Welfare Decentralization in Korea: In Between Two Models of Unitarism and Federalism*

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1 Introduction

Since the late 1990s, the size of social expenditure in Korea has increased quite significantly. In 1995, the share of social expenditures in GDP was 3.3 percent but it has risen to 7.6 percent in 2007. Compared to OECD countries, the size of social expenditures in Korea is very low. However, with a rapid aging and growing political demand for social expenditures, it is expected to grow to a much higher level.

In dealing with the mounting fiscal burden associated with social expenditures, the central government has decentralized its responsibilities and fiscal burdens of many social welfare programs to local governments. The mechanism of "welfare decentralization" was to include partially funded mandates in the system of specific grants and to introduce categorical block grants with a limited amount of compensation for new expenditure responsibilities delegated to local governments.

This process has generated many controversies and has been strongly criticized by local governments. The central government, however, argues that it is a necessary measure since the central government shares its tax revenue with local governments to a significant degree through tax sharing.[1]

The main reason for these controversies and conflicts over welfare decentralization in Korea is in the weakness of fiscal institutions that deal with intergovernmental fiscal relations. In particular, Korea's fiscal institutions do not possess the characteristics of cooperative fiscal federalism found in unitary countries such as the Nordic countries, nor an intergovernmental forum or agency that facilitates dialogues and negotiations between the central and local governments found in many regional and federal countries. At a deeper level, therefore, the problem of Korea's fiscal decentralization model is that it is unable to identify itself as either a unitary or federal/regional country. Unless these fundamental issues are resolved, Korea is likely to stuck between unitarism and federalism, and lack the ability to respond dynamically to rapidly changing fiscal environments.

This paper is organized as follows. An overview of local public finance in Korea is given in section 2. In section 3, the recent development of welfare decentralization is discussed. In

[1] About 31 percent of the central government's tax revenue is transferred to the local public sector by a system of tax sharing.

section 4, the current model of fiscal decentralization in Korea is critically evaluated. Section 5 concludes.

2 Overview of local public finance in Korea

The size of the local public sector in 2010 was 139.9 trillion won, approximately 12 percent of GDP.[2] Out of this total budget, 79.4 trillion won consists of own sources, and 55.25 trillion won of intergovernmental grants. The size of local debt in Korea is negligible at about 5.17 trillion won in 2010. On average, the share of local governments' own-source revenue is about 56 percent, and 44 percent comes from intergovernmental grants.

Table 1: Revenue of local governments (trillion won)

	2008	2009	2010
Total	125	137.5	139.9
Own Revenue	73.65	80.84	79.43
(share)	(58.9)	(58.8)	(56.8)
Transfers	47.82	53.01	55.25
(share)	(38.3)	(38.6)	(39.5)
Local Debt	3.5	3.69	5.2
(share)	(2.8)	(2.7)	(3.7)

source: Ministry of Public Administration and Security.

The size of total local expenditures in 2010 was 123.5 trillion won, a little bit lower than total local revenues due to carry-overs. Korea has three government accounts: central government account, local governments account, and local education account. Local education offices, independent local bodies separate from local governments, do not collect taxes but receive transfers from local governments (Local Education Tax) and the central government's transfers (general grants).[3] The system of general grants in Korea is based on a tax sharing scheme by which 19.24 percent of "domestic tax" is allocated to local governments and another 20.27 percent to local education offices. All together, the size of general grants is about 31.3 percent of the central government's tax revenue.[4] As a result of the large amount of intergovernmental transfers, the size of local expenditures is larger than central government expenditure, at 110.5

[2]With an exchange rate of 1,100 won to the dollar, the size of the local public sector in 2010 was about 127.2 billion dollars. The GDP in 2010 was about 1172.8 trillion won.

[3]In 2010, Local Education Tax revenue was 4.54 trillion won.

[4]In 2010, the revenue of "domestic tax" was 140.9 trillion won and that of the national taxes 177.7 trillion Won.

trillion won in 2010. As Table 2 shows, the share of local expenditures out of total government expenditures was 35.9 percent in 2005 but has increased to 45.1 percent in 2010, mainly due to rising intergovernmental grants.

Table 2: Expenditures of the public sector (trillion won)

	2005	2006	2007	2008	2009	2010
Central	105.45	105.91	108.55	111.13	104.85	110.55
(share)	(50.5)	(48.4)	(47.2)	(46.1)	(42.3)	(40.3)
Local	74.88	82.64	88.89	97.61	108.05	123.52
(share)	(35.9)	(37.7)	(38.6)	(40.5)	(43.6)	(45.1)
Education	28.32	30.45	32.76	32.47	35.08	39.99
(share)	(13.6)	(13.9)	(14.2)	(13.4)	(14.1)	(14.6)

source: Ministry of Public Administration and Security.

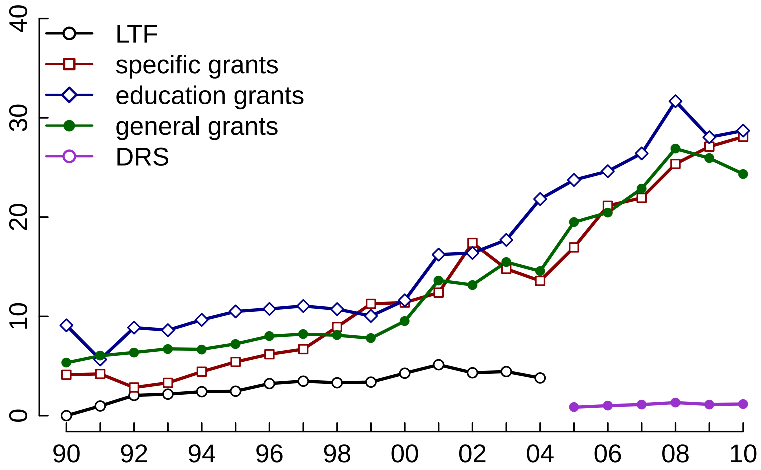
Apart from general grants, specific grants play a significant role in Korea's system of intergovernmental grants. Currently its size is as large as those of general grants. In 1990s, several specific grants, mostly those for local roads and environmental facilities, were consolidated in a kind of block grants named Local Transfer Fund (LTF). It existed for fourteen years and then absorbed into general grants in 2005. In the 2000s, another effort was made to reduce the size of specific grants. More than one hundred small-sized specific grants, this time mostly welfare facilities for the elderly and children, were consolidated to create a block grant named Decentralization Revenue Sharing (DRS). It was scheduled to be absorbed into general grants, but it has been delayed to 2012.

During the 1990s, the size of specific grants was generally smaller than those of general grants. However, due to a rapid increase in welfare programs delivered by local governments through the system of specific grants, its size has grown to be at least as large as general grants.[5]

Recent trend of welfare decentralization in Korea shows that the fiscal burden of local governments is increasing for two reason. Firstly, the size of welfare programs delegated to local governments is increasing. Secondly, matching rates of the central government is decreasing as well. In 2007, matching rates for specific grants provided by the Ministry of Health & Welfare was 73.6 percent. However, it has steadily decreased to 68.7 percent in 2011. In terms of absolute size, the fiscal burden of local governments has increased by 2.4 times, while that of the

[5]In case DRS is counted as general grants, the size of specific grants is smaller than that of general grants. However this is a very controversial issue as will be discussed in next sections. In figure 1, a sharp decrease in general grants and education grants in 2008 was due a major tax cut in 2008.

Figure 1: Trend of intergovernmental transfers (trillion won)



central government by 1.9 times during the said period. This trend has been criticized by local governments because they recognize that Korea is only at a beginning stage of rapidly increasing social expenditures. They are also concerned that there is a good chance that the current trend of decreasing matching rates of the central government continues in the future. In next sections, these controversies of welfare decentralization will be discussed in more details.

Table 3: Trend of budgets of the Ministry Welfare & Health (trillion won, %)

	2007	2008	2009	2010	2011	growth rate
Total amount	11.3	15.9	19.3	19.2	20.5	16.1
Grants to LG	7.8 (73.6)	11.7 (69.6)	13.9 (69.5)	13.7 (68.8)	14.7 (68.7)	17.2
Matching of LG	2.8 (26.4)	5.1 (30.4)	6.1 (30.5)	6.2 (31.2)	6.7 (31.3)	24.4

source: Ministry of Health & Welfare.

3 Welfare decentralization: recent developments

The structure of public finance in Korea is quite different from that of European countries. The share of tax revenue, including social securities, as a percentage of GDP, is less than 30 percent in Korea, while that of most European countries exceeds 40 percent.[6] As a consequence, the size of public expenditure in Korea is much smaller compared to most European countries. In

[6] As of 2009, the shares of tax revenue as a percentage of GDP in Korea, Denmark, Sweden, France, Germany, Italy were respectively 26.5%, 48.2%, 47.3%, 43.2%, 37.0%, and 43.3% (OECD, Revenue Statistics, 2010).

addition to that, the share of social protection in public expenditure in Korea is also very small at less than 4 percent of GDP.[7] Altogether, the scope of welfare decentralization is limited in Korea compared to European countries in which many welfare programs are provided by local governments.

However the structure of the public sector in Korea is changing rapidly. The first significant change took place in the late 1990s, when a severe economic crisis hit Korea. In response to the economic crisis, the government enforced harsh policy measures to strengthen market discipline in the financial sector and to achieve more flexibility in the labor market. As a result of structural reform measures, many companies files for bankruptcy and the unemployment rate almost tripled in one year, giving rise to more than one million newly unemployed. The government therefore combined measures for structural reform with those to strengthen the social safety net. In particular, the government introduced new welfare programs and extended old ones to support the unemployed and those who fell into poverty. An important welfare program – National Basic Livelihood Security Program (NBLSP) – a subsidy to the poor, was introduced during this period. The NBLSP replaced the old system to assist the poor with a more flexible criteria and much larger amount of subsidies.

A notable feature of the NBLSP from the perspective of intergovernmental fiscal relations is that it is provided by local governments through conditional matching grants (National Subsidy), of which its conditions and benefit levels are all determined by the central government. As a matching grant, the central government's contribution to the NBLSP is matched by local governments with matching rates that vary depending on the fiscal capacities of local governments. In a strict sense, however, the total amount of the NBLSP is not determined by matching grants because the number of beneficiaries and the amount of co-payments by local governments are all fixed by law. Therefore it is a partially funded mandate.

The increasing trend of social expenditures has been reinforced in the 2000s. One of the reasons was due to a left-wing government taking power in 2002. But more fundamentally Korea is rapidly developing into an aging society[8] and currently has the lowest fertility rate among

[7] As of 2006, the shares of social protection as a percentage of GDP in Korea, Denmark, Sweden, France, Germany, Italy were respectively 3.7%, 21.8%, 22.7%, 22.3%, 21.2%, and 18.2% (OECD, Government at a Glance, 2010).

[8] The percentage of population aged 65 years and over in Korea has grown from 5.8 in 1995 to 11.3 in 2010. It is expected to reach 23.4 in 2030, among the highest in OECD countries.

OECD countries.[9] As a result, many types of welfare programs for the elderly and children have been introduced in the 2000s. As in the case of the NBLSP, most of these programs are provided by local governments with recipient criteria and the amount of benefits determined by law. Therefore, to the viewpoint of local governments, welfare decentralization in Korea has been proceeded mainly in the form of partially funded or unfunded mandates.

Another notable development in the early 2000s was the then president's ambition for a decentralized country. Decentralization was one of his biggest political agendas and therefore "fiscal decentralization" was a consequential policy priority to achieve a decentralized country. The trend of increasing welfare expenditures and the political movement for decentralization gave rise to, from a theoretical point of view, a fundamentally difficult question as to how we provide 'merit goods' in a decentralized setting. In practice, however, such a theoretical question didn't prevent "welfare decentralization reform" from taking place.

According to article 9 of the Local Autonomy Act, local governments are responsible for providing "public services that enhance residents' welfare" as well as several other categories such as local industrial development of agriculture and commerce; public services that promote education and culture; and environmental protection. These public services are referred to as "inherent functions" of local governments. More detailed examples are provided in the Local Autonomy Act under each broad category of inherent local functions, . As for category 2 – public services that enhance residents' welfare – welfare facilities, public hospital, support for seniors, low-income, and disabled are listed as examples. In other categories of inherent local functions, small&medium sized business, housing, local economy, and elementary and junior high schools are listed.

Obviously, the definition of local public services in the Local Autonomy Act is too broad to act as a practical guide for expenditure assignment between central and local governments. In reality, public sectors such as welfare, education, small-medium size business, and housing are all major responsibilities of the central government in Korea. However, the Local Autonomy Act – as a legal document – played an important role as a guideline during the debates on fiscal decentralization that took place during the 2000s. As a result, many small-sized welfare programs – mostly subsidies for welfare facilities for the poor, disabled, elderly and children –

[9] As of 2009, the fertility rate in Korea, Japan, Denmark, Sweden, France, Italy, and Germany were respectively 1.15, 1.37, 1.84, 194, 1.99, 1.41, and 1.36 (OECD, Society at a Glance, 2011).

became decentralized. An initial plan was to make local governments exclusively responsible for these “inherent local functions”. But this was met with strong resistance from local governments. As a result, more than one hundred matching grants for welfare facilities were merged into one categorical block grant named Decentralization Revenue Sharing (DRS).

The size of DRS is not large, at about 0.1 percent of GDP, but many controversies arose after its introduction. Local governments are especially critical of DRS. There are two main arguments against this new system. One strand of argument is that redistribution is the the central government’s function, an argument along the line of Musgrave’s famous three branches of state functions. Another strand of argument against DRS accepts the notion that local governments provide redistributive public services, but only under the condition that local governments are guaranteed sufficient fiscal resources required for fulfilling such responsibilities.

There is of course an argument for making local governments more responsible for welfare programs. Among the proponents of the DRS, the Ministry of Finance argues that local governments, unlike the central government, do not sufficiently shift their fiscal resources to social expenditures, a category which is in increasing demand in Korea today. From a theoretical point of view, the change of the expenditure composition of local governments should be determined by the local residents, not by the central government. But, as the Ministry of Finance sees it, the political pressure for more social expenditures is put only on the central government while its tax revenue is shared with local governments. This argument underlines the complicated structure of intergovernmental fiscal relations in Korea. As outlined in section 2, about 31 percent of national tax revenue is distributed in the form of general grants to both local governments and local education offices. Given the low levels of tax burden and social expenditures in Korea, a rise of tax burden is most likely to result from an increased demand for social expenditures. The argument of the MoF is then an increase in the central governments’ tax revenue should either be earmarked for the central government’s social expenditures, or the fiscal burden of social expenditures should be vertically shared either by partially funded mandates, as in the case of the NBLSP, or by insufficiently funded categorical grants, as in the case of the DRS.

The different views among the Ministry of Finance and local governments do not seem to be easily resolved. When the DRS was introduced in 2005, it was scheduled to be absorbed into the system of general grants in 2010. However the plan has been extended to 2012, and it is quite likely that it will be further delayed. As for the partially funded mandates such as the NBSLP and subsidies to the elderly and children, local governments make continuous requests to the central government to either increase the central government's share of the fiscal burden or to abolish the mandates themselves.

4 Assessment

4.1 Mixture of unitarism and federalism

The structure of intergovernmental fiscal relations, as discussed in the previous sections, can be summarized as the result of conflicting forces that exist in the decentralized system in Korea. First of all, Korea is a unitary country by constitution and its people are homogeneous in terms of ethnicity, language, and culture. It is a small country with an area of about 100,000 square kilometers. Therefore, according to the work of Panizza (1999), the degree of fiscal decentralization in Korea should be lower than the average of western European countries.[10] However the share of local tax revenue in Korea is above the average and the share of local expenditure is among the highest in OECD countries.[11] Considering the size of local public sector, Korea is a very much decentralized country.

It is of course not rare to find unitary countries that have large local public sectors. Nordic countries are such examples, where local tax revenue and expenditure shares are among the highest in OECD countries. Compared to Nordic countries, however, Korea has a similar characteristics of a federal or regional country as well. Firstly, its population size of about 50 million is much larger than that of Nordic countries with a population between 5 to 8 million. Among OECD countries, most countries with a population size above 50 million are either federal or regional countries.[12] Secondly, Korea relies heavily on a system of tax sharing for allocating

[10] Panizza (1999) defined the degree of fiscal decentralization as the share of local revenue in the total revenue and ran a regression with explanatory variables such as the level of democracy, country size, ethnicity, and the level of income per capita. As expected, the degree of decentralization is positively related to these variables.

[11] The share of local tax in Korea and OECD average of unitary countries are respectively 22 percent and 16 percent in 2008 (OECD Revenue Statistics, 2009). The share of local expenditure in Korea and OECD average of unitary countries are respectively 55 percent and 30 percent in 2006 (OECD, Government at a Glance, 2009).

[12] Among the large unitary OECD countries, U.K. consists of four devolved countries (England, Scotland, Wales, and Northern Ireland), Spain and Italy are federalized countries. Turkey and Japan are only the other large countries, along with Korea, which are not federal.

tax revenues between central and local governments. In OECD, most federal countries except U.S. and Canada rely on the system of tax sharing for allocating tax revenues across levels of government.[13]

From this perspective, the model of fiscal decentralization in Korea is a mixture of those found in both unitary and federal countries. It is notable, however, that the coexistence of different fiscal decentralization models is not unique to Korea only. Banting (2007) characterizes Canadian federalism into three different types; classical federalism; shared-cost federalism; and joint-decision federalism. He then argues that great difficulties of Canadian federalism lie in the domain of shared-cost federalism, by which costs of major sectors of the welfare state such as health care, post-secondary education, social assistance, and social services are shared between federal and provincial governments.[14] Therefore the problem of establishing a clear-cut model of fiscal decentralization, especially in the area of welfare programs, seems to be a difficult issue both in Canada and Korea. However, it is even more challenging in Korea because, having begun decentralization only in 1995, its fiscal institutions that deal with fiscal decentralization are weak. Borrowing the terminology of Wildasin (2004), Korea is not a maturely decentralized country, unlike many advanced OECD countries. Therefore time will be needed for a more stable system of fiscal decentralization to emerge. Among many challenging issues that are yet to be resolved in this regard, fiscal institutions that can help reduce the controversies over partially funded mandates and insufficiently funded categorical grants, as previously discussed in section 3, will be discussed below.

4.2 Fiscal institutions for fiscal decentralization and challenges for Korea

Fiscal institutions of unitary countries

The root of the controversies over allocating fiscal resources and responsibilities that are related to the provision of welfare programs in Korea seem to come from the inability to decide whether to follow a fiscal decentralization model of a unitary country or a federal/regional country. An arguably successful fiscal decentralization model of a unitary country is that of

[13]It is notable that both Japan and Turkey, the large non-federal countries, also rely on the system of tax sharing.

[14]By classical federalism, federal and provincial governments make unilateral decisions on public services. In this framework, the federal government makes decisions on unemployment benefits, child benefits, and non-contributory old-age pension and provincial government on worker's compensation. An example of joint-decision federalism is the Canada Pension Plan.

the Nordic countries. This of course does not mean that controversies on intergovernmental fiscal relations do not exist; the pendulum of decentralization swings back and forth in these countries as well. However, a notable feature of intergovernmental fiscal relations in Nordic countries is their ability to change the system of fiscal decentralization according to changing economic environments.

During the economic crisis in the early 1990s, the central governments of Sweden and Norway were able to control the level of local income tax rates to fight the recession. In many other decentralized countries, control of local tax rates by the central government, even during an economic recession, cannot be an easy policy option. Changes in the system of intergovernmental grants also took place during this period, transforming earmarked grants into block grants (general grants). These changes were then followed by further adjustments in the structure of local revenues, local expenditures, and regulations that govern intergovernmental fiscal relations. Such dynamic changes are not easily found in federal and regional countries. For one thing, Italy changed its constitution in 2001, but the process of introducing “fiscal federalism” in Italy seems to be taking place over a very long period of time with much uncertainty (Brosio and Piperno, 2010).

An important fiscal institution that makes intergovernmental fiscal relations in Nordic countries more flexible than in many other countries seems to be cooperative fiscal federalism that makes budget negotiations take place on an annual basis between the central and local governments. In Denmark, local budgets are determined through annual collective agreements between the central and local governments (Mau, 2008). In Norway, the central government announces a desirable growth of total local government revenue prior to each fiscal year (Rattso, 2004). The central government of Sweden relies on a fiscal rule – balanced budget requirement – rather than an annual negotiation in controlling local budgets. However, the level of intergovernmental grants in Sweden is not determined by a fixed formula, and the central government has full authority to decide over it (Bonato et al., 2004).

As discussed before, Korea is similar to the Nordic countries in that it is a unitary country with a large local public sector. However it does not have an established budget negotiation system between the central and local governments. A main reason for this is because the Ministry of Finance, a budget ministry, has few legal rights over local budgets. Laws and regulations regarding local budgets, local taxes and intergovernmental transfers are all administered by the Ministry of Public Administration and Security (MOPAS). In theory, budget negotiations can take place between the MoF, MoPAS, and local governments. However, there is no legal mechanism that makes such negotiations necessary. In particular, the total amount of general grants is determined by law – 19.24 percent for general local administration, and 20 percent for eduction – and therefore, there is not much room for the MoF to take part in changing the size of local budgets.

Fiscal institutions of federal and regional countries

The fact that central and local revenues are determined by laws, rather than budget negotiations led by the central government, makes intergovernmental fiscal relations in Korea resemble those of Italy and Spain. These countries are not federal, nor are their systems of intergovernmental fiscal relations unitary. In particular, budgets of subnational governments are mostly determined by constitutions and laws, rather than budget negotiations between different levels of government. The fact that tax sharing is an important source of subnational governments' revenue in Spain and Italy also indicates that local public finance in Korea is similar to those of Italy and Spain rather than the Nordic countries.

In federal or regional countries, fundamental intergovernmental fiscal reforms such as the revision of constitutions have taken place. In Spain, the 1978 constitution has played its role in shaping the current system of intergovernmental fiscal relations. In Italy and Switzerland, constitutional changes have been made in the 2000s, which have brought about the recent fiscal federalism reforms. An additional fiscal institution that deals with intergovernmental fiscal relations in federal countries is intergovernmental forums. In Germany, the Financial Planning Council, which consists of federal ministers of finance and economics, state ministers of finance, and representatives of municipalities, provides inputs for reaching solidarity pacts between federal and state governments (Shah, 2007). In Spain, the Fiscal and Financial Policy Council (CPFF) assesses the evolution of the regional finance system on a regular basis and recommends necessary changes to the central and regional governments (López-Laborda et al., 2007).[15] In Australia, Commonwealth Grants Commission (CGC) – an independent advisory

[15] According to López-Laborda et al. (2007), significant changes in subnational finance were initiated by CPFF in 1987, 1991, 1996, and 2001.

body – guides the federal and state governments in the determination of intergovernmental grants.

Although Korea has the characteristics of a regional country, there is no intergovernmental forum or agency that deals with intergovernmental fiscal relations. This may be a natural aspect of a unitary country. But as discussed before, the decision-making processes on local public finance in Korea are compartmentalized by laws. In this sense, Korea is stuck with both unitarism and federalism in favor of status-quo bias: it does not have the cooperative intergovernmental fiscal relations found in Nordic countries, nor the fiscal institutions in federal/regional countries that provide channels for information and negotiation to help the decision making processes of central and local governments.

Coercive federalism

The lack of fiscal institutions that deal with intergovernmental fiscal relations seems to be related to the large amount of conditional matching grants in Korea. As was seen in section 2, the size of conditional grants, including partially funded mandates, is as large as general grants and has been rapidly growing since the start of decentralization. In a sense, the only fiscal tools the central government can exert flexibility on local budgets is specific grants. It is worth noting that there are few OECD countries in which the size of specific grants is as large as that in Korea. The only exception is the U.S., in which federal grants to the states consist mostly of specific grants.

What is notable in the system of federal-state fiscal relations in the U.S. is that it is actually quite similar to that of many European countries in that it heavily relies on mandates and regulations as well as intergovernmental grants. A traditional view on the model of fiscal decentralization in the U.S. is that it is best explained by the Tiebout type fiscal federalism model which emphasizes mobility-induced competition and aggregation of voter preferences. However, this view has recently been convincingly challenged by Baicker et al. (2011), which show that the rapid growth in state budgets in the last 50 years has been mainly due to education, health and public welfare, which are provided by heavily incentivised federal grants, unfunded or partially funded mandates, and regulations. As argued by, e.g., Kincaid (1990) and Posner (1998), the fiscal decentralization model of the U.S. can be at least partially described as "coercive federalism".

Reliance of the central government on unfunded or partially funded mandates is certainly a controversial issue, and its evaluation is divided. In a report by ACIR (1994), unfunded mandates were criticized for involving, "inadequate consideration of the costs imposted on the benefits to states and local jurisdictions" and "distortions of state and local government budgets and policy priorities", among others. These are standard arguments, based on the principle of subsidiarity, against the central government's regulatory interventions in local governments. However, there is a view – based on principal-agency theory – that it plays a positive role of controlling the costs of local public services. Huber et al. (2005), for example, argue that mandates combined with unconditional block grants provide an incentive for the state government to minimize the costs of the mandate. Similarly, Spahn (2007) argues that making local governments co-finance local public services can reduce the problems of moral hazard and fungibility created by the full compensation of the central government.

Apart from the theoretical arguments, unfunded mandates are defended for practical reasons. Cole and Comer (1997) argue that unfunded mandates provide a substantial net subsidy to state and local governments and the fiscal burden of these mandates is much larger for the federal government. Amid controversies on the pros and cons of unfunded mandates, the U.S. Congress decided to enact the Unfunded Mandates Reform Act (UMRA) in 1995 to control the growth of the unfunded mandates. The effects of UMRA have been debated to a great extent since then but it is generally agreed that UMRA has played a positive role: firstly, it increases the information available for legislative and administrative decision-making by requiring cost estimates for new mandates; secondly, it improves the quality of legislative decision-making by requiring a separate recorded vote to approve new legislative mandates (Cole and Comer, 1997).

The debates on partially funded mandates in Korea are in many ways similar to the ones in the U.S. Local governments in Korea are strongly criticize the coercive nature of partially funded mandates for welfare programs. On the other hand, the central government argues that its fiscal burden is greater and local governments should devote more fiscal resources to social expenditures. What is notable in Korea and the U.S. is the absence of fiscal institutions that deal with intergovernmental fiscal relations.[16] Although theoretical elaboration is needed, this fact seems to be linked with the dominant role of specific grants and unfunded mandates in these countries. Compared to the U.S., however, the coercive nature of specific grants in Korea is even stronger since it does not have any legal mechanism such as the UMRA that allows cost estimates of partially funded mandates, which in turn initiates debates on the methods of cost-sharing. With a growing trend of mandates on social expenditures, the demand for fiscal institutions that deals with the nature of coercive federalism embedded in the system of specific grants will increase as well. Whether to address this problem with a legal mechanism similar to the UMRA or, more fundamentally, deal with the choice between unitary or federal model of fiscal decentralization is a challenging question faced by Korea.

5 Conclusion

The fiscal decentralization model in Korea can be described as a mixture of cooperative fiscal federalism of the Nordic countries, fiscal federalism model of regional countries, and coercive federalism similar to the one found in the U.S. The problem of Korea's fiscal decentralization is weak fiscal institutions that deals with intergovernmental fiscal relations. One reason is due to Korea's short history of decentralization, which started in 1995. But a more fundamental reason is its inability to decide on whether to follow a fiscal decentralization model of a unitary country or a federal/regional country. Lacking fiscal institutions that provide channels for budget negotiations between the central and local governments, the central government relies mainly on specific grants with regulations such as partially funded mandates. Although there is theoretical reason to positively evaluate partially funded mandates, proliferation of intergovernmental grants with coercive measures is likely to be caused by the lack of efficient and cooperative intergovernmental fiscal tools.

Being a unitary state under the constitution, the best route Korea can take, to efficiently manage the local public sector, seems to be to follow the cooperative fiscal decentralization model of the Nordic countries. However, Korea's legal and political structures make it a demanding role

[16]It is interesting to note in this regard that the U.S. Advisory Commission on Intergovernmental Relations (ACIR) was abolished in 1996 after its publication of a report in 1994 named "Federally Induced Costs Affecting State and Local Governments" which recommended the abolishment of unfunded mandates (Poster, 1998; Kincaid, 1999).

for the central government to take a lead in the matters of intergovernmental fiscal relations. As a matter of fact, it is hard to find a unitary system in OECD countries whose population is large. Given the fact that Korea has the characteristics of a regional country, it will be desirable to have some kind of intergovernmental forum or agency that could enhance negotiations and dialogues across levels of governments. This again, however, is a difficulty task since the idea of fiscal federalism is a weakly defined concept in Korea.

An immediate issue Korea faces is to establish an institutional mechanism to build a consensus on how to deal with partially funded mandates. The Unfunded Mandates Reform Act (UMRA) in the U.S. sets an example to solve the conflicts and controversies over unfunded mandates on a legal basis. There are some doubts on the effectiveness in controlling the growth of unfunded mandates in the U.S. Nevertheless the lesson to be drawn from the UMRA is that it reveals the total fiscal burden associated with unfunded or partially funded mandates. Therefore, in a similar way, a medium-term projection of the total cost incurred by partially funded mandates will improve the decision-making process on rapidly increasing social expenditures in Korea.

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