

JAPAN

UNITARY COUNTRY

BASIC SOCIO-ECONOMIC INDICATORS

INCOME GROUP: HIGH INCOME

LOCAL CURRENCY: JAPANESE YEN (JPY)

POPULATION AND GEOGRAPHY

Area: 377 692 km²
Population: 126.728 million inhabitants (2017), i.e. -0.1% per year (2010-2015)
Density: 335 inhabitants / km²
Urban population: 91.5% of national population
Urban population growth: -0.1% (2017 vs 2016)
Capital city: Tokyo (29.6% of national population)

ECONOMIC DATA

GDP: 5 487.2 billion (current PPP international dollars), i.e. 43 279 dollars per inhabitant (2017)
Real GDP growth: 1.7% (2017 vs 2016)
Unemployment rate: 2.8% (2017)
Foreign direct investment, net inflows (FDI): 18 837.5 (BoP, current USD millions, 2017)
Gross Fixed Capital Formation (GFCF): 23.5% of GDP (2016)
HDI: 0.909 (very high), rank 19 (2017)

MAIN FEATURES OF THE MULTI-LEVEL GOVERNANCE FRAMEWORK

Japan is a constitutional monarchy and a parliamentary democracy. Japan's constitution was promulgated in 1946 and came into force in 1947. Legislative power is vested in the National Diet (*Kokkai*), a bicameral parliament composed of the House of Councillors (upper house) and the House of Representatives (lower house), whose members are directly elected by the people, for respectively six-year terms and four-year terms. Three-fifths of the members of the upper house are elected from the prefectural constituencies. The Head of Government, the Prime Minister, is elected by members of the Diet, and the Head of State is the Emperor.

The 1947 constitution established the principle of local autonomy for both residents and local public entities (Chapter 8, Art. 92) and conferred administrative power on local governments (Art. 94). The relation between the various levels of governments is stipulated in the 1947 Local Autonomy Law, which came into effect concurrently with the Constitution. Various laws relating to local autonomy have been enacted such as the Local Public Service Law, the Public Offices Election Law, the Local Finance Law, and the Local Tax Law.

Each local government has its own assembly, with members directly elected by local residents for four-years. Local assemblies have authority to approve budgets and to establish ordinances within law. In addition, administrative committees are established in education, public safety, etc. Prefectures are administratively headed by governors (*chiji*), while cities, towns, and villages are headed by mayors.

In Japan, the push for decentralisation started during the post-World War II period, and was viewed as a means of achieving more democratic political outcomes. The promotion of a democratic system of local government was part of the national agenda. However, the model of central-local relations put in place remained quite centralised in practice, based on the agency-assigned function system. In the 1990s, an ambitious decentralisation programme was launched, encompassing changes to local governments' functions, an increase in local authorities' autonomy, a revision of local governments' financing, and a territorial reform based on municipal amalgamations.

This process was carried out through several steps over a long period, with the support of a Decentralisation Promotion Committee set up in 1995. The first "Decentralisation Promotion Reform" (1995-2001) led to the adoption of the Omnibus Decentralisation law in 2000 - the cornerstone of the new wave of decentralisation in Japan. This law was followed by the Trinity Reform in 2004-06, which laid out the financial component of the decentralisation reform. In 2006, the Second Decentralisation Promotion Reform was launched. It supplemented the first reform and aimed at reaching similar objectives: granting further authority to local governments and rationalising their functions; rationalising the power of central government on local authorities; and consolidating local administrative systems through municipal mergers. It also considered reforming the regional administration of the central government. New sets of recommendations led to the adoption of a new set of bills, in 2008 and 2009. In parallel, reform of the prefectural level and the creation of a "*Doshusei*" Regional System were considered but have not been implemented since. Further decentralisation reforms are still on the agenda as SNGs still have limited autonomy, in particular, in relation to spending and revenue.

TERRITORIAL ORGANISATION

2018	MUNICIPAL LEVEL	INTERMEDIATE LEVEL	REGIONAL OR STATE LEVEL	TOTAL NUMBER OF SNGS
	1 718 municipalities (<i>shichouson</i>) and 23 special wards within Tokyo		47 prefectures (<i>todofuken</i>)	
	Average municipal size: 72 790 inhabitants			
	1 741		47	1 788

OVERALL DESCRIPTION. Japan is a unitary country with two tiers of local governments, prefectures and municipalities, with no hierarchical link. They are specified in the Local Autonomy Law as the two basic types of local authorities in Japan.

PREFECTURAL LEVEL. The prefectural level of government in Japan consists of one metropolitan district (Tokyo), two urban prefectures (Kyoto and Osaka), one district (Hokkaidō), and rural prefectures. Regionalisation plans have been considered for decades, and new regionalisation projects were proposed in the 2000s, under the term "*Doshusei*", but reorganisation has not been scheduled yet. As stipulated by the National Spatial Planning Act, regions are responsible for drawing their own regional plans, in coherence with the National Spatial Strategies elaborated at national level for a ten-year period.

MUNICIPAL LEVEL. Municipalities form the basic level of government in Japan. The municipalities are not uniform, being subdivided, in descending order, into 20 designated cities, 58 core cities, 27 “national enforcement time special cities”, and 685 other cities. They also include 745 towns (*machi*) and 183 villages (*mura*). All these local government units have their own mayors, or chiefs, and assemblies. Cities with a population above 500 000 inhabitants can be given the status of designated cities (*shitei toshi*). Designated cities are divided into wards (*ku*), each of which has a chief and an assembly, the former being nominated by the mayor and the latter elected by the residents. According to the Local Autonomy Law, the 20 designated cities and the 23 Metropolitan Tokyo wards have a special status based on their population size, and they have more administrative and fiscal autonomy than the other municipalities.

Several waves of mergers have drastically reduced the number of municipalities, from 9 868 in 1953 to 1 718 today. The first wave was “*Shōwa no Daigapperi*” which reduced the number of municipalities from 9 868 in 1953 to 3 472 in 1961. The objective was to reduce the number of municipalities to one-third of the original number and to attain a minimum target size of 8 000 inhabitants per municipality. A second wave (*Heisei no Gapperi*) took place from 1999 until 2010, which reduced the number of municipalities from 3 232 to 1 727, based on voluntary merger policy supported by a mixture of incentives. Inter-municipal cooperation is increasingly promoted, in particular through voluntary partnership agreements that are established under the Local Autonomy Act.

As a result of these amalgamations, municipalities have grown in size, and as of 2016, 59% of Japanese municipalities had more than 20 000 inhabitants and only 13% fewer than 5 000 inhabitants, with an average municipal size of 72 831 inhabitants (vs 9 700 in the OECD on average) and a median size of 31 300 inhabitants.

SUBNATIONAL GOVERNMENT RESPONSIBILITIES

Local governments in Japan have a large array of responsibilities, with an asymmetrical decentralisation system at regional and local levels. Despite no clear-cut separation, the prefectures have considerably stronger administrative powers than the municipalities. However, in many of these spheres, the central legislation often establishes uniform policies and standards for the whole country. The 1999 Omnibus Decentralisation Act abolished the former system of delegated functions (“agency-delegated functions” in which regional governors and mayors serve as regional representatives of the central government), which was in place under the 1947 Law on Local Autonomy. It increased significantly subnational autonomy and responsibilities, by revising the 475 previous laws. Overall, SNGs have both “local own functions” and “statutory entrusted functions”, which remain under the supervision of the central government. According to the Local Autonomy Law, local governments are responsible for a range of functions in the fields of economic development, public infrastructure, public housing, education, social assistance policies and public health.

In addition, a network of 8 398 local public companies are active in public service delivery, especially in the sewerage (43.2% of all local public companies), water supply (22.9%) and hospitals (7.5%).

MAIN RESPONSIBILITY SECTORS AND SUB-SECTORS

	PREFECTURES	MUNICIPAL LEVEL
1. General public services	Communication and coordination affairs relating to municipalities	Internal administration; Family registers; Resident registrations
2. Public order and safety	Police	Fire fighting
3. Economic affairs / transports	Economic development; Public infrastructure; Prefectural roads; National highways; Harbours; Agriculture; Employment	Local roads; Local harbours
4. Environmental protection	Forest and river conservation; Environmental protection	Sewage; Waste disposal; Parks
5. Housing and community amenities	Public housing	Urban planning; Public housing; Water supply
6. Health	Public health centres	Nursing
7. Recreation, culture & religion		Leisure services; Sport; Libraries
8. Education	Upper secondary schools	Pre-schools; Elementary schools; Lower secondary schools
9. Social protection	Social assistance policies	Child welfare; Elderly; National health insurance; Ageing insurance

SUBNATIONAL GOVERNMENT FINANCE

Scope of fiscal data: : Cabinet-Order Designated Cities, cities, towns, villages and special wards at the municipal level; Tokyo metropolitan district, Kyoto and Osaka urban prefectures, Hokkaido district, and rural prefectures at the prefectural level.

SNA 2008

Availability of fiscal data:
High

Quality/reliability of fiscal data :
High

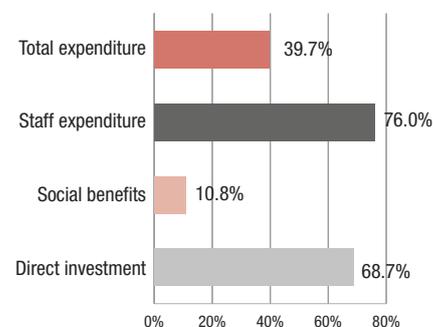
GENERAL INTRODUCTION. As a unitary country, public spending in Japan tends to be very decentralised, with shares of SNG spending in GDP and in overall public spending significantly above the OECD average. The Trinity Reform, from 2002 to 2006, laid the financial basis of the decentralisation reform, by setting up three major components: the creation of a tax-sharing system between the national and subnational level, a reform of the equalisation tax (local allocation tax) and the abolishment of several national earmarked grants. “Basic Policy on Economic and Fiscal Management and Reform 2015” tended to strengthen local fiscal discipline, stating that “Local government expenditures shall also be controlled in line with the efforts by the central government”. However, the level of decentralisation should not be overstated as SNGs often remain “paying agents” on behalf of the central government, implementing policies designed by the different ministries.

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SUBNATIONAL GOVERNMENT EXPENDITURE BY ECONOMIC CLASSIFICATION

2016	DOLLARS PPP / INH.	% GDP	% SNG EXPENDITURE	% GENERAL GOVERNMENT EXPENDITURE (SAME EXPENDITURE CATEGORY)
Total expenditure	6 561	15.5%	100%	
Incl. current expenditure	5 181	12.3%	79.0%	
Staff expenditure	1 761	4.2%	26.8%	
Intermediate consumption	1 005	2.4%	15.3%	
Social expenditure	972	2.3%	14.8%	
Subsidies and current transfers	1 318	3.1%	20.1%	
Financial charges	121	0.3%	1.8%	
Others	4	0.0%	0.1%	
Incl. capital expenditure	1 380	3.3%	21.0%	
Capital transfers	268	0.6%	4.1%	
Direct investment (or GFCF)	1 112	2.6%	16.9%	

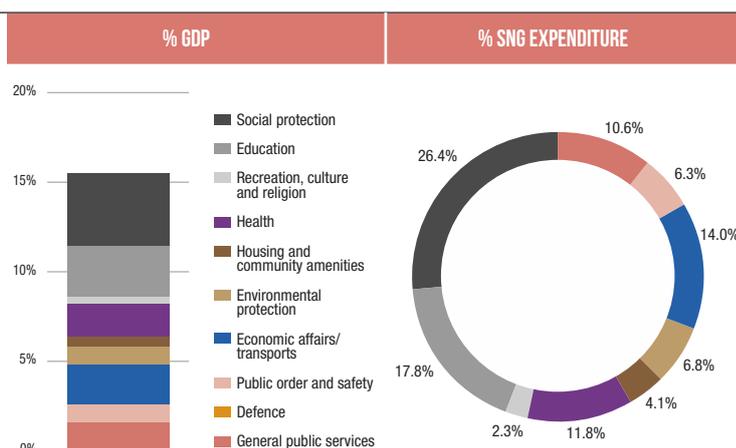


EXPENDITURE. In Japan, share of SNGs in public expenditure was in line with the OECD average in 2016. Prefectures and municipalities are each responsible for approximately half of total SNG spending. Japanese SNG share in public staff spending is particularly high compared to the OECD average (62.9% for all OECD countries and 43% for OECD unitary countries).

DIRECT INVESTMENT. Japanese local governments play a crucial role in public investment, as investment accounted for 17% of their budget in 2016, as compared to 10.7% on average in the OECD. The SNG share in public investment is noteworthy, compared to the OECD average (59%) as well as the weight in GDP, representing 2.6% of GDP vs 1.7% in the OECD. Most subnational investments in Japan are dedicated to economic affairs, as local governments are responsible for roads, bridges and harbours, among others. Indeed, infrastructure such as roads, waterfronts, sewage systems, and sea ports, which were developed during the high growth era (1955–1973), are rapidly aging. Other large categories of investment spending include environmental protection, education and housing. Yet in their mission, SNGs are often limited to a role of implementing agents of the national governments on the one hand and, on the other hand, constrained by a tight fiscal situation to focus more on projects with high returns. They are guided by Japan's National Spatial Strategy (NSS) in the areas of integrated territorial and infrastructure development. As an example of government financial support, based on Act on Development of Infrastructures for Wide-Area Revitalization, the Ministry of Land, Infrastructure and Tourism (MLIT) grants subsidies to SNG to form self-reliant wide-area blocks. SNGs create wide-area regional revitalization infrastructures development plans and promote infrastructure development to revitalize the regions through buoyant human and material traffic.

SUBNATIONAL GOVERNMENT EXPENDITURE BY FUNCTIONAL CLASSIFICATION – COFOG

Subnational governments dominate general government expenditure in most major areas in Japan, such as social protection (child, elderly, public assistance and disaster relief), education (primary, secondary and high school), economic affairs (notably transport infrastructure) and general public services. Municipalities' prime spending areas are social welfare, general public services and economic affairs/transport. On the other hand, prefectures spend more on education and economic affairs. In addition, SNGs are responsible for the large majority of total public spending in the areas of environmental protection, recreation and culture as well as housing and community amenities.



SUBNATIONAL GOVERNMENT REVENUE BY CATEGORY

2016	DOLLARS PPP / INH.	% GDP	% GENERAL GOVERNMENT REVENUE (SAME REVENUE CATEGORY)	% SNG REVENUE
Total revenue	6 562	15.5%	43.5%	
Tax revenue	3 112	7.4%	39.9%	47.4%
Grants and subsidies	2 838	6.7%		43.3%
Tariffs and fees	407	1.0%		6.2%
Property income	46	0.1%		0.7%
Other revenues	158	0.4%		2.4%

OVERALL DESCRIPTION. SNGs still depend on central government transfers for 43% of their revenue, based on a tax sharing system established by the 2004 Trinity Reform, which is above the OECD average (37.2% in 2016). However, the share of taxes in SNG funding has increased significantly in recent years thanks to fiscal reforms (+3 percentage points since 2013) to become the first source of SNG revenues in 2016. Reforms also tend to reduce the share of earmarked grants, providing more leeway to SNGs. The degree of fiscal dependence of Japanese local governments on grants and subsidies varies across prefectures and municipalities.

TAX REVENUE. The share of SNG tax revenue in GDP and public tax revenue in Japan is higher than the OECD average in 2016 (7.1% of GDP and 31.9% of public tax revenue).

The Local Tax Law provides for 12 types of prefecture taxes and 13 types of municipal tax. Moreover, local governments can introduce new, non-statutory taxes, which are not stipulated in the Local Tax Law if they have specific needs. Yet, they represent a very small share of their total tax revenues. As of 2014, tax revenue accounted for 34% of prefectures' revenues and 33% of municipal revenue. In 2016, a tax reform was launched to correct the uneven distribution in tax sources across regions and the uneven distribution of local government corporation taxes, intended to minimise disparities in financial strength.

The primary SNG tax is by far the resident tax which is a combined prefectural and municipal tax calculated on the basis of 10% of the income earned in the previous year, regardless of the amount of income. It is levied both on individuals and businesses, and in 2016, both taxes combined represented around 40% of SNG tax revenue. This system enables areas with a high concentration of businesses and high income, such as Metropolitan Tokyo, to be almost self-financing. By contrast, most of the prefectures from more isolated areas on the Japan Sea coast cannot rely only on this source of revenue.

In addition to the resident tax, prefectures also perceive local taxes including an enterprise tax (around 19% of prefectures' revenue in 2014), a local consumption tax (19%) and an automobile tax (10%). Other taxes include light-oil delivery tax, prefectural tobacco tax, etc. For municipalities, the second highest tax is the fixed asset tax (property tax on land and buildings, accounting for approximately 42% of municipal revenue in 2014), followed by a city planning tax (6%), and a municipal tobacco tax (5%).

Overall, the income tax was the primary source of tax revenue in 2016, accounting for 32% of SNG tax revenue, 15% of SNG revenue (i.e. 2.4% of GDP). The recurrent property tax was the second most important source, representing 26.4% of SNG tax revenue and 12.5% of SNG revenue, amounting to 1.9% of GDP, a level which is well above the OECD average (1.1% of GDP in 2016). The third biggest source was the business tax, amounting to 17.5% of SNG revenue, followed by the consumption tax.

GRANTS AND SUBSIDIES. Japan's intergovernmental transfer system aims at filling the gap between SNG own-source resources and their spending responsibilities, as well as alleviating fiscal inequalities among local governments.

Major central government transfers are based on the sharing of national taxes. The most important one is the Local Allocation Tax Grant (LAT), based on national tax revenues from the five major national taxes (33.1% of PIT and CIT, 22.3% of the consumption tax, 50% of the liquor tax and all local corporate tax revenues), SNGs receive between 25% and 34% of the receipts. LAT allocation is determined by local fiscal capacity and expenditure needs, and therefore no distribution is made to local revenue with base revenues exceeding their financial needs. The LAT is broken down into an "ordinary" LAT (94% of funds) and a "special" LAT (6%), dedicated to extraordinary expenses such as damages from natural disasters. For two decades, LAT funding itself has been an issue as the grant's base revenue has been inadequate to cover the local financial need. It still requires topping up from other funding sources, including the general account of the national government's budget, and debt financing co-financed at 50% by local governments. Another transfer is the Local Transfer Tax (LTT), which is made up of the local gasoline transfer tax and other national taxes redistributed to SNGs as a general grant.

Other transfers include, for example, funds for local revitalisation and subsidies for the Overcoming Population Decline and Revitalizing the Local Economy, and national treasury disbursements. In 2016, around 17% of all grants was for capital expenditure, a decrease of 6 percentage points since 2013.

OTHER REVENUES. Other revenues include charges and fees, which represent around 6.2% of SNG revenue and, revenues from property (sales of assets, rents, dividends) and social contributions. Japan SNGs are expected to increase their user fees (i.e. for garbage collection, etc.) in the coming years to improve their overall revenue.

■ SUBNATIONAL GOVERNMENT FISCAL RULES AND DEBT

	DOLLARS PPP/INH.	% GDP	% GENERAL GOVERNMENT DEBT	% SNG DEBT
Total outstanding debt	14 340	33.9%	15.3%	100%
Financial debt*	13 613	32.2%	14.9%	94.9%

* Currency and deposits, loans and bonds

FISCAL RULES. The 2009 Act on Assurance of Sound Financial Status of Local Governments established new deficit and debt ratios to monitor the financial solidity of SNGs and strengthen their fiscal discipline. The "Basic Policy on Economic and Fiscal Management and Reform 2018" sets two fiscal consolidation goals for the central and local governments: a primary surplus by FY 2025 and reducing the public debt-to-GDP ratio steadily.

DEBT. SNGs may borrow freely but only to finance capital expenditure ("Golden Rule"). SNG borrowing is very high by international standards, well above OECD averages in terms of GDP (24.5% for all OECD). Yet in contrast with their high share of subnational expenditures, the share of SNG debt in total public debt is lower than the OECD average (20.7% in 2016), which can be explained by the significant level of Japanese public debt, reaching 221.1% of GDP in 2016.

SNG outstanding debt is made up mainly of financial debt (95%), the remaining coming from "other accounts payable". Financial debt is composed of loans (60%) and bonds (40%). Local bonds are funded either on the financial markets, by commercial banks or through the Japan Finance Organisation for Municipalities (JFM), established in 2009. As of 2013, 55% of local bonds were owned by prefectures, against 45% for municipalities. The Ministry of Internal Affairs and Communications drafts every year the Local Government Bond Plan in line with the Fiscal Investment and Loan Program Plan of the Ministry of Finance. The plan includes estimates of bond issuance by type and purpose. A consultation system with the central government replaced a prior approval system in 2006 for the issuance of local bonds. Before debt issuance, prefectures and municipalities must consult respectively with the Minister of Internal Affairs and Communications, and the prefecture governors, to obtain their consent. For those that can issue bonds without consent, the head of the local government must report it to the assembly.



Lead responsible: OECD
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Socio-economic indicators: OECD // World Bank // UNDP // UN Desa // ILO // Statistics Japan.

Fiscal data: OECD National Accounts Statistics // OECD Revenue Statistics // OECD (2018) Subnational Government in OECD countries: key data (brochure and database) // IMF-GFS Office.

Other sources of information: OECD (2017) Multi-level Governance Reforms: Overview of OECD Country Experiences // OECD (2017) Economic survey : Japan // OECD (2016) Territorial Reviews: Japan // Ministry of Finance (2016) Japan : Fiscal discipline of local governments Japanese // Council of Local Authorities for International Relations (2016) Local Government in Japan // Ministry of Internal Affairs and Communications (2015) White Paper on Local Public Finance // OECD (2015) The State of Public Finances 2015: Strategies for Budgetary Consolidation and Reform in OECD Countries // Tokyo Metropolitan Government (2013), Tokyo's Financial System // UN-Habitat (2012) Fiscal decentralisation in Japan.