cycle, so the tax revenue from prefectural taxes is less stable.

On the other hand, municipal tax revenue has been relatively stable, although it has been on a downward trend since fiscal 2001.

Prefectural Taxes Trend



Municipal Taxes Trend



4 Local Allocation Tax

From the perspective of local autonomy, it would essentially be the ideal for each local government to ensure the revenue sources necessary for administrative activities through local taxes collected from their residents. However, there are regional imbalances in tax revenue, and many local governments are unable to acquire necessary tax revenue. Therefore, the central government collects financial sources that should fundamentally be attributable to local tax revenue through national taxation and reallocates them as the local allocation tax to local governments where financial sources are insufficient.

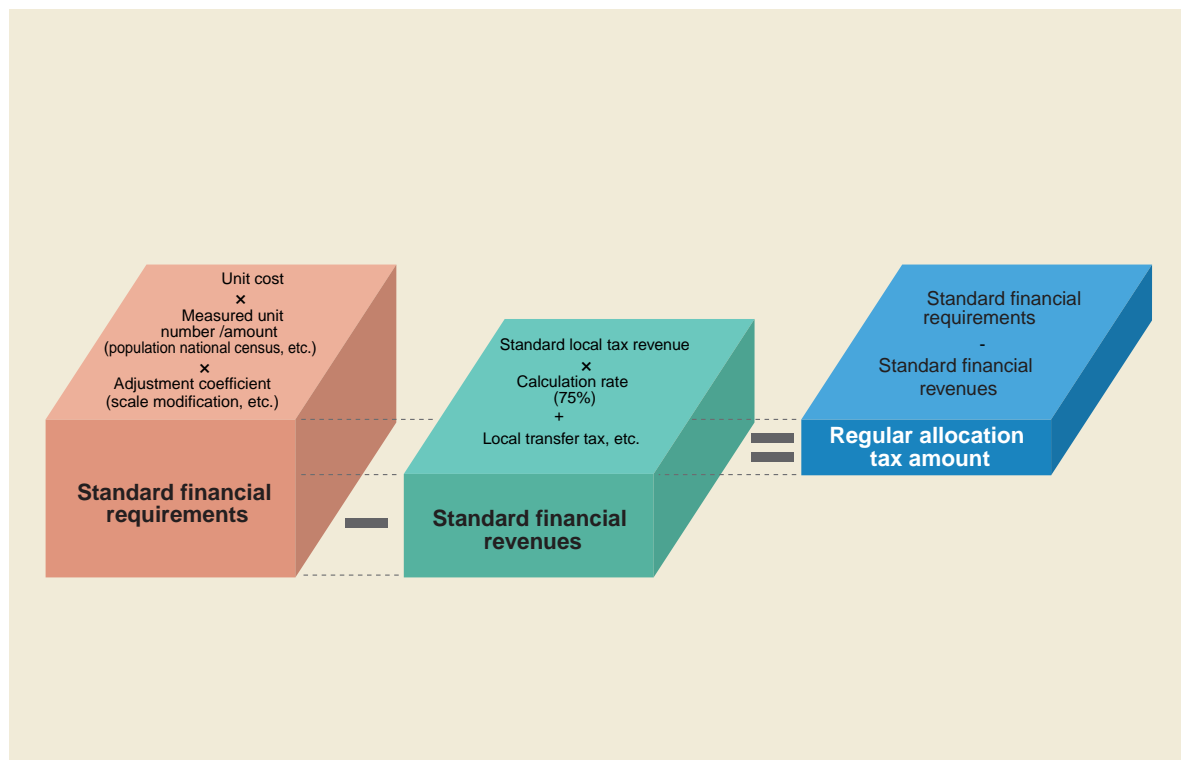
1 Determination of total amount of local allocation tax

The total amount of the local allocation tax is determined on the basis of certain ratios for national taxes (32% for income tax and liquor tax, 35.8% for corporate tax, 29.5% for consumption tax, and 25% for tobacco tax) as well as estimates of standard revenue and expenditure of local public finance as a whole.

The total amount of local allocation tax in fiscal 2003 was ¥18.0693 trillion, down 7.5% from the initial figure for the previous fiscal year.

2 Method of calculation of regular local allocation tax for each local government

The regular local allocation tax for each local government is calculated by the following mechanism:



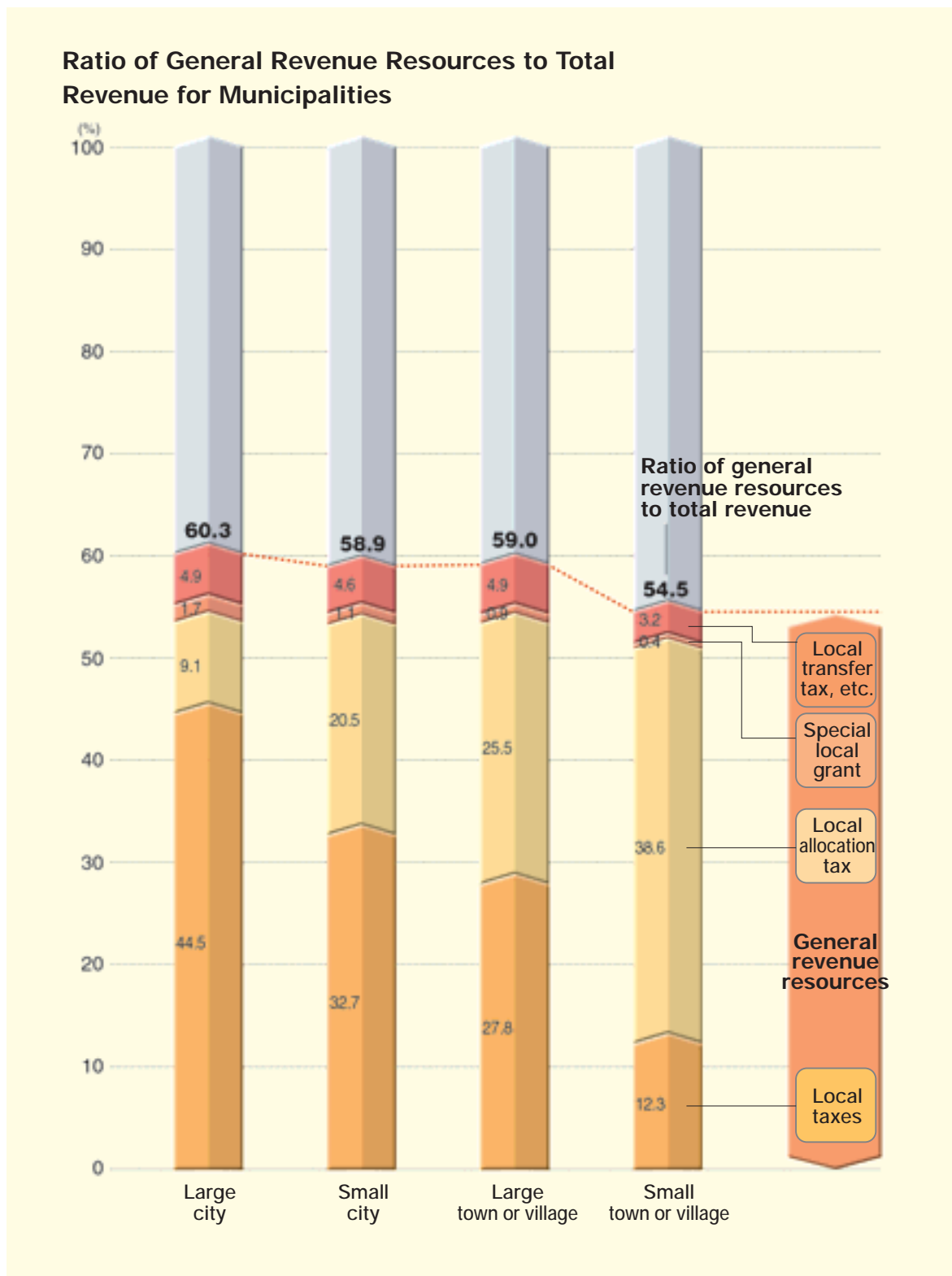
Notes:

1. Standard financial requirements are calculated as the financial requirements of each local government based on rational and appropriate standards. It is required to include the local share of the national treasury projects, such as compulsory education, livelihood protection, and public works, work project in calculating the standard financial requirements. From FY 2001 to FY 2006, part of the standard financial requirements is being transferred to special deficit-financing local bonds (extraordinary financial countermeasures bonds) under Article 5 of the Local Finance Law.
2. Normal local tax revenue neither includes “non-statutory ordinary taxes” and “non-statutory special purpose taxes” imposed independently by the local government nor “excess tax” that exceeds the standard tax rate stipulated in the Local Tax Law.

3 Function of the local allocation tax

The function of the local allocation tax is to adjust imbalances in revenue among local governments in order to guarantee revenue so that local governments can provide standard administrative services and basic social infrastructure to their residents in whatever region.

Accordingly, as a result of the revenue adjustment mechanism through the local allocation tax, few differences in such factors as size of population have been found in the ratio of general revenue resources to total revenue.



Notes:

1. A "large city" refers to a city with a population of more than 100,000 persons according to the national census of 2000; a "small city" refers to a city with a population of less than 100,000.
2. A "large town or village" refers to a town or village with a population of more than 10,000; a "small town or village" refers to a town or village with a population of less than 10,000.

Expenditure

What is revenue being expended for?

1 Expenses by Function

When expenses are classified by function, we see that a lot of revenue is expended for such items as education expenses, civil engineering work expenses, and public welfare expenses. In prefectures it is mainly expended for education expenses, civil engineering work expenses, and debt servicing, in that order. In municipalities it is primarily expended for public welfare expenses, civil engineering work expenses, and debt servicing, in that order.

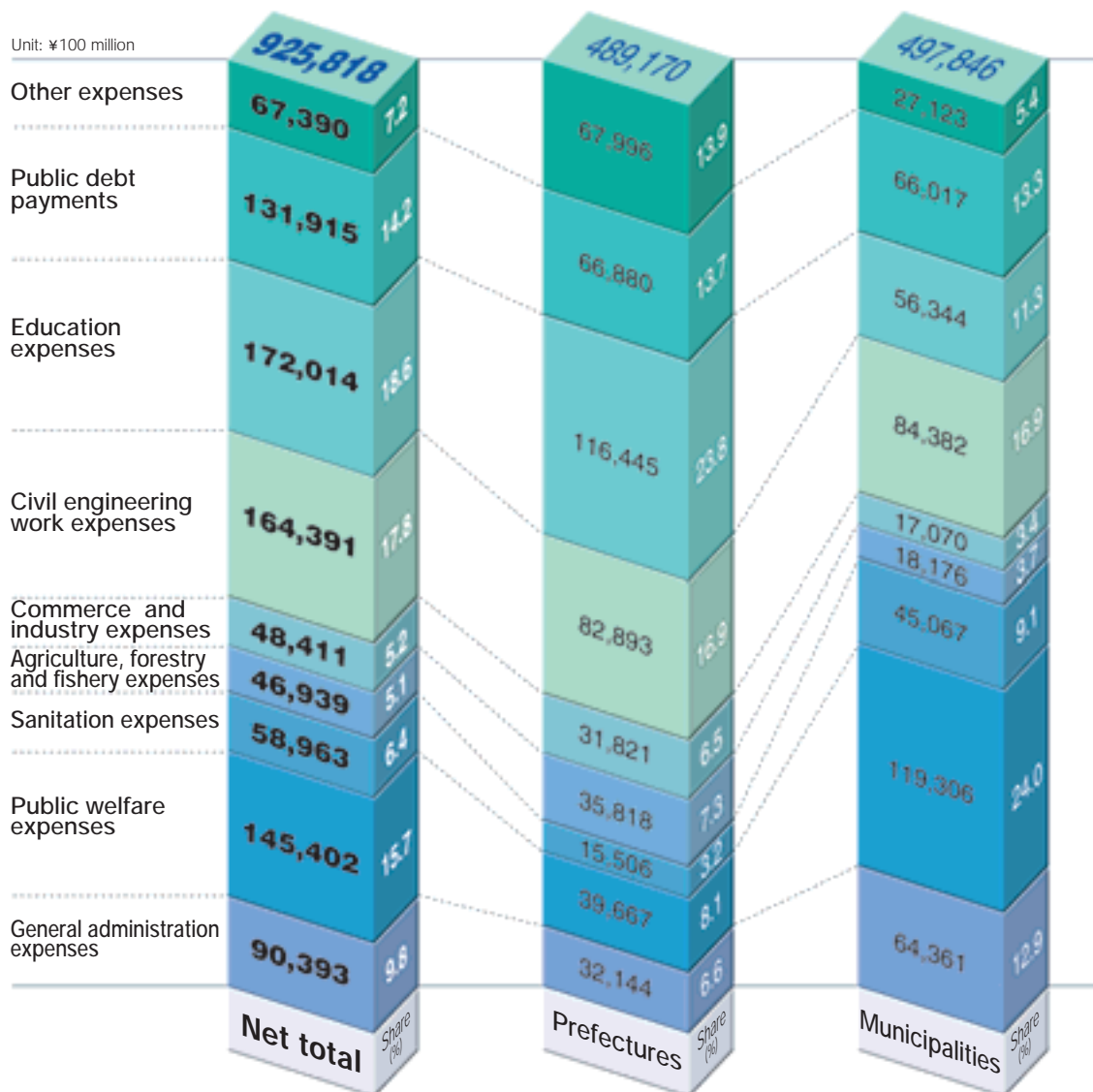
Education expenses: Expenses for school education, social education, etc.

Civil engineering work expenses: Expenses for the construction and improvement of public facilities, such as roads, housing and parks.

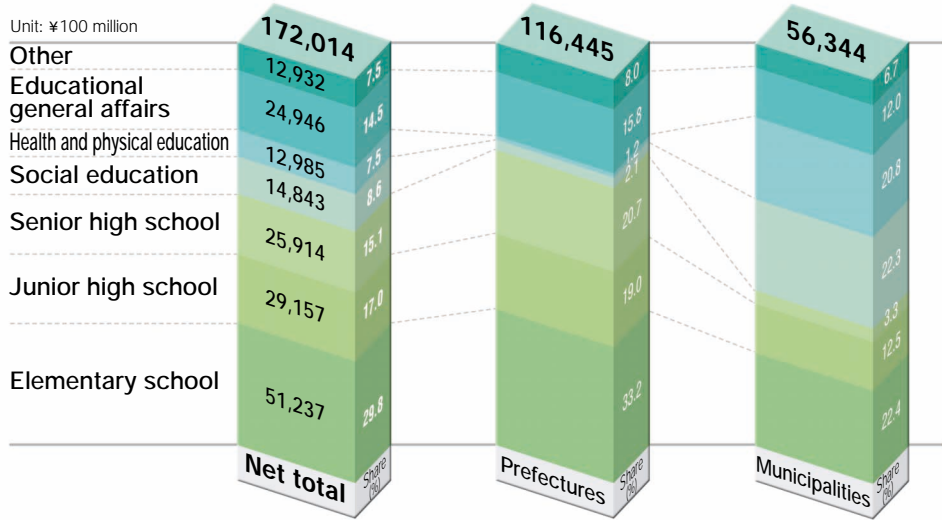
Public welfare expenses: Expenses for the construction and operation of welfare facilities for children, the elderly, the mentally and physically disabled, etc. and for the implementation of livelihood protection, etc.

Public debt payment: Expenses for the payment of principal, interest, etc. on debts.

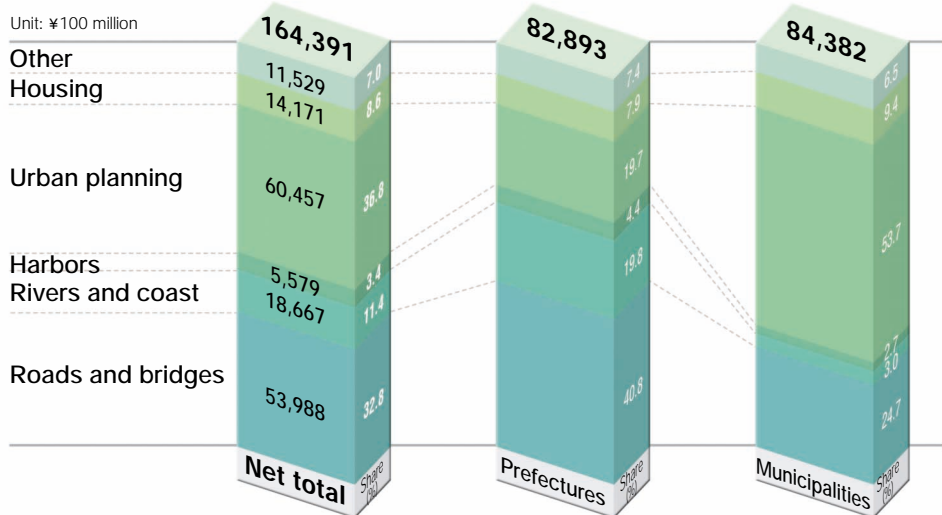
Composition of Expenditure by Function (FY 2003)



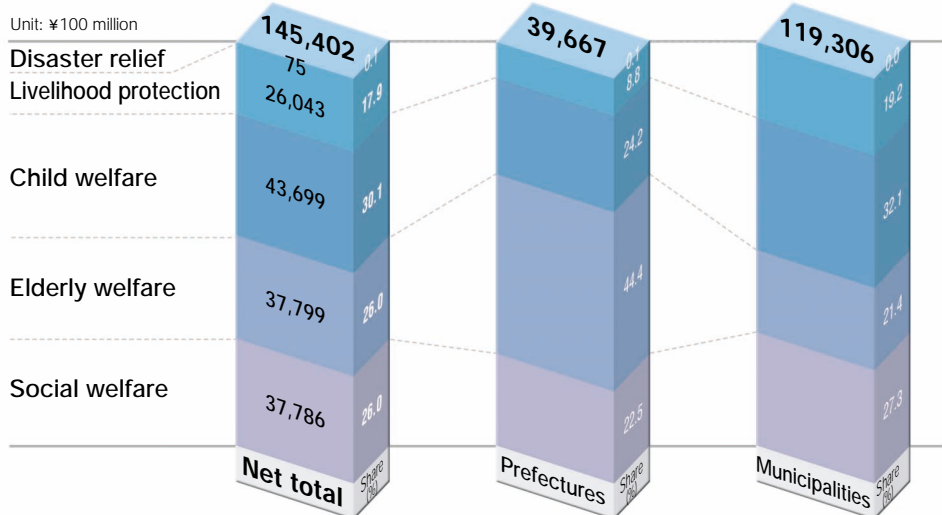
Breakdown of Educational Expenses by Purpose



Breakdown of Civil Engineering Work Expenses by Purpose



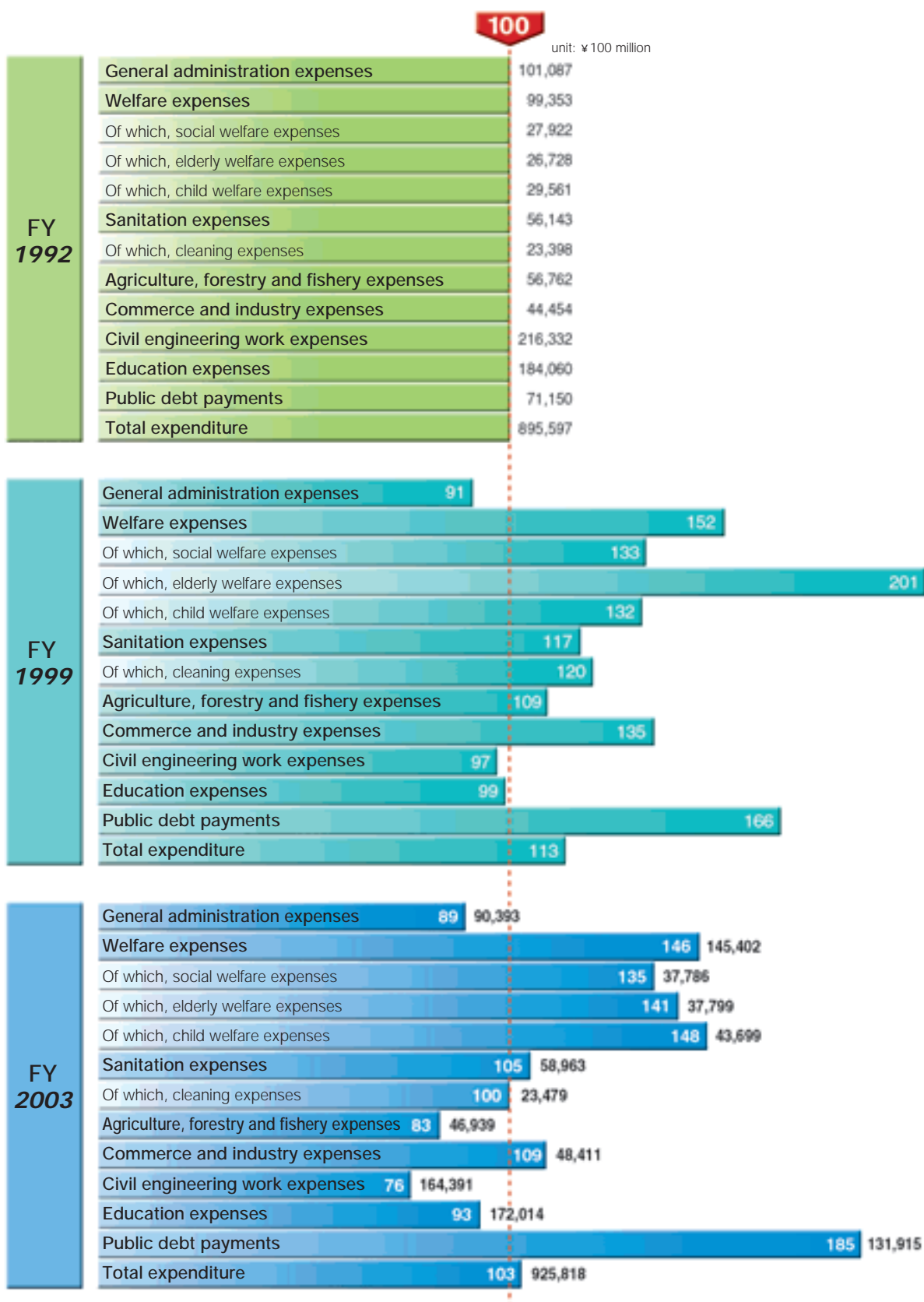
Breakdown of Public Welfare Expenses by Purpose



In recent years, while there has been a decline in such items as agriculture, forestry and fishery expenses, public debt payments have been increasing.

Trends in Expenditures by Function (ordinary account net total)

Unit: Ratio with FY 1992 as 100.

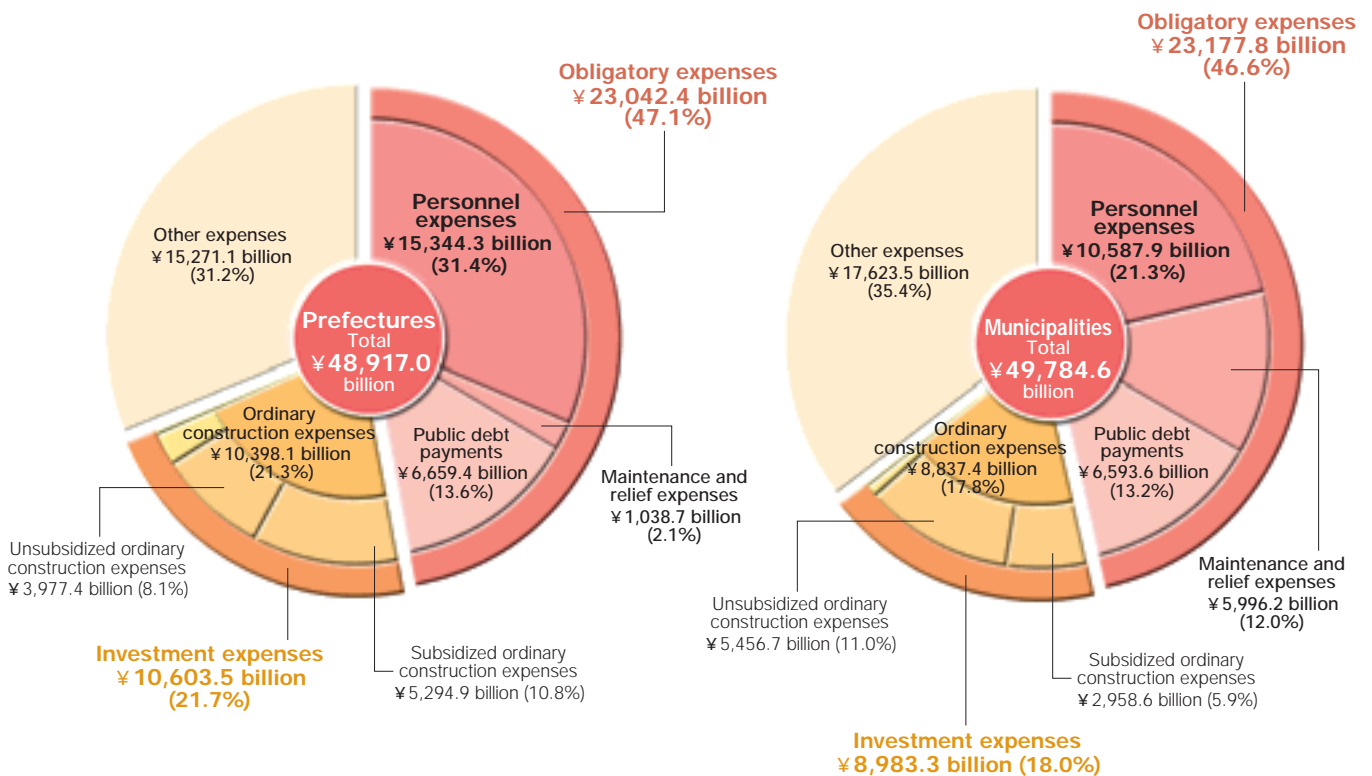
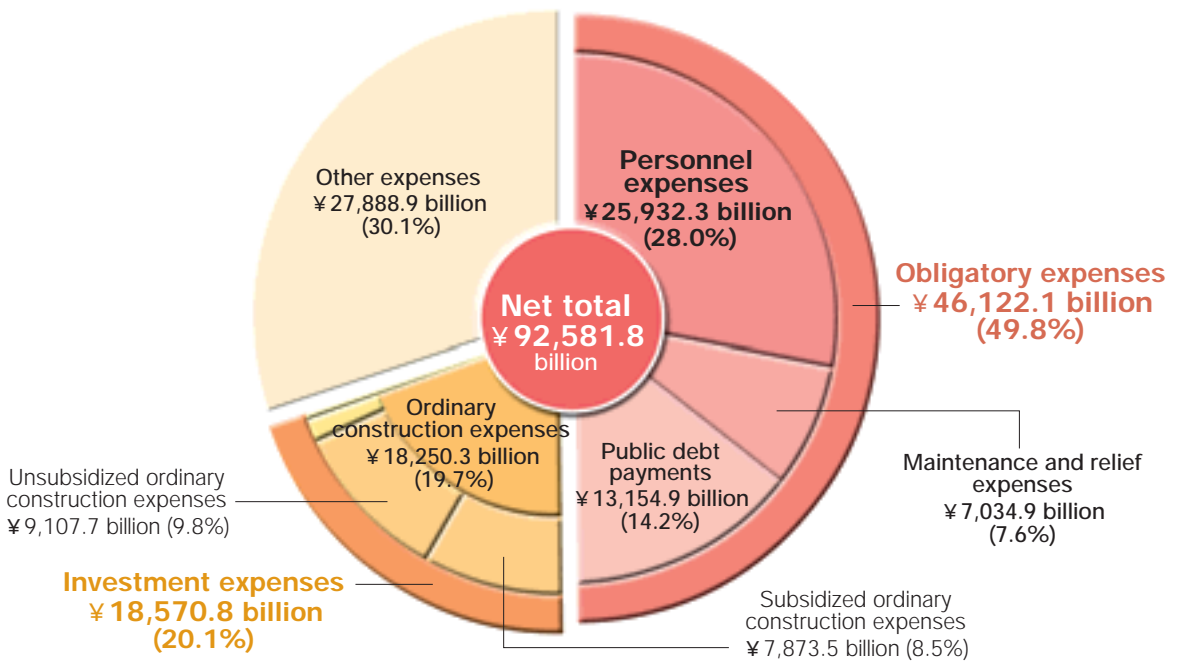


What are expenses for?

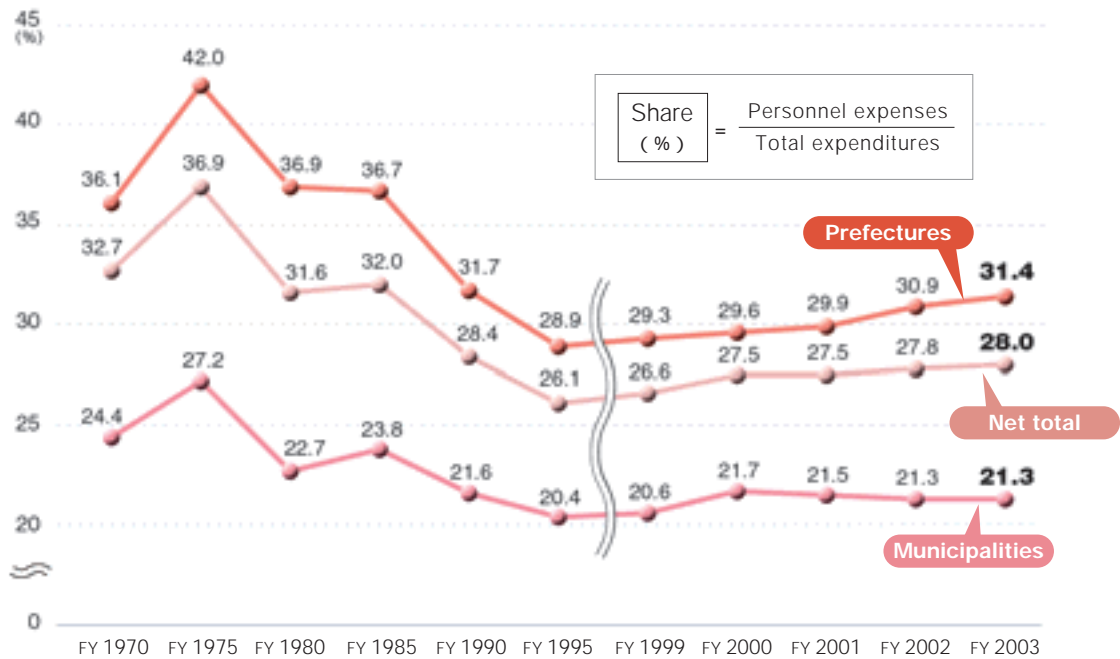
2 Expenses by Character

Classified by character, expenses can be divided into "obligatory expenses" (personnel expenses, maintenance and relief expenses and public debt payments), which are mandatory and difficult to cut down at the discretion of individual local governments; "investment expenses," including ordinary construction expenses, etc.; and "other expenses."

Expenditure by Character (FY 2003)

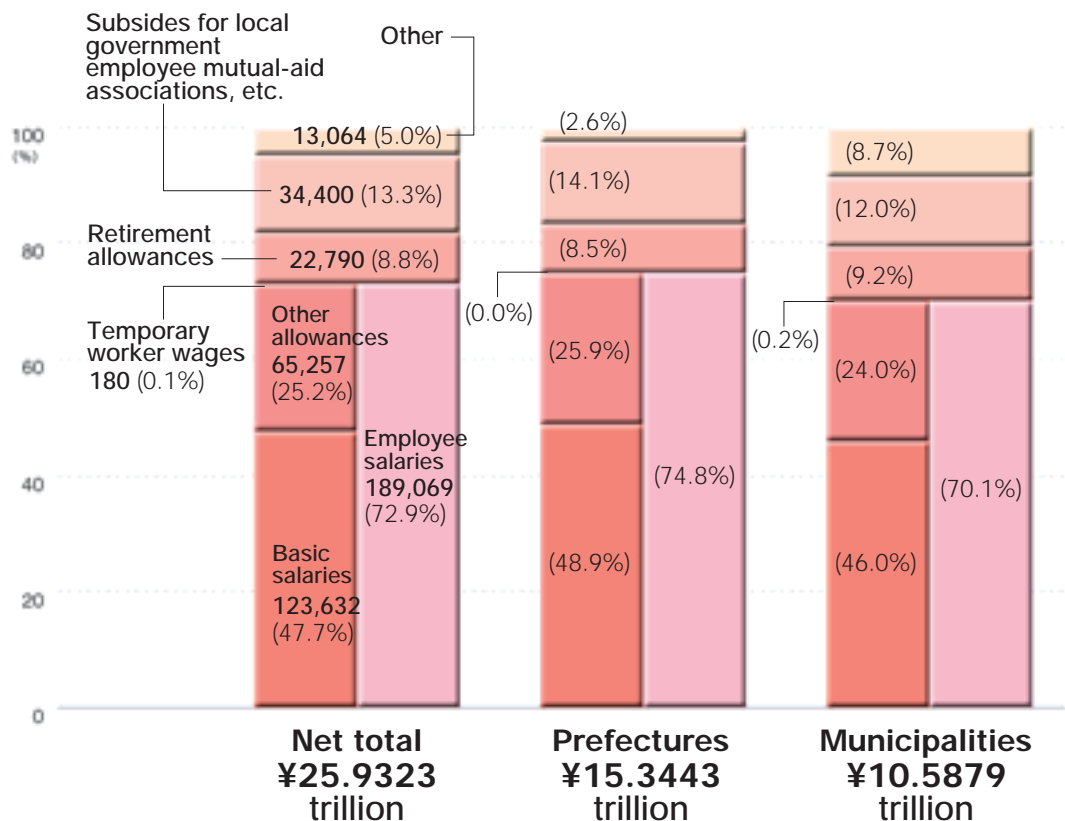


Trends in Personnel Expenses



Breakdown of Personnel Expenses by Item

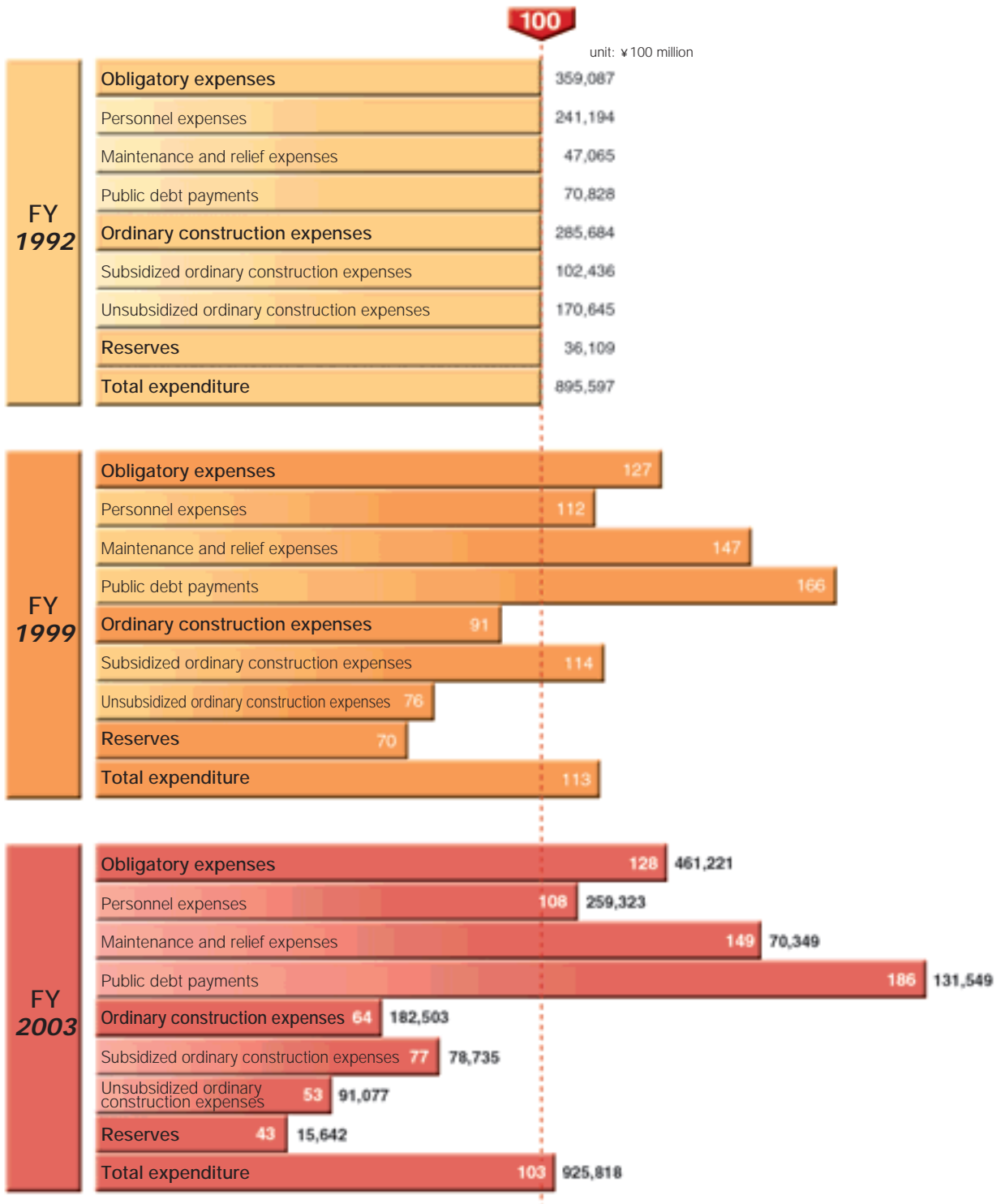
Unit: ¥100 million



In recent years, while there has been a decline in such items as ordinary construction expenses and personnel expenses, maintenance and relief expenses, public debt payments and so on have been increasing.

Trends in Breakdown of Expenditures by Character (ordinary account net total)

Unit: Ratio with FY 1992 as 100.



Maintenance and relief expenses

Expenses which include child welfare expenses, livelihood protection expenses, etc., aimed at assisting the needy, children, the elderly, mentally and physically disabled, etc., as a part of the social security system.

Ordinary construction expenses

Expenses necessary for the construction of social capital, such as roads, bridges, parks, schools, etc.

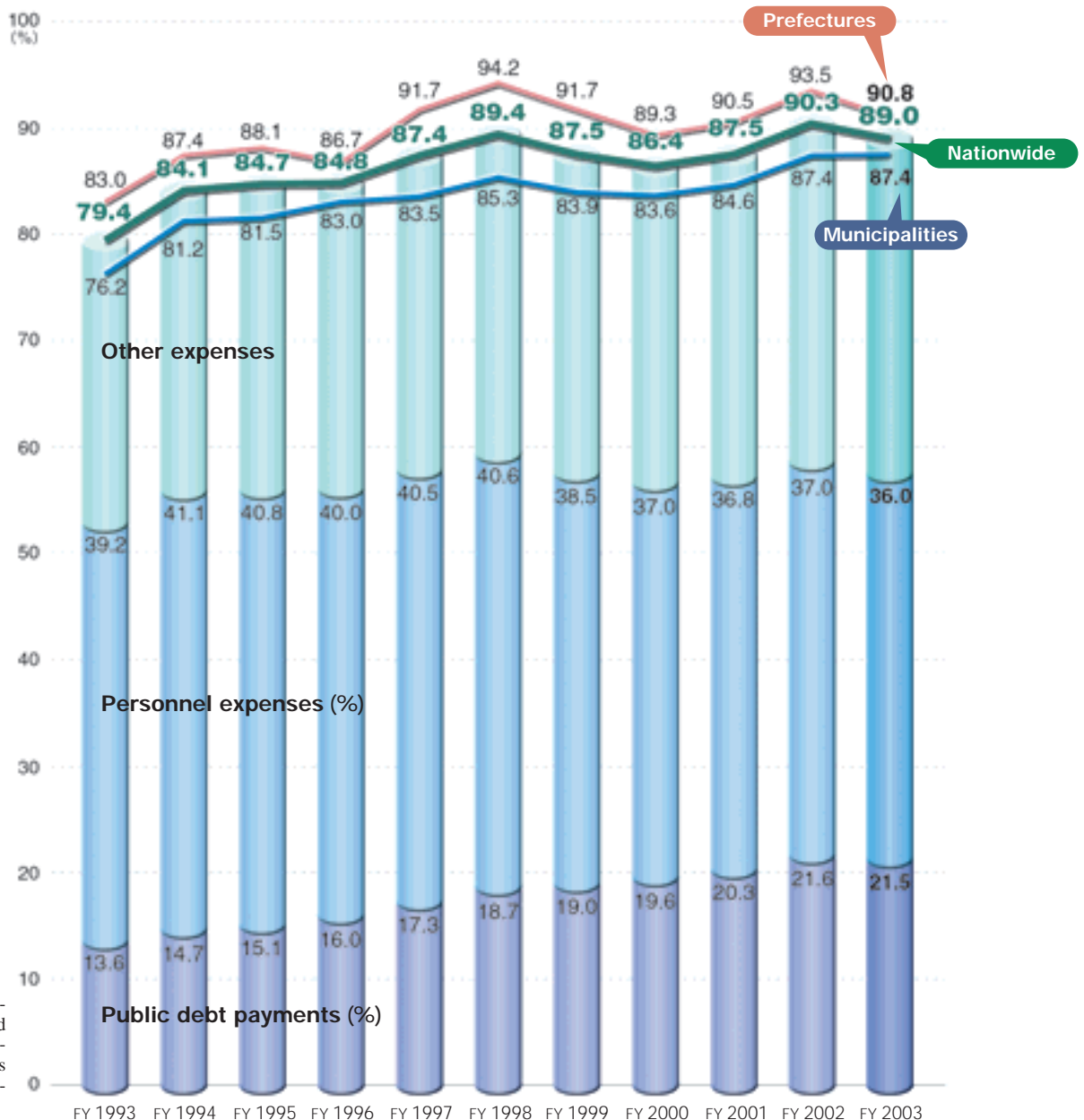
Flexibility of the Financial Structure

How can local finance respond to the demand toward local governments?

In addition to revenue sources allocated to obligatory expenses required every year, it is necessary for local governments to ensure revenue sources for measures to respond properly to social and economic trends and changes in the demand of the residents. The extent to which these revenue sources can be ensured is called the flexibility of the financial structure.

1 Ordinary Balance Ratio

The ordinary balance ratio (the ratio of ordinary revenue allotted to expenses recurring every fiscal year to the total of ordinary revenue recurring every fiscal year, centered on local taxes and the local allocation tax, as well as tax reduction supplementary bonds and extraordinary financial countermeasures bonds [see note]) is declining, both on a prefectural average and national average, because of such factors as a decrease in personnel expenses and an increase in tax-reduction supplementary bonds and extraordinary financial countermeasures bonds.



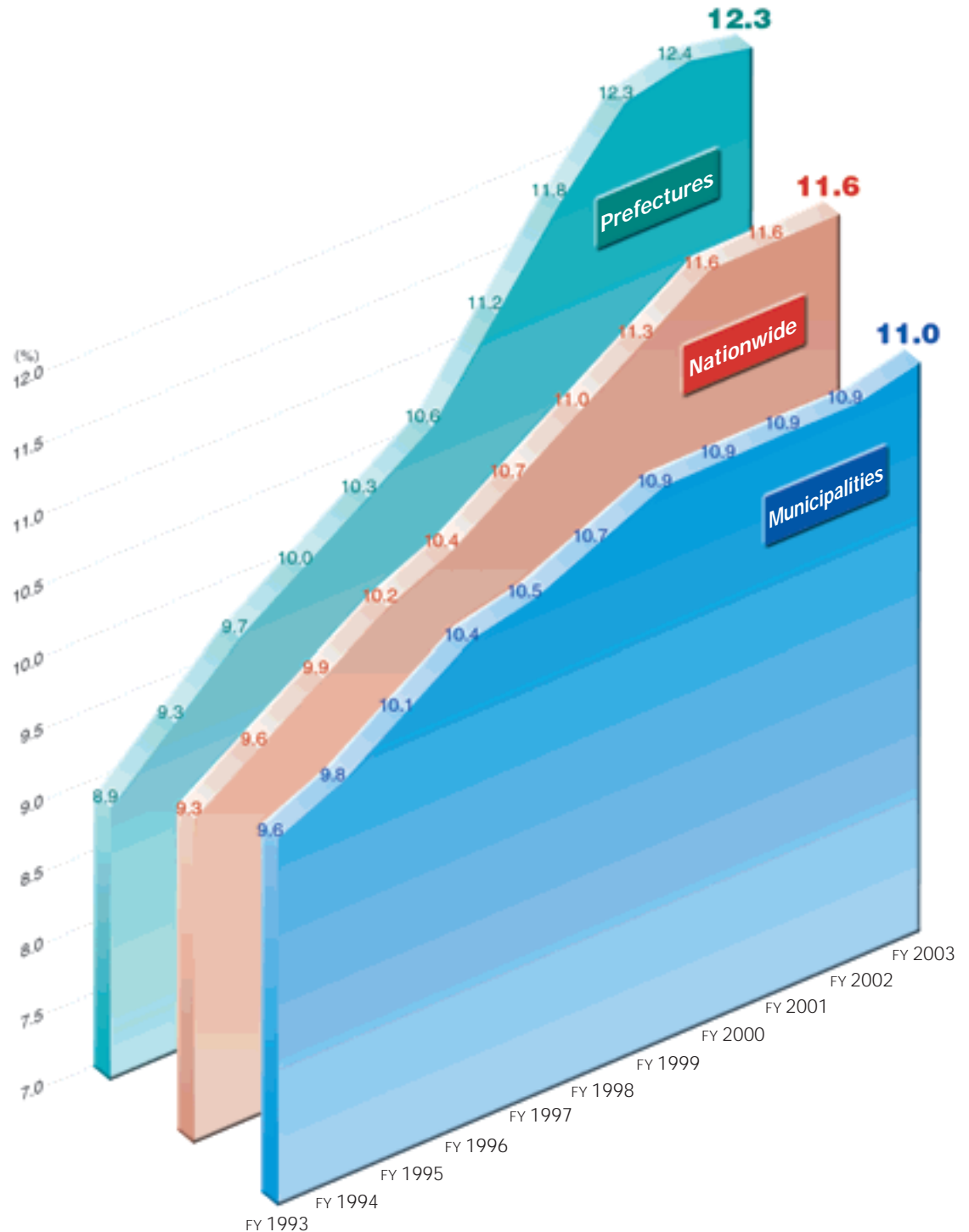
Note:
Tax-reduction supplementary bonds and extraordinary financial countermeasures bonds have been added since fiscal 2001.

2 Debt Service Payment Ratio Used for Permission to Issue Local Bonds

It is necessary to keep a close watch on trends in public debt payments at all times, since public debt payments, payments of principal and interest on the debts of local governments, are expenses especially lacking flexibility.

The debt service payment ratio used to restrict the issue of local bonds, which is an index that takes into consideration the local allocation tax calculated for debt payments and indicates the actual degree of debt payment burden, has been continuing to maintain a high level; the national average, for example, was the same as the record high figure of the previous fiscal year.

Trends in the Debt Service Payment Ratio Used for Permission to Issue Local Bonds



Debt service payment ratio used for permission to issue local bonds

The debt service payment ratio used for permission to issue local bonds is an index showing the ratio of local debt principal and interest repayment (excluding advanced redemption and the amount of general revenue resources calculated for this purpose that includes the local allocation tax) to the total of standard financial amount (excluding the amount of local allocation tax calculated for service payment) and possible issue of extraordinary financial countermeasures bonds. This index is one of the criteria to limit the issue of local bonds. In principle, the issue of local bonds relating to general unsubsidized projects, etc. is prohibited in the case of local governments with a ratio of 20% or over.

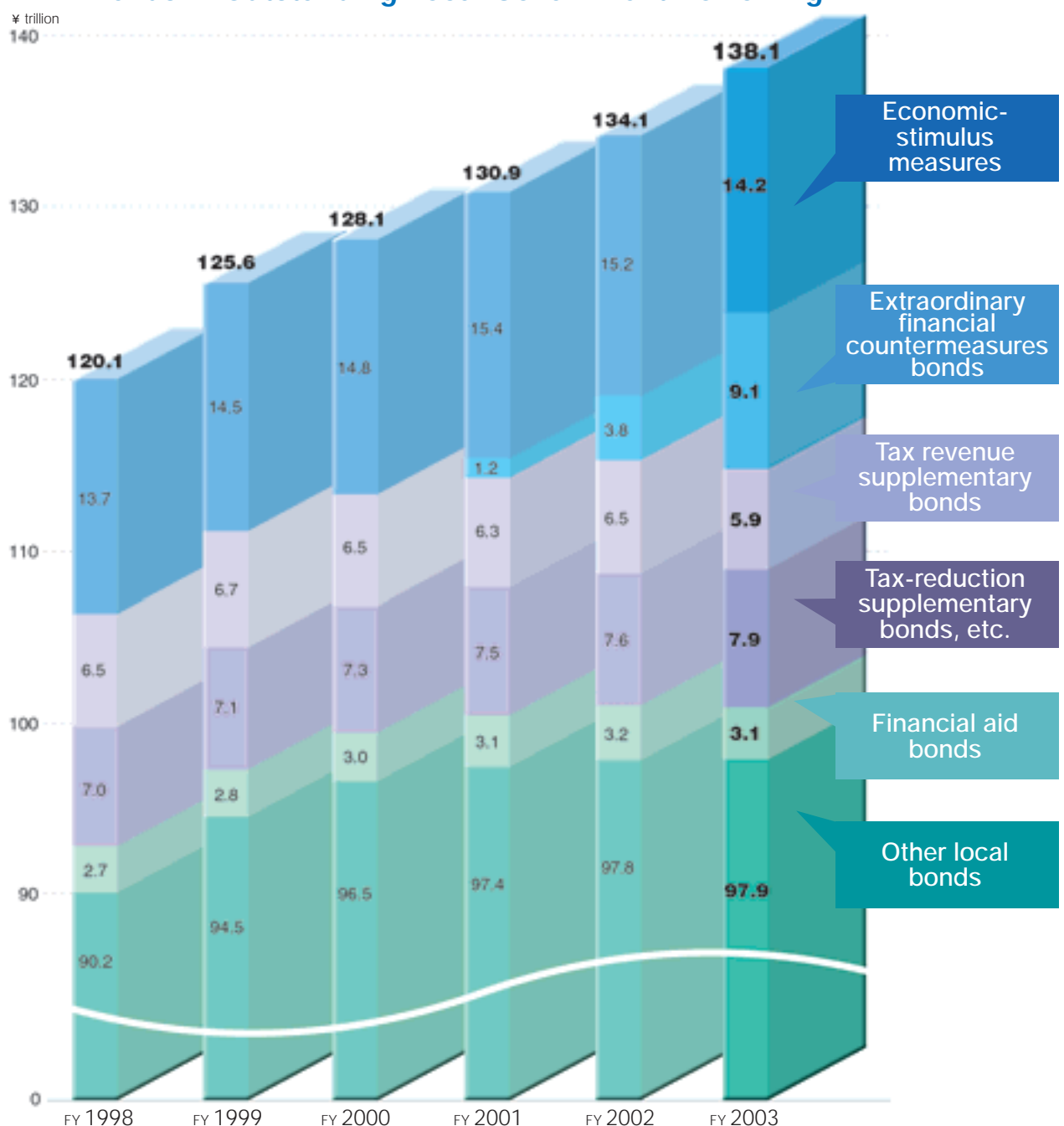
Outstanding Local Government Borrowing (Ordinary Account)

What is the state of debts in local public finance?

1 Trends in Outstanding Local Government Borrowing

Outstanding local government borrowing, the debts of local governments, amounted to approximately ¥138 trillion at the end of fiscal 2003. This figure has been increasing in recent years because of such factors as the need to supplement tax revenue as a result of the decrease in local tax revenue and tax cuts, the added public investment by economic-stimulus measures, and the issue of extraordinary financial countermeasures bonds. The figure is 1.5 times larger than total revenue and 2.6 times larger than general revenue resources, such as local taxes and local allocation tax.

Trends in Outstanding Local Government Borrowing



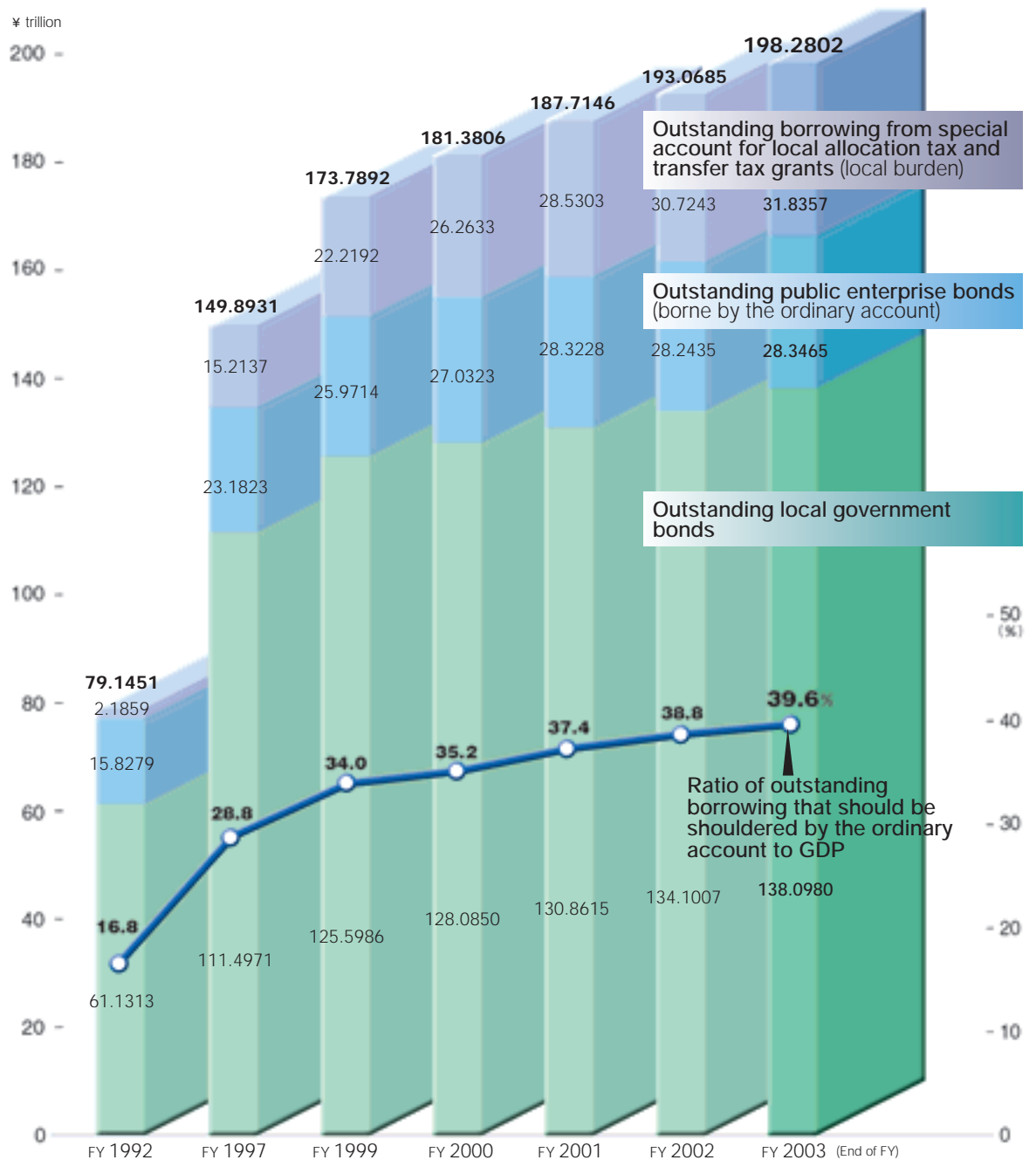
Notes:

1. Outstanding local government borrowing excludes special fund public works bonds and special fund public investment bonds.
2. Economic-stimulus figures are estimates.

2 Outstanding Borrowing of Local Finance

The outstanding borrowing of local finance, including the local burden of borrowing from the special account for local allocation tax and transfer tax grants and those public enterprise bonds borne by the ordinary account, as well as current outstanding local government bonds, has been increasing sharply in recent years. The figure reached about ¥198 trillion at the end of fiscal 2003 and is expected to reach ¥205 trillion at the end of fiscal 2005.

Trends in Outstanding Borrowing That Should Be Shouldered by the Ordinary Account and Ratio of Outstanding Borrowing to Gross Domestic Product



Notes:

1. Outstanding local government borrowing excludes special fund public works bonds and special fund public investment bonds.
2. Outstanding public enterprise bonds (borne by the ordinary account) are estimates based on settlement statistics.

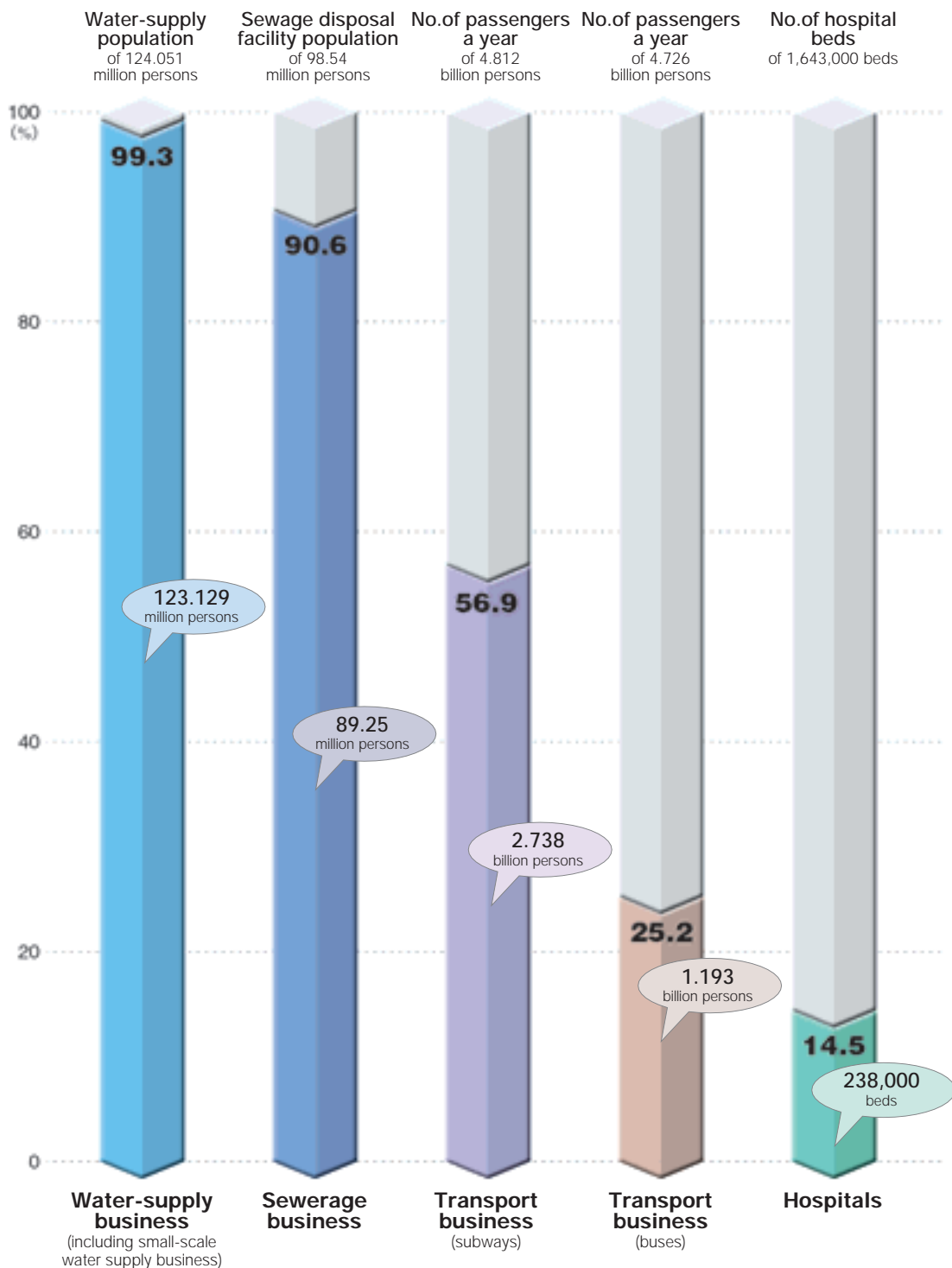
Local Public Enterprises

What is the state of local public enterprises?

Local public enterprises are managed directly by local governments for the purpose of social and public benefit. They provide social infrastructure and services indispensable for local residents and the development of the community, including water supply, sewerage, transport and hospitals.

1 Ratio of Local Public Enterprises

Local public enterprises play a major role in improving the standard of living of residents.

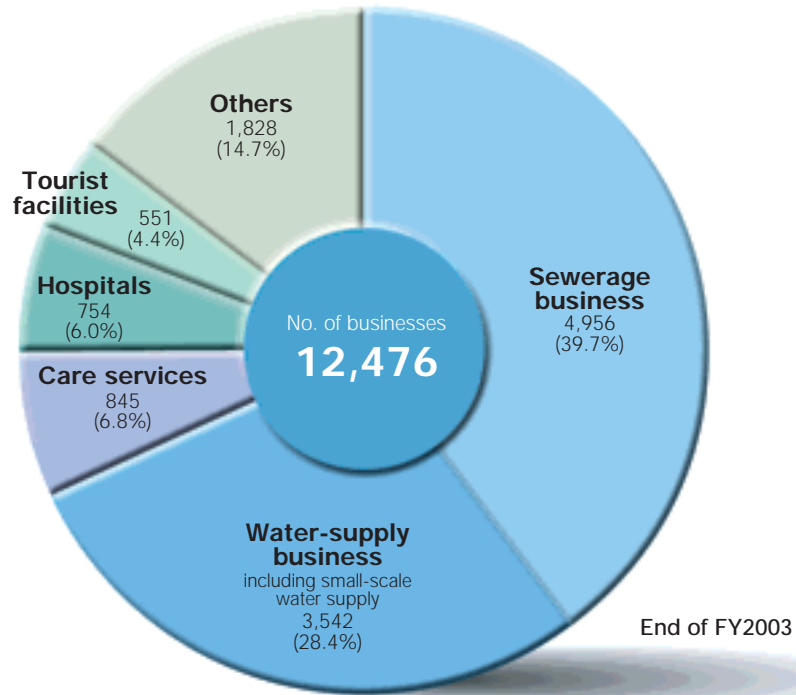


*The graph shows the ratio of local public enterprises when the total number of business entities nationwide is taken as 100.

*Figures for the total number of enterprises nationwide are compiled from statistical materials of related organizations; figures for local public enterprises are compiled from figures for the total number of enterprises and settlements for the previous fiscal year.

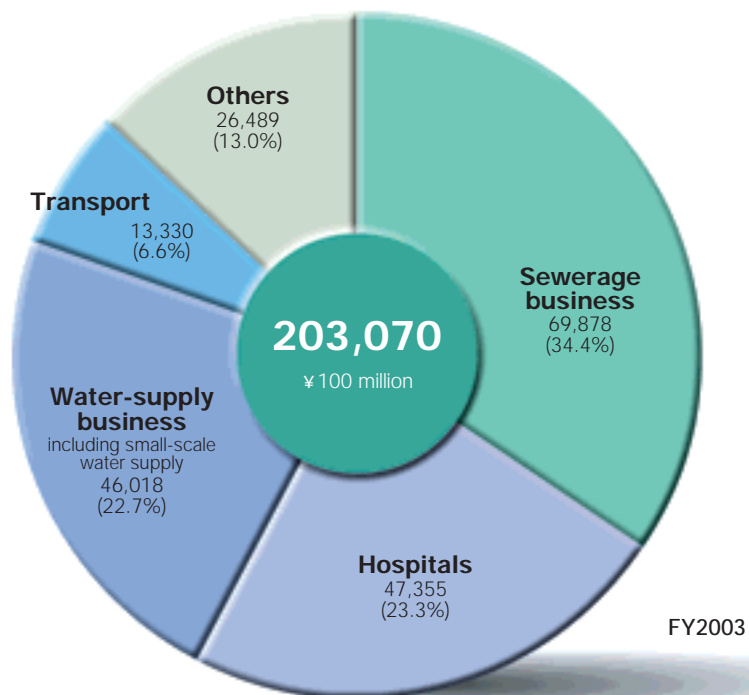
2 Number of Businesses Operated by Local Public Enterprises

The number of businesses is 12,476. By type of business, sewerage accounts for the largest ratio, followed in order by water supply, care services, and hospitals.



3 Scale of Financial Settlement

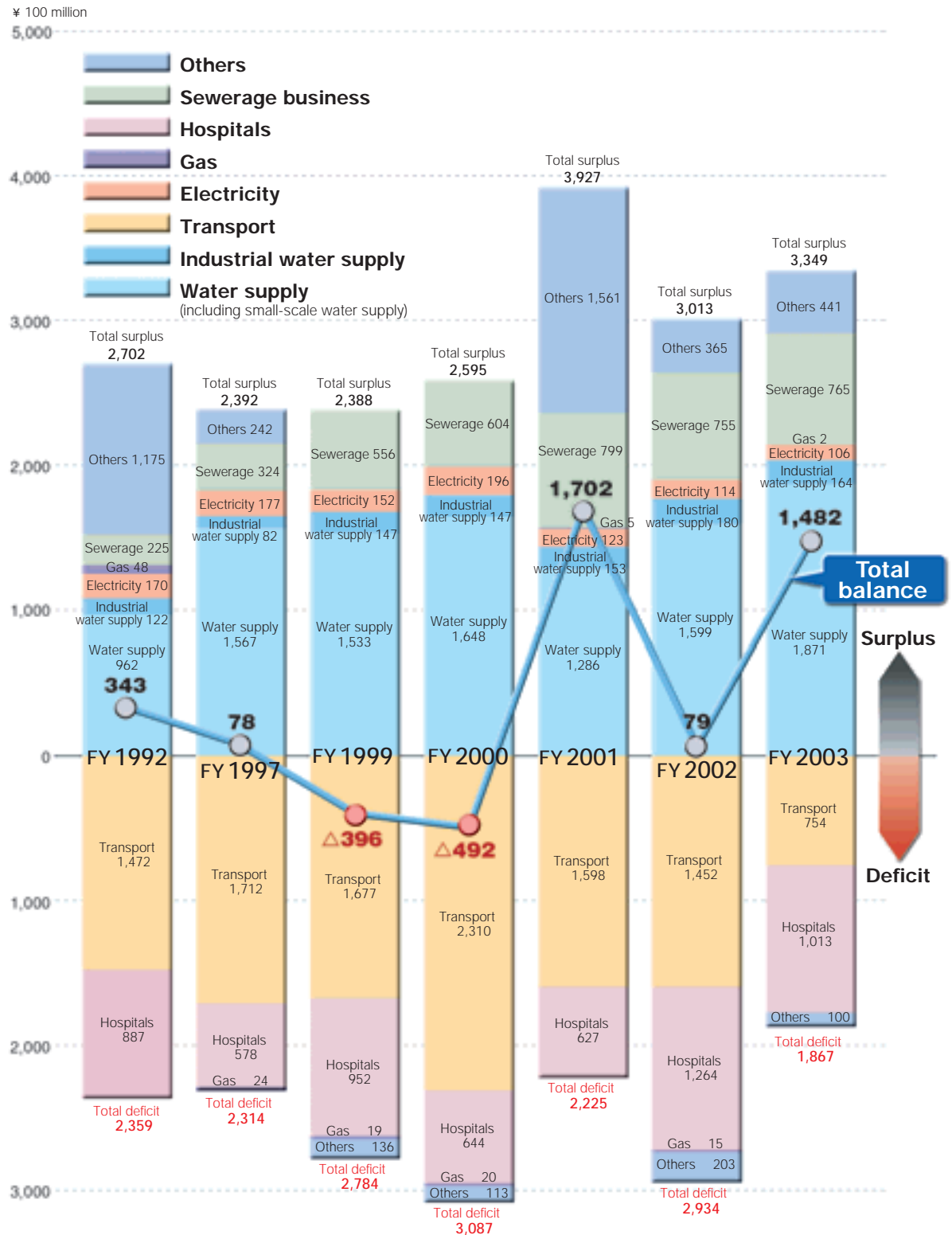
The total financial settlement scale is ¥20.3070 trillion. By type of business, sewerage accounts for the largest ratio, followed in order by hospitals, water supply, and transport.



4 Management Conditions

Local public enterprises had a surplus of ¥148.2 billion. By type of business, while water supply, industrial water supply, electricity, and sewerage showed a surplus, transport and hospitals are continuing to register a deficit.

Trends in Management Conditions of Local Public Enterprises



Efforts Toward Sound Financial Conditions

What efforts have been made toward sound local finance?

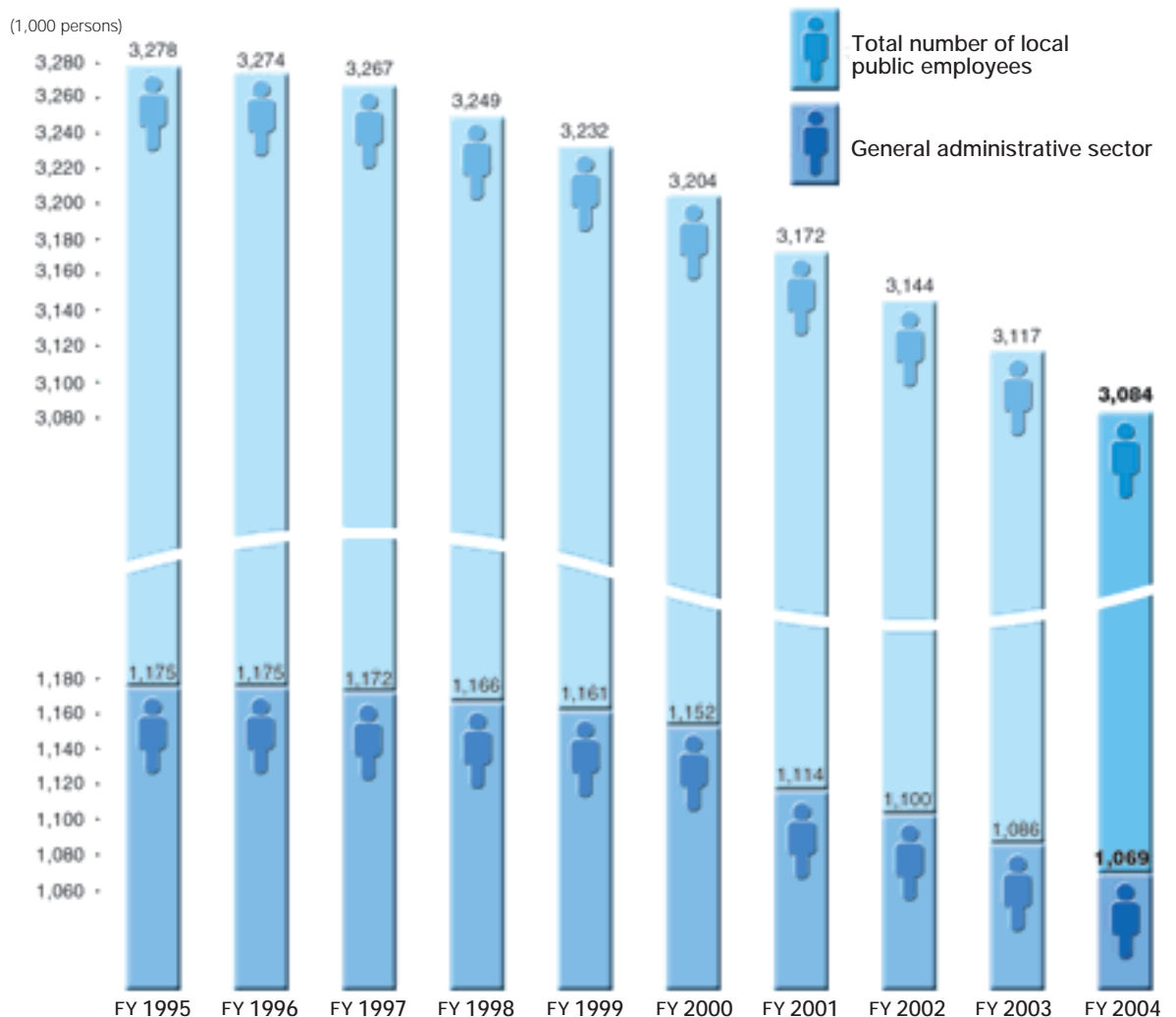
While local public finance is certainly in an extremely severe situation, the role of the local government, which is clarified as the comprehensive administrative entity of the region, is becoming increasingly important. For this reason, various efforts for administrative reform are being made with the aim of making administrative organizations simpler, more efficient and more responsible to new administrative issues.

1 Number of Public Employees

The number of local public employees has declined for 10 consecutive years since 1995. The number of employees has fallen for nine consecutive years in the general administrative sector and 13 consecutive years in the special administrative sector and has also dropped for three consecutive years in the public enterprise sector.

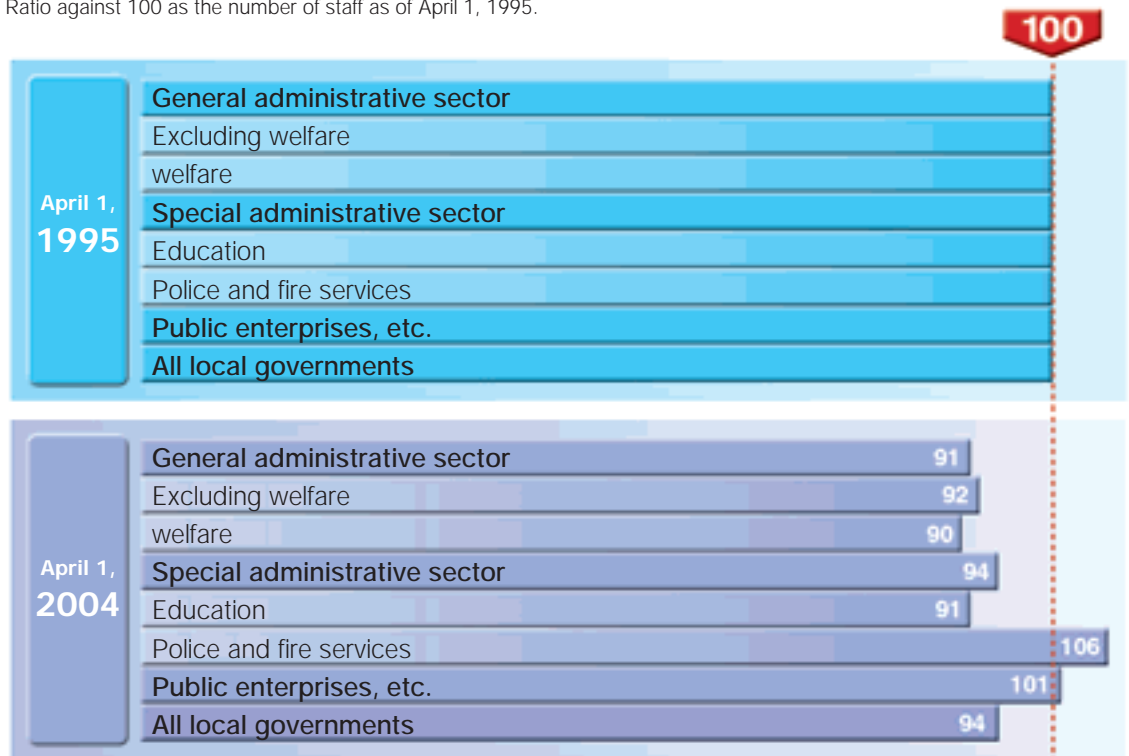
The background of this trend lies the efforts, which have been made to restrain the increase of the total number of employees through the setting of numerical targets and scrap-and-build policies, although the number of employees has increased in some areas because of such factors as the enhancement of public-security and disaster-prevention measures.

Number of Local Public Employees



Trends in the Number of Staff in Local Governments by Sector

Unit: Ratio against 100 as the number of staff as of April 1, 1995.

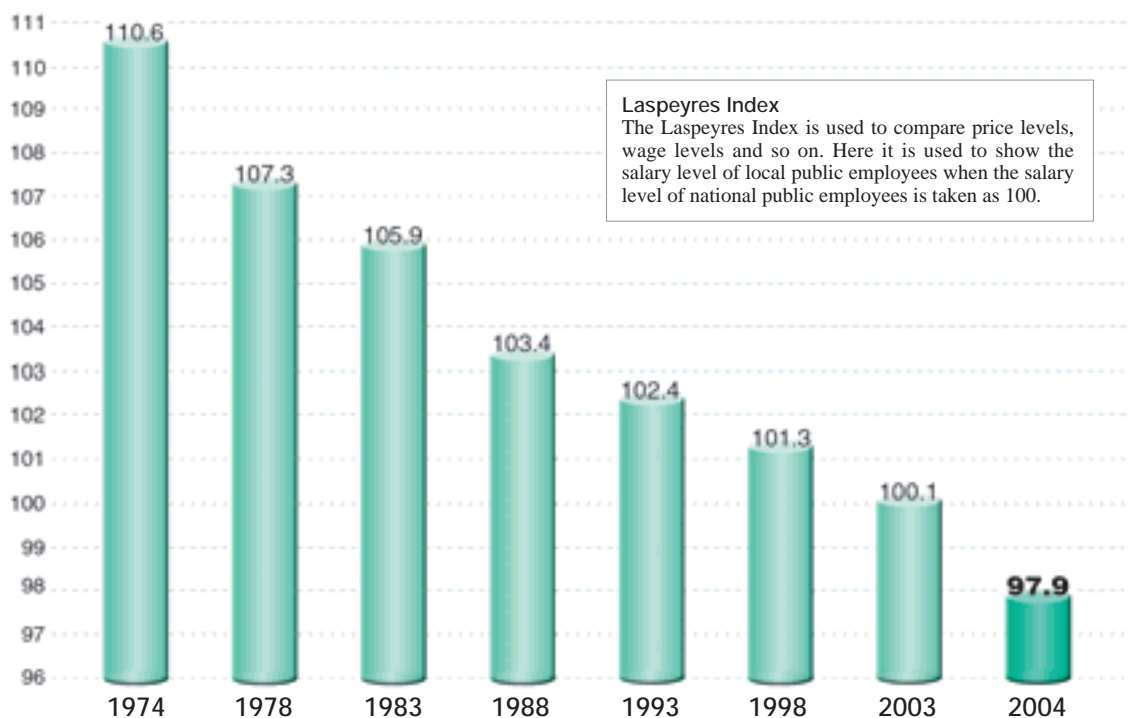


2 Salary Level

When the salary level of local public employees is shown on the Laspeyres Index, the average for all local governments is 97.9.

More than 1,400 local governments have implemented their own salary-reduction measures, as a result of which personnel expenses in fiscal 2004 were expected to be cut by approximately ¥140 billion.

Trends in the Laspeyres Index (Trends in the Average for All Local Governments)



Laspeyres Index

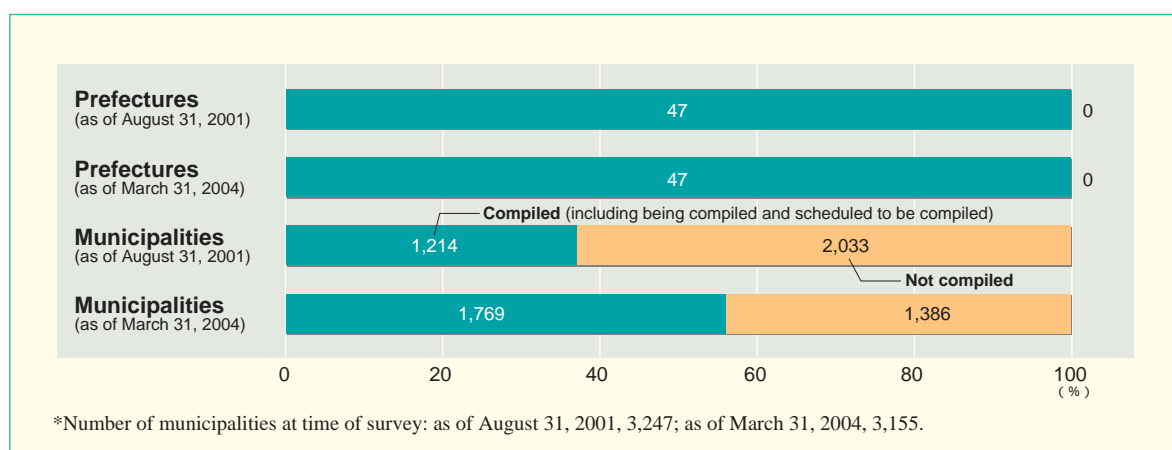
The Laspeyres Index is used to compare price levels, wage levels and so on. Here it is used to show the salary level of local public employees when the salary level of national public employees is taken as 100.

In the meantime, in recent years an increasing number of local governments have been compiling balance sheets as a means of disclosing and analyzing financial conditions in order to grasp the state of their assets and liabilities in a comprehensive manner.

Example of Balance Sheet (City A)

FY 2003 Ordinary Account Balance Sheet		(As of March 31, 2004; unit: ¥1,000)	
Debit		Credit	
(Assets)		(Liabilities)	
1. Tangible fixed assets		1. Fixed liabilities	
(1) General administration expenses	11,988,830	(1) Local government bonds	58,864,797
(2) Welfare expenses	2,896,302	(2) Contract authorization	
(3) Sanitation expenses	4,638,834	(1) Purchase of property, etc.	0
(4) Labor expenses	375,522	(2) Guarantee of obligation or loss compensation	0
(5) Agriculture, forestry and fishery expenses	4,969,931		Total 0
(6) Commerce and industry expenses	2,227,833	(3) Retirement allowance reserve	5,991,639
(7) Civil engineering work expenses	57,481,118	Total	64,856,436
(8) Fire service expenses	544,254	2. Liquid liabilities	
(9) Education expenses	52,306,962	(1) Scheduled redemption in next fiscal year	7,373,172
(10) Others	273,934	(2) Appropriation made in advance	0
	Total 137,703,520	Total	7,373,172
(of which, land	46,861,437)	Total liabilities 72,229,608	
Total	137,703,520	(Net assets)	
2. Investment, etc.		1. National treasury disbursements	
(1) Investment and equity funds	4,590,696		19,888,897
(2) Loan	895,408	2. Prefectural disbursements	
(3) Funds			5,473,103
(1) Special purpose funds	6,630,887	3. General revenue sources, etc.	
(2) Land development funds	2,048,740		61,383,240
(3) Fixed-in investment	4,000	Total net assets	86,745,240
	Total 8,683,627	Total of liabilities and net assets 158,974,240	
Total	14,169,731		
3. Liquid assets			
(1) Cash, deposits			
(1) Adjustment fund for finance	2,091,975		
(2) Sinking funds	1,207,658		
(3) Cash in yearly account	884,405		
	Total 4,184,038		
(2) Receivables			
(1) Local taxes	2,187,109		
(2) Others	730,450		
	Total 2,917,559		
Total	7,101,597		
Total assets	158,974,848		
Information relating to contract authorization			
(1) Matters relating to the purchase of property, etc.		669,219	
(2) Matters relating to guarantee of obligation and loss compensation		5,073,577	
(3) Matters relating to compensation for paid interest, etc.		1,403,984	

State of Compilation of Balance Sheets (no. of organizations)



4 Examples of Administrative Reform Efforts

Local governments are making various administrative reform efforts with the aim of achieving sound financial conditions. The following are some of them:

Examples of Specific Efforts

Prefecture

A

Greater efficiency in the payment of travel expenses and salaries through establishment of the General Affairs Administration Center

In fiscal 2002 established, for the first time in the country, a General Affairs Administration Center for the comprehensive processing of administrative work relating to the payment of travel expenses, salaries, etc. of main office staff and commenced the consignment of administrative work to the private sector. The number of staff was reduced by 41 persons through integration and outsourcing. This move has the effect of cutting expenses by about ¥350 million a year.

Implementation of administration evaluation utilizing administrative inventory sheets

Since fiscal 1997 has compiled administrative inventory sheets to fully clarify the work of the prefecture and uses them in administration evaluation. In fiscal 2003 the inventory sheets, with additional information for evaluation, were submitted to the special committee on settlement of the prefectural assembly and also reflected in the budget and business. Is building a purpose-oriented administrative management system that can be called the Japanese version of New Public Management (NPM).

Building of a speedy and flexible administrative work processing setup through the streamlining of the organization

In fiscal 1998, for the first time in the country, abolished sections and established purpose-oriented offices. Abolished middle management posts and trimmed ranking classes. This contributed to reducing the time take for the standard processing of license applications to an average of about 5.2 days and a reduction in the number of staff by 100 persons.

Prefecture

B

Reduction of number of staff by about 20% (about 3,000 persons) in the 10 years from fiscal 1999 - 2008 (reduction of 2,540 persons in the six years from fiscal 1999 - 2004)

Reduction of managerial allowances (10% reduction from fiscal 2001-04)

Reduction of number of prefecture-related organization staff by about 20% (about 600 persons) in the nine years from fiscal 2000 - 08 through a review of prefecture-related organizations (reduction of 516 persons in the five years from fiscal 2000 - 04)

A review of public facilities to abolish, privatize, etc. more than 26 facilities (about 20%) in the seven years from fiscal 2002 - 08

City

C

Reduction of number of staff by 1,000 persons (about 5.9%) in the five years from fiscal 2004 - 08. (Reduction of 202 persons in fiscal 2004.)

Reduction of salaries for special posts. (15% reduction for mayor and 10% reduction for deputy mayor, etc. in fiscal 2002 - 04.)

In the five years from fiscal 2004 - 08 the number of auxiliary organizations (45 organizations) will be reduced by more than 10% (5 organizations).

In the five years from fiscal 2004 - 08 the number of full-time staff dispatched from the city to auxiliary organizations will be reduced by more than 30% (78 persons) from the total of 259 persons in fiscal 2003. (In fiscal 2004, the number was reduced by 8.5%, or 22 persons.)

Raising the municipal tax collection rate from 94.8% in the settlement of fiscal 2002 to the 96% level in the fiscal 2008.

Revision of administrative work using the administration assessment system. (In fiscal 2003 the revision of 430 projects had a fiscal effect of approximately ¥10.2 billion; in fiscal 2004 the revision of 352 projects had a fiscal effect of approximately ¥5.6 billion.)

5 Promotion of Local Administrative Reform Through the New Local Administrative Reform Guidelines

In order to solidly promote local administrative reform, the Ministry of Internal Affairs and Communications compiled the New Guidelines for the Promotion of Administrative Reform in Local Governments (the New Local Administrative Reform Guidelines) and notified local governments of them on March 29, 2005.

These guidelines indicate important items in the promotion of administrative reform and, in order to promote administrative reform in an intensive manner, requests local governments during fiscal 2005 to disclose intensive reform plans showing specific efforts from fiscal 2005 as the starting point to around fiscal 2009.

Administrative Reform Outline and Intensive Reform Plan

Adoption of numerical targets, easy-to-understand indicators, etc.

During FY 2005

Disclosure of intensive reform plans showing specific efforts from fiscal 2005 as the starting point to around fiscal 2009.

- Reorganization and arrangement of administrative work and projects
- Promotion of private-sector consignment, etc. (including utilization of the designated manager system)
- Rationalization of staff management (show prospects for numbers of retirees and recruits and staff target for April 1, 2010)
- Rationalization of salaries, including thorough inspection of allowances (operation of wage table, revision of various allowances, including retirement allowance and special work allowance)
- Revision of third sector
- Fiscal effect through reducing expenses, etc.

Etc.

*Also disclosure concerning local public enterprises

Regarding the intensive reform plans submitted by prefectures, designated cities, and municipalities, the Ministry of Internal Affairs and Communications will give advice to the local government concerned as necessary and disclose the plan in an easy-to-understand manner.

In the light of severe criticism from the public concerning, among other things, the payment of inappropriate allowances in some local government bodies, efforts will be aggressively made to correct such conditions.

Issues of Local Finance

1 The Trinity Reform

Background of the Reform

Amid a situation in which local finance is suffering a severe shortage of resources, in order to further promote decentralization, under the principle of “entrusting to local governments what they can do,” it is necessary to increase the degree of freedom of local governments in terms of both income and expenditure and to foster the true independence of the regions. From this perspective, it was decided to mutually connect, study, and revise, in a uniform manner, the reform of national treasury subsidies, the distribution of tax resources, including the transfer of tax resources, and the local allocation tax.

Realization of an income structure based mainly on local taxes

→ Further clarification of correspondence between benefit and burden of administrative services

Reduce the gap between the expenditure scale and tax revenue of local governments as much as possible.

Expenditure state : local = 2 : 3

Tax revenue state : local = 3 : 2

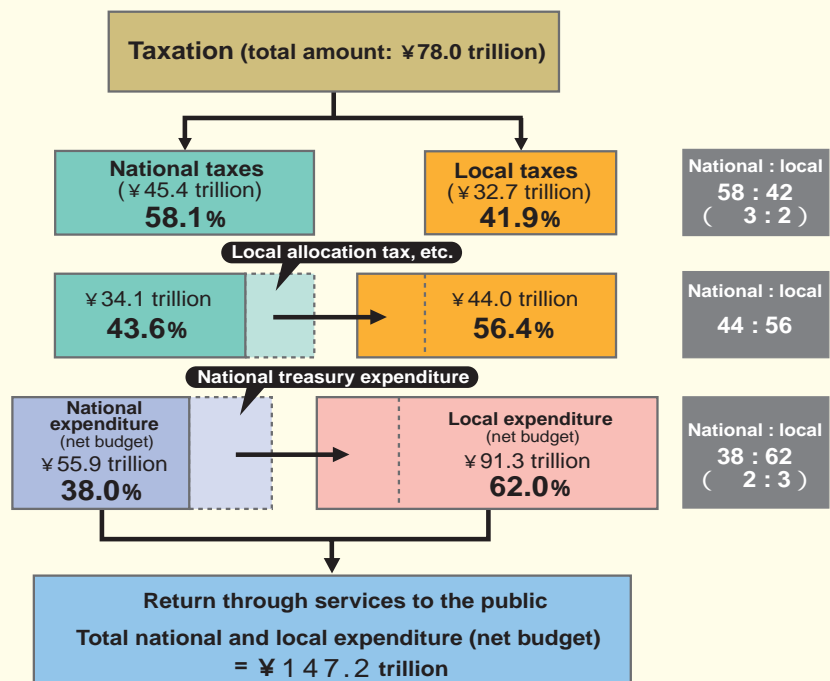
Revision of involvement of the central government through national treasury subsidies, legislation, etc.

Promotion of administrative reform and fiscal structure reform in the national and local governments

The Trinity Reform

Reference

Distribution of Financial Resources Between the National and Local Governments (FY 2003)



Overall Picture of the Trinity Reform Until FY 2006

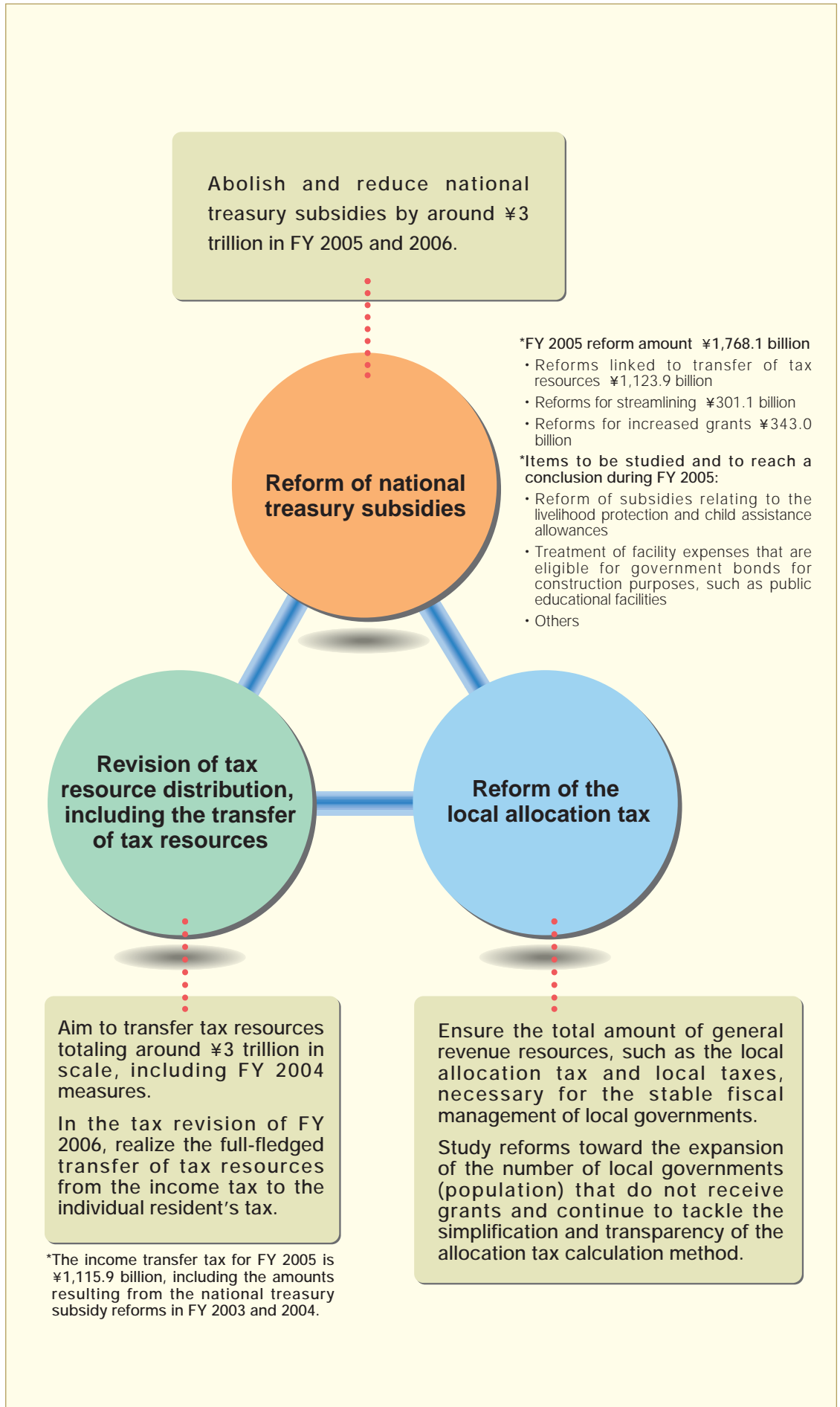
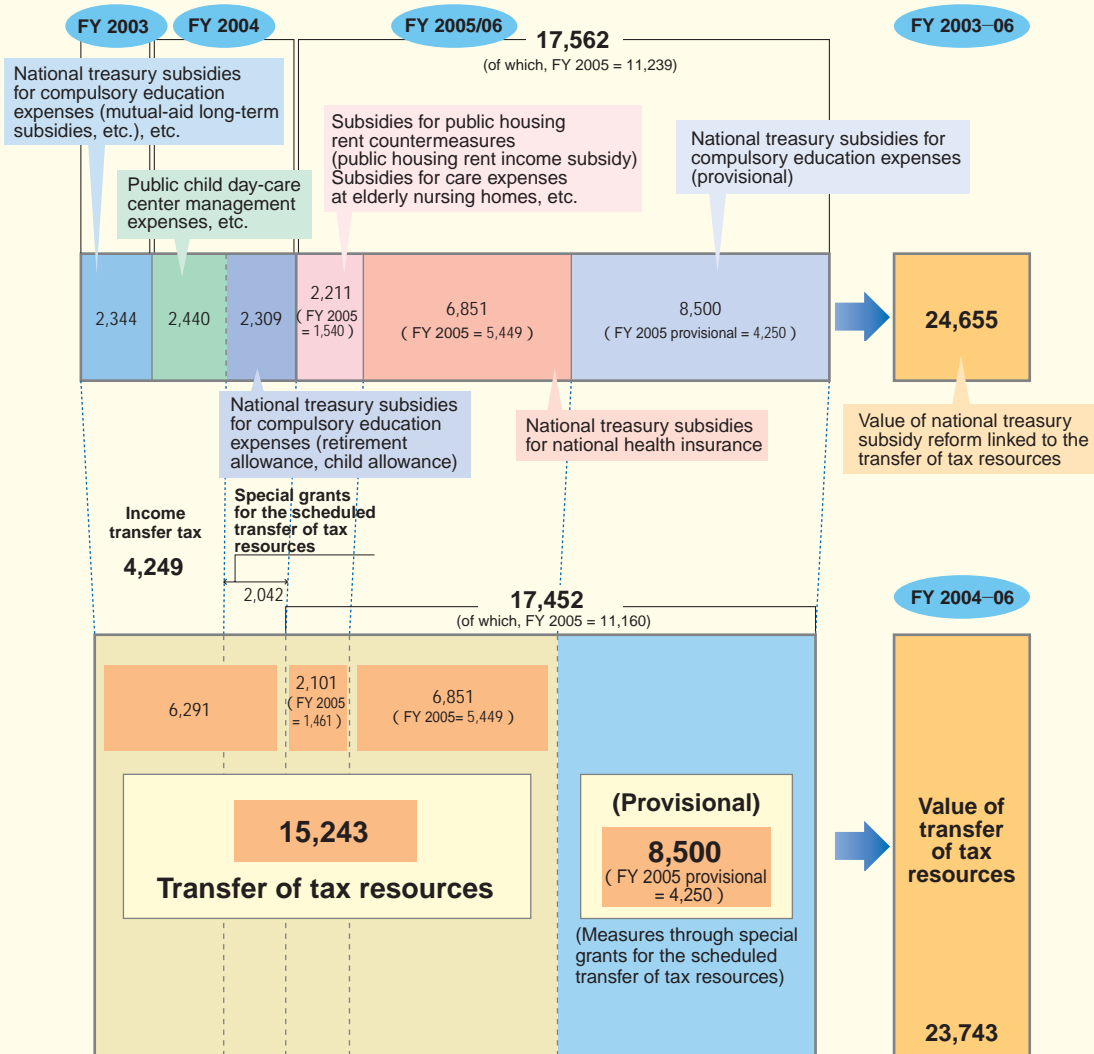


Image of National Treasury Subsidy Reform Linked to the Transfer of Tax Resources

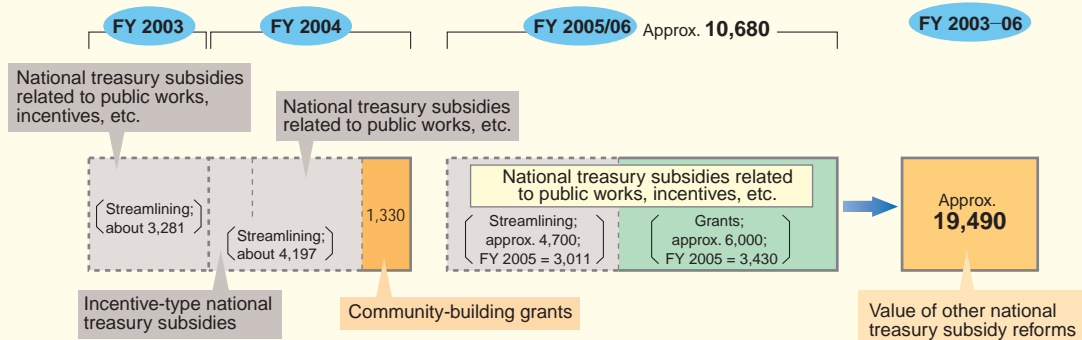
FY 2005 base
(unit: ¥100 million)



(Including provisional)

*Regarding special grants for the scheduled transfer of tax resources relating to national treasury subsidies for compulsory education expenses (retirement allowance and child allowance), the calculation has been made on the basis of the required value for FY 2005.

(Reference) Other national treasury subsidy reforms



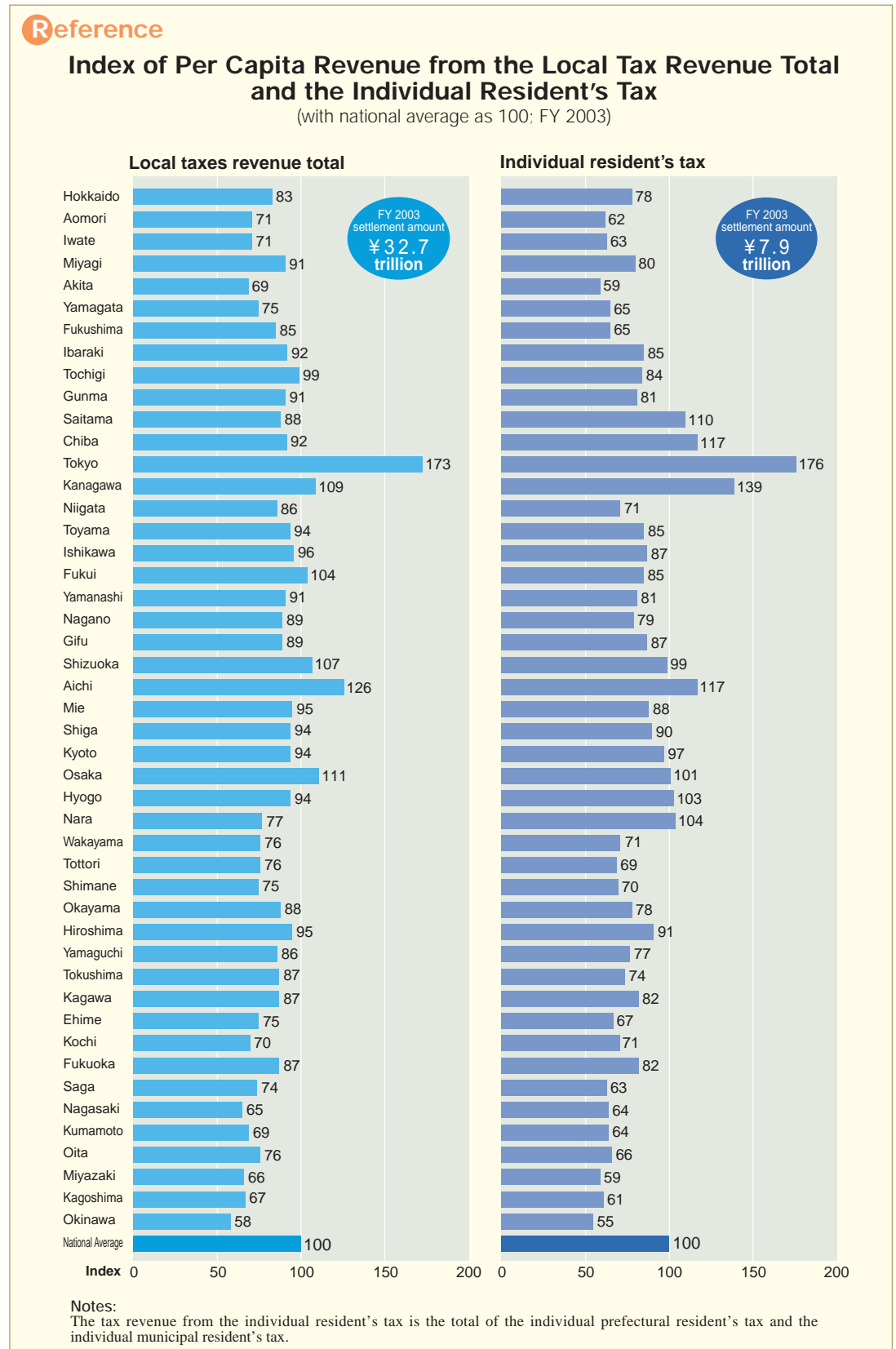
Notes:

1. Of the above, the required value of national treasury subsidies for compulsory education expenses (retirement allowance and child allowance) that is being implemented through special grants for the scheduled transfer of tax resources from FY 2004 fluctuates depending on the fiscal year.
2. The figures for "other national treasury subsidy reforms" for FY 2005 and 2006 are calculated on the basis of an agreement between the government and the ruling parties on November 26, 2004.
3. In addition to the above, in FY 2003 tax resources of ¥93 billion were transferred to the automobile tonnage transfer tax through the introduction of a new direct-control formula in the construction of national highways.

2 Expansion of the Financial Base

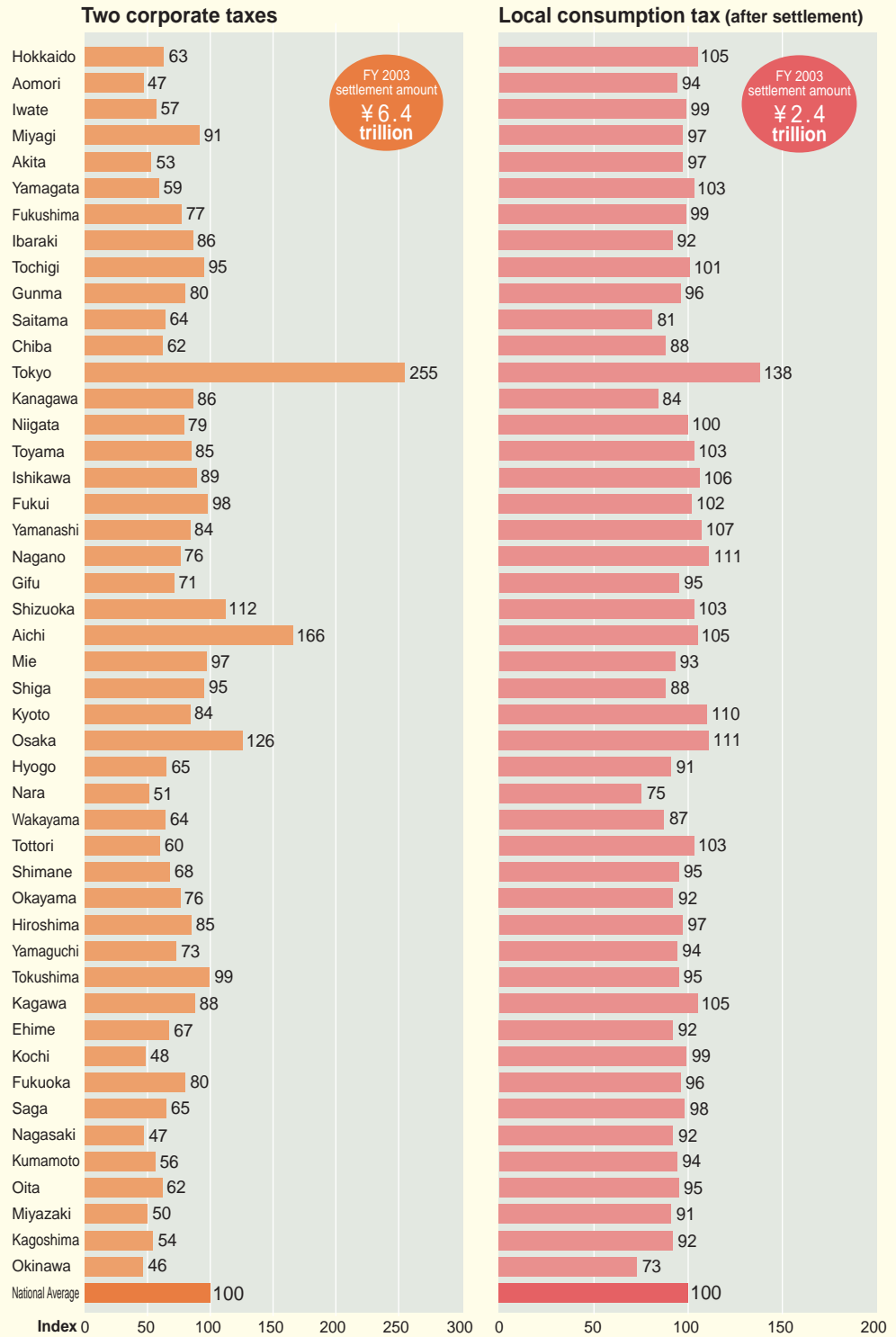
Local Taxes

In order for local governments to provide administrative services in response to local needs with responsibility and at their own discretion, it is necessary to expand and secure local taxes so as to build a local tax system in which the uneven distribution of tax sources is limited and the stability of tax revenue is ensured.



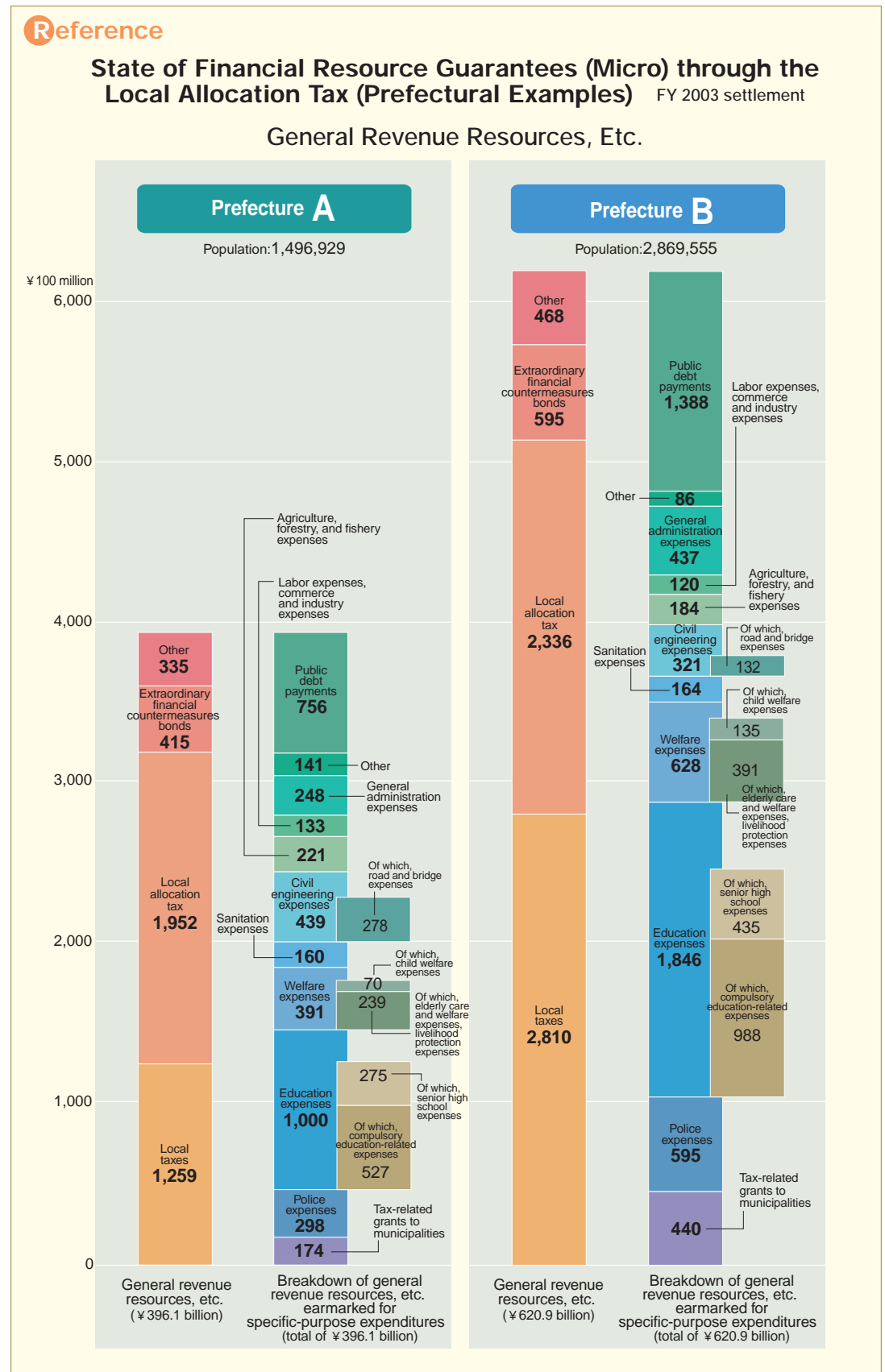
Index of Per Capita Revenue from Two Corporate Taxes and the Local Consumption Tax (After Settlement)

(with national average as 100; FY 2003)



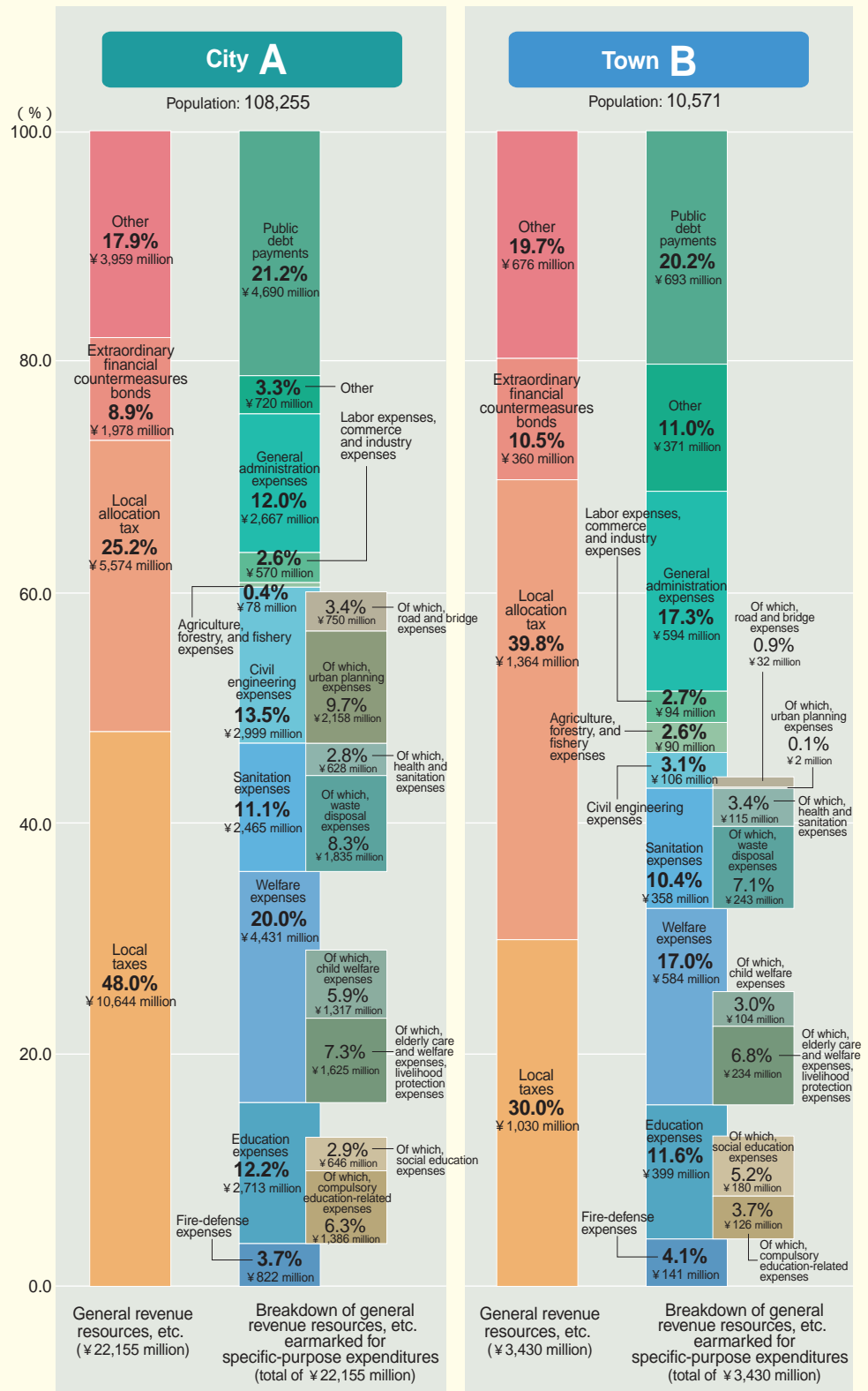
Local Allocation Tax

The local allocation tax fulfills an extremely important role in view of the fact that there are differences in economic strength and financial strength among the regions and that in Japan, with regard to a large part of domestic administrative affairs, local governments are required through legislation, etc. to ensure a certain administrative level in the regions.



State of Financial Resource Guarantees (Micro) through the Local Allocation Tax (Municipal Examples) FY 2003 settlement

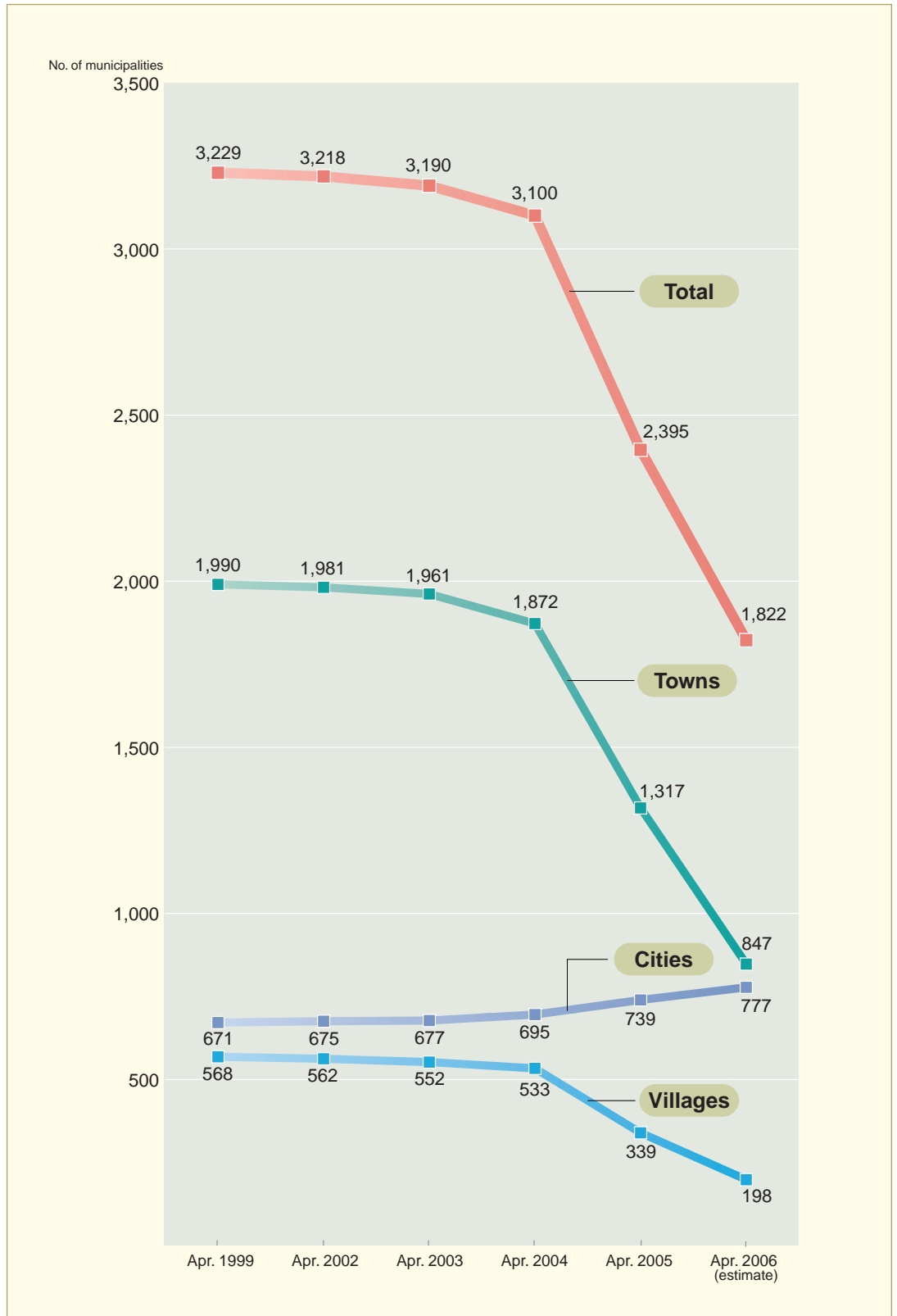
General Revenue Resources, Etc.



3 Promotion of Municipal Mergers

As the role of the municipality becomes increasingly important amid the advance of decentralization, in order to strengthen the administrative and financial bases of municipalities and to maintain and improve the administrative services of municipalities even in the present condition of severe fiscal conditions both centrally and locally, it is necessary to expand administrative scale and efficiency through municipal mergers.

State of Progress of Municipal Mergers



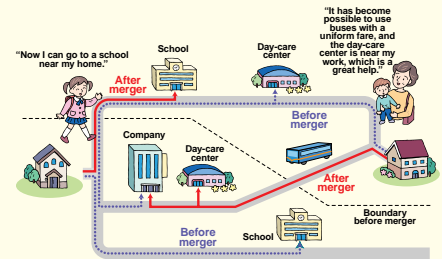
What are the advantages of

1. Improvement in the convenience of residents

If a merger is implemented, it becomes possible for residents to use public facilities and services beyond the borders of the former municipalities, making life becomes even more convenient.

Ex.

In Niigata City, after the merger it has become possible to go beyond municipal boundaries and make use of the vacancies in child day-care centers.

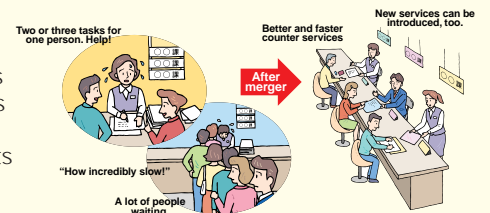


2. Diversification and upgrading of administrative services

Through the establishment of specialized organizations and staff, which had been difficult to implement before, it becomes possible to provide more specialized and high-level administrative services.

Ex.

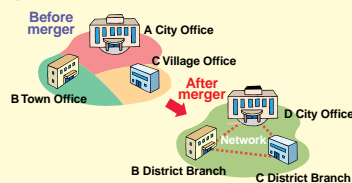
In Asagiri Town in Kumamoto Prefecture, there was an increase in the number of staff with qualifications as public health doctors after the merger, so it has become possible to organize vaccinations for infants and health courses for adults, which previously had almost not been implemented at all.



Are there any disadvantages?

Q Won't the municipal office be farther away for some people?

A After a merger, the old city, town, or village offices can still be used as branches or outposts of the new municipal office. In addition, a law has been enacted to ensure that certain specific administrative business for which there is much local need, such as the issue of residence certificates, can be handled by post offices, which have deep roots in the local community. Furthermore, with the development of information communication technology, the government plans to make it possible for people to submit online applications and so on without even leaving them home, so in the not too distant future we are going to have a society in which distance is no longer a problem.



Q Won't it become more difficult for residents to make their voices heard?

A As well as things like local public meetings and local administration monitors that have existed before the merger, district councils will be established in the former municipal localities after the merger so that the wishes of residents can be taken into consideration. Also, the government is providing support for community-development efforts with the independent participation of residents, for example in elementary school zones. In addition, arrangements for information disclosure and accountability will be strengthened, and new forms of participation by residents will become possible through, for example, utilization of the Internet, which has interactive functions.



C District Council



B District Council

Q Won't there be a deterioration in service?

A Before a merger, there might have been differences between the municipalities concerned in terms of the level of services to residents, rates for using facilities, fees, and so on. The settlement of such problems will be decided through consultations between the municipalities concerned before the merger. The usual approach is to coordinate such things as the level of services and the burden in a manner that is acceptable to residents by increasing the efficiency of administrative processing and so on. In addition, legislation has been implemented so that the burden on residents does not increase suddenly as the result of a merger.

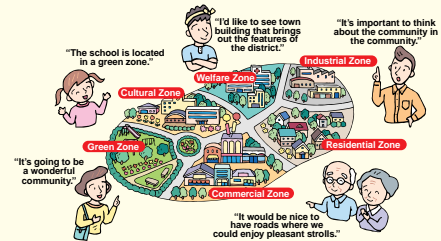


municipal merger?

3. Wide-area community development

It becomes possible to implement more effective community development from a wide-area perspective, including the construction of roads and public facilities, land use, and zoning that takes advantage of local characteristics.

Ex.
In Mito City, regarding housing estates, land readjustment projects, industrial estate readjustment projects, and so on, integrated land use from a wide perspective has become possible.



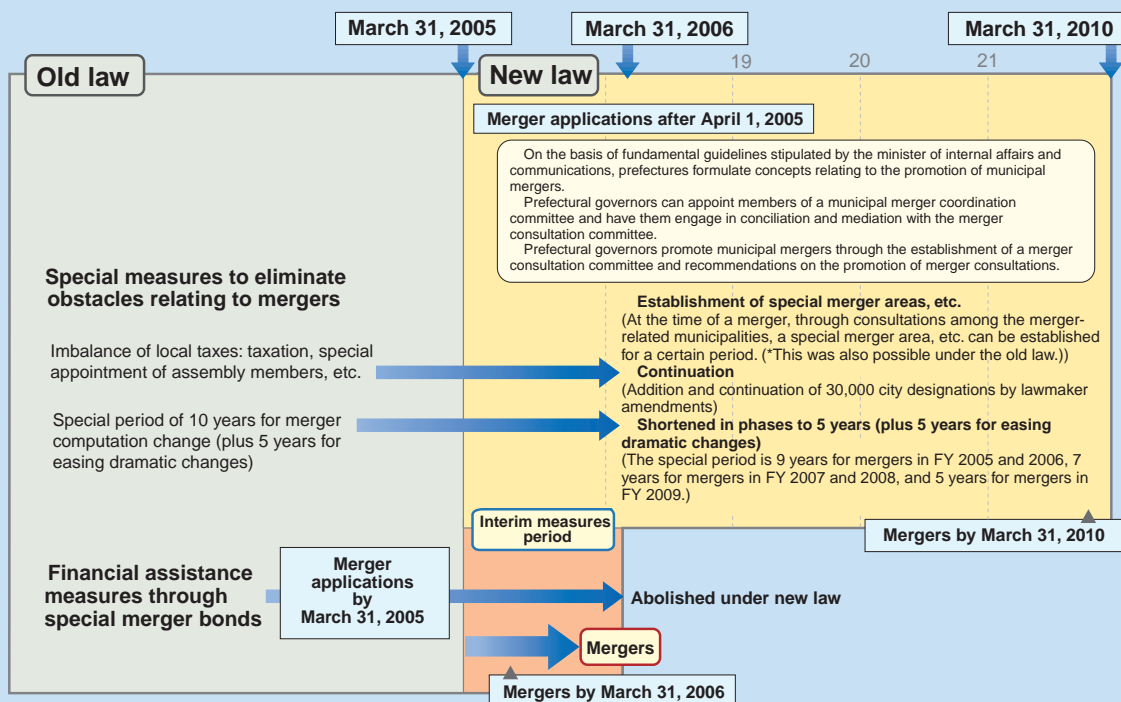
4. Greater administrative and financial efficiency

Greater administrative and financial efficiency becomes possible after a merger by bringing together the work and business that was previously carried out by the separate municipalities and constructing and operating public facilities in a more efficient manner.

Ex.
In Sasayama City, expenses of about ¥200 million a year were saved by cutting the number of assembly members from 57 in the old municipal assemblies to 26.
In Nishitokyo City, as a result of a merger, it has become possible to reduce expenses by an estimated ¥19 billion over 10 years.



Comparison of the Old and New Municipal Merger Laws



White Paper on Local Public Finance 2005

FY 2003 Settlement

Illustrated

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