

4th EASP Conference

The Impact of "Finance Decentralization" on the Social Welfare Expenditure of Local Governments in South Korea

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1. Introduction

In late 20th century, localization based on a decentralization of both authority and responsibility had an effect on the entire world with globalization. In France, a representative centralized country of Europe, a decentralization bill passed their national assembly in 2002 and they expanded local governments' authority and their Financial Independence Ratio, this passed local referendums and unified units of public administration. Japan passed a law of decentralization in 1999 and then transferred center functions to local governments. They revised a total of 475 laws, abrogated Assigned Function and promoted a combination of the local governments.

In the 2003, Participatory Government of South Korea came into power with decentralization and selected decentralization a top priority of the government. They prioritized 'Decentralization and Balanced Regional Growth' for government functions and created a Presidential Committee on

Government Innovation & Decentralization. The central government transferred numbers of a total of 769 businesses to local governments and expanded the financial scale of local governments through an enlargement of the Decentralization Revenue Sharing System, also there was an improvement in the government grant system.

This government decentralization does not exclude social welfare. According to the Korea Ministry of Government Administration and Home Affairs (2006), the government decided upon a 'Government Grant Improvement Plan' and created a "Decentralization Revenue Sharing System" which transfers financial resources to local businesses. A total of 67 government enterprises of social welfare were transferred to local governments. These included 13 elderly welfare services, 24 disabled people welfare services, 4 children welfare services, 7 family welfare services , 6 healthcare services and 11 other services. This is about 45% of the total government businesses which were transferred. According to the revised law on social work, the local governments has the responsibility to set up local social welfare plans and also to created a local social welfare council

This decentralization has increased the responsibility of local governments through transferring of authority and financial responsibility of the central government to local governments and reinforces the autonomy of local governments. Hence, the social welfare responsibility of local governments which are under the influence of this decentralization has

increased and these local governments must take charge as the major provider of social welfare services.

The decentralization of social welfare is divided into two separate opinions. One is from those who wish to increase social welfare. They insist that people who have political power have responsibility regarding welfare policy and they must effectively understand the needs of residents. The other view is a reduction of social welfare. In the case of decentralization, local governments have priority concerning economic growth for financial security reasons. Also, "Decentralization Revenue Sharing System" is unable to meet the needs of residents because of lower expenditures and has difficulties in promoting new social welfare services. The "Decentralization Revenue Sharing System" is a block grant, in contrast with a categorical grant, it can cause welfare differentials between local governments due to different administrators control of their governments' financial conditions.

The purpose of this study is to analyze the change of social welfare finance operations of local governments in South Korea in the year 2005, which is when the "Decentralization Revenue Sharing System" was created and government programs were transferred to local governments.

2. Social Welfare Expenditure of Local Government

We are able to understand the finances of local governments through analyzing the structure of revenue and expenditures. Financial resources for

revenue is gathered by local taxes, central government grants, local bonds and etc and has thus expanded administration expenditures, social development expenditures, local development expenditures, industry & economy expenditures and etc(Kang, 2004).

Social development expenditure is closely related to social welfare expenditure and this expenditure has seen a change in its content. Social development expenditures include welfare services expenditures, health & hygiene expenditures and environment & greens expenditures until 1993.

After 1993, social development expenditures include social security expenditures, education & culture expenditures, health & Amenities and housing & Development of local communities. There was change of titles, but welfare services expenditures or social security expenditures are really social welfare expenditure.

According to table-1, social development expenditure consists of constituted education & culture expenditures, health & amenities expenditures, and social security expenditures. Social security has seen as expansion in general social welfare expenditures, public assistance expenditures and family welfare expenditures.

However, Yoon(2006) has indicated that social development expenditures and social security expenditures categories in expenditure curriculum system are identical in the entire country, but the other categories are decided by the local governments. Hence coverage of expenditure is different between local governments and should agree with

concept of social welfare expenditure and coverage.

<Table-1> Welfare Expenditures Structure of Local Governments

Social Development Expenditure	Education & Culture			
	Health & Amenities			
	Social Security	General Social welfare		
		Public Assistance		Protection of low income residents
		Family Welfare		Family welfare
				Women welfare
			Infants Welfare	
	Housing & Development of Local Community			
General Administration Expenditure				
Economic Development Expenditure				
Civil Defense Expenditure				
Support & Other Expenditures				

Source: Korea Ministry of Government Administration & Home Affairs, Annual Local Expenditure Statistics Report (2006)

Look at the social security expenditures in 2005. The total expenditures are 137,380,241 million won and the social development expenditures are 68,843,882 million won (50.1% of total expenditures). Social security expenditures are 19,033,621 million won (26.7%). Social security expenditure ratio varies among local governments.

<Table-2> Social Development Expenditures of Local Governments

Unit: Million Won

	Total	Metropolitan City, Province	City	County	Autonomous District
Total	137,380,241	67,872,947	37,875,747	19,269,228	12,362,320
Social Development Expenditure	68,843,882	33,688,232	20,993,100	8,279,314	5,883,237
-Education&Culture	10,858,571	7,339,241	2,321,931	995,523	201,877
-Health&Amenities	20,624,803	7,121,318	8,629,724	3,096,375	1,777,386
-Social Security	19,033,621	9,650,995	4,183,928	1,957,992	3,240,706
- Housing & Development of Local Community	18,326,887	9,576,678	5,857,518	2,229,423	663,268

Source: Korea Ministry of Government Administration & Home Affairs, Annual Local Expenditure Statistics Report (2006)

We are able to see a situation of transfer of health & welfare to local businesses in 2006. All of these 76 businesses didn't secure their real expenditures.

<Table-3> Transfer of Health & Welfare to Local Businesses in 2006

Unit: Thousand Won

	Budget formation amounts(B)			Real expenditure (C)	Lack amount (D=B-C)	Secure Ratio (E=B/C)
	Total	Decentralization Revenue	Local amounts			
Total	1,801,981,245	645,105,492	1,156,875,753	1,940,058,629	-38,077,384	92.9%
Elderly welfare	276,628,295	61,467,015	215,161,280	312,173,214	-35,544,919	88.6%
Disables welfare	236,497,461	59,941,697	176,555,764	246,673,359	-10,175,898	95.9%
other welfare	638,458,000	215,841,393	422,616,607	689,388,755	-50,930,755	92.6%
General Demands	27,977,381	5,399,371	2,578,010	30,134,627	-2,157,246	92.8%
Specific Demands	622,420,108	302,456,016	319,964,092	661,688,674	-39,268,566	94.1%

Source: Korea Ministry of Government Administration & Home Affairs, Budget Formation of local transfer businesses in health & welfare(2006)

3. Changing of the Social Welfare Expenditure of Local Governments

1) Economical Points

We are able to analyze the impact of expanding the responsibility of social welfare by using economical points. Local governments make economic growth a policy priority and fulfill local developments. Hence, social welfare policy which hinders economical growth will see a reduction.

Lee & Kim(1992) explain why local governments make economic growth a priority for policy making. First, local governments are unable to secure finances for their administration without local economic growth. Second, economic growth is the best method to gather support from the community. Third, it is a catastrophic result if local businesses go bankrupt, thus increasing unemployment and decreasing land prices because of a slowdown of local economic growth.

However, this welfare policy has exhausted resources for economic growth, obstructing new incoming funds and labor through taxation burdens and interruption of economic growth with (Pauly, 1973; Blank, 1985; Gramlich&Laren, 1984; Bae, 2000).

For these reasons, local governments prefer development policies which create the greatest economic growth and they evade welfare policies that are harmful for economic growth (Kim, 1994).

Kim(1998) explained that this economic point is largely suitable in Korea. Local governments, those with a lack of economic power make an effort for local development and reduce social welfare expenditure.

2) Political Points

The opposition idea' s impact of expanding responsibility on social welfare regarding economical points and political points. Concerning the political points, people who have power must pursue a welfare policy for security of political support though this is harmful for economic growth.

Insistence upon the political points are that local governments receive political demands and pressure from residents, groups and parties and they can' t disregard their demands(Bolye&Jacob, 1982; Lee& Kim, 1992).

Gang(1995) has explained the political points with concerning the concept of welfare demands. Local governments decide their expenditure policy according to the demands of residents. Especially, services for the elderly and children in need because these policies have a noticeable impact on the community and people quickly notice any change in these areas (Kim, 1998).

When considering the political points of the welfare policy of local governments, local autonomy has had an positive influence on the welfare policy of the local government. First, local governments under centralization attach greater importance to political support of the central government than residents do, but after local autonomy was initialized, political support from residents became more important. Second, under centralization, it is

very difficult to cause a policy reaction. Because, there were no local elections and local participation of political parties, local governments were unable to meet the welfare needs of residents. Local autonomy creates a system which the local government is able to reflect upon through local assembly, meetings elections, and parties (Lee & Kim, 1992).

4. Research Methods

1) Research Target & Data collection

This Study analyzed 4 years of expenditures to understand the impact of “finance decentralization.” The data before the "Decentralization Revenue Sharing System" is from the year of 2003 and 2004 and 2005 and 2006 represent the years after the system was implaced.

The research target for local governments is based 16 basic local governments located in Busan, Korea and this includes 15 autonomous districts and 1 county governments data was gathered through statistical materials including “Annual Local Expenditure Statistics Report” , “Budgeting Plans for individual local governments” and “Annual Administration Statistics Reports ” .

2) Variable Definitions

Variables		Survey Index	
Dependent Variable	Ratio of Social Security Expenditure	Social Security expenditure/General Account *100	
Independent Variable	Politics & System	Decentralization Revenue	Before operation=0 After operation =1
		Local Election	There is no election=0 There is an election =1
		Parties of administrator	Hannara=0, No Party=1
	Social & Economy	Ratio of public assistance	Total number of public assistance/Total population *100
	Finance Ability	Financial Independence Ratio	Local tax +Non Tax Revenue / General Account *100
	Incrementalism	Last year' s Ratio of Social Security Expenditure	Social Security expenditure/General Account *100

3) Analysis Method

Pooled regression analysis was used in this study, which is often used in prevalence studies, for analyzing 4 times -series. This study combines time-series data of social welfare expenditure of local government from 2003 to 2006 with crossing data for each year. This combination increases the numbers of cases and we were able to get more significant results.

5. Results

1) Descriptive Analysis

<Table-4 > Descriptive Analysis of Variables

	N	Minimum	Maximum	Mean	Std. Deviation
Ratio of Social Security Expenditures (%)	64	9.60	47.5	29.1	8.8
Ratio of public assistant (%)	64	1.50	11.0	4.0	2.1
Financial Independence Ratio (%)	64	16.30	392.0	39.1	45.5

For the descriptive analysis of independent variables and dependent variables had a mean of 29.1% and the std.deviation is 8.8% in the ratio of social security expenditure. In the case of ratio public assistant, the mean is 4.0%, std.deviation is 2.1% and the financial independence ratio has a mean of 39.1%, std.deviation 45.5%.

To explain by using annual data, the ratio of social security expenditures and ratio of public assistant increased continually, but we couldn' t find any tendency of a financial independence ratio.

<Table-5 > Annual Means of Variables

Variables	Annual means			
	2003	2004	2005	2006
Ratio of Social Security Expenditures (%)	26.3	27.4	28.3	34.3
Ratio of public assistant (%)	3.5	3.5	4.8	5.0
Financial Independence Ratio (%)	33.4	55.9	32.0	27.2

The ratio of social security expenditure means are higher after decentralization revenue occurs and during a local election year when the political party Hannara is in power.

<Table-6 > Decentralization Revenue, Local Election, Parties of Administrator and Ratio of Social Security Expenditure

Variables		N	Ratio of Social Security Expenditure
Decentralization Revenue	Before operation	23	26.8
	After operation	23	31.3
Local Election	There is no election	48	27.3
	There is election	16	34.3
Parties of administrator	Hannara	52	29.7
	No party	12	26.4

2) Regression

This result of pooled regression came about due the impact of independent variables on the ratio of social security expenditure. The fit of

the regression is generally positive, with an adjusted R square of .953 and the F-value is statistically significant at the 99 percent level.

First, we had to figure out the impact of decentralization revenue. An operating decentralization revenue is $-.553$ which has a negative impact on the ratio of social security expenditures compared to the before the operating decentralization revenue took place, but this is not statistically significant. To look at local election variables, the local election year has a 5.061 positive impact on the ratio of social security expenditures when there is no local election, this is statistically significant at the 99 percent level. Also last year's ratio of social security expenditures has a 1.063 positive impact on the ratio of social security expenditure and this is statistically significant at the 99 percent level. However, the party of the local administrator, the ratio of public assistant and the financial independent ratio have no statistically significant impact on the ratio of social security expenditures.

<Table-7 > Result of Regression

Independent Variables	N=64, Dependent Variable=Ratio of social security expenditures
	b
Constant	.340
Decentralization Revenue (After Operation=1)	-.553
Local election (Local election year=1)	5.061***
Party of administrator (No Party=1)	-.015
Ratio of Public Assistant	.623
Financial Independent Ratio	-.002
Last year' s Ratio of social security expenditures	1.063***
F Value	213.6***
Adj R-Square	.953

***p<0.001

6. Conclusion

The Korean government executed financial decentralization in 2005 and started its real decentralization. One of the goals of this study is to figure out the impact of decentralization revenue, local elections, the political party of the administrator, ratio of public assistant, financial independent ratio and last year' s ratio of social security expenditures to the social security expenditure from 2003 to 2006.

Local election and last year' s ratio of social security expenditure had a statistically significant positive impact and decentralization revenue had a negative impact but this was not statistically significant.

These results present to a relation between financial decentralization and social welfare expenditure.

First, financial decentralization had a negative impact on social welfare expenditures. In this study, we were able to figure out a negative correlation, but this was not statistically significant, and this result implies that financial decentralization decreased the will of local governments to spend on welfare.

Second, last year's ratio of social security expenditure saw a positive impact on the ratio of social security expenditure. This result implies that incrementalism is a significant determinant to the budget of local governments.

Third, there was not a good correlation with the welfare demands of local residents, such as the ratio of public assistant, and the ratio of social security expenditures. This implies that local governments are unable to react to the welfare demands of residents and they do not have the political structure for reacting to those demands.

However this study has a few limits. The total numbers of cases are just 65, one can not exclude the central government's part in social security expenditures and further analysis with more precise independent variables is needed.

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