

Analysis of local tax system formulation process - A case study  
on unifying the two tax bases of municipal income tax in Japan

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**Abstract**

In this paper, I have analyzed the factors that led to the unification of the two tax bases of the municipal income tax in Japan. Until FY 1963, there were two bases for municipal income tax. They were the principle and the exception, and the municipalities could choose either of the two. This study discusses the process of unifying the two tax bases into the principle. The driving force of unification was the public commitment of tax reduction made by the LDP in view of the general elections of 1963. Prime Minister Ikeda played a prominent role in accomplishing the unification of the two tax bases. With the support of the LDP under pressured petitions from the National Association of Towns and Villages during the budget negotiation process, compensation to offset the fall in tax revenue that were being opposed by the Ministry of Finance were introduced, and the two tax bases were unified.

**Keywords:** Municipal Income Tax, Disparity, Tax Base, Tax Reduction, Grant

## **1. Introduction**

The purpose of this paper is to clarify the reasons behind the unification of the local tax bases and rates of municipal income tax. Until FY 1963, there were two tax bases for municipal income tax. They were the principle and the exception. The municipalities could choose either of the two. The former was calculated by making various kinds of deductions from the gross income. Whereas, the latter was calculated by making only the standard deduction. It could be adopted when additional tax revenue was necessary. This paper discusses the process of unifying the two tax bases into the principle.

If we look back in time, the year 1963, in which this system modification was decided, was a huge turning point for the local governments. The unification of the two tax bases and introduction of the standard tax rate and the limited tax rate systems, discussed in this paper, modified the flexible management of tax rate and base that had been continuing since the Shoup Report. Also deemed as "the greatest reform since Shoup"<sup>1</sup>, it formed a standard base of taxation and tax rate, which is one of the features of the local taxes in Japan. Depicting the forming process of this system clarifies the formation of Japanese features.

Some previous studies analyzed the burden disparities of municipal income tax in the 1950s and 60s. Imai (1993) found that the burden disparities had expanded after 1955 and the tax burden of low income earners was heavy. Toh (2005) revealed that the tax burden of the exception was higher compared to the principle. However, they didn't clarify why the system of municipal income tax was changed.

The contents covered in this paper are as follows. Section 2 identifies the burden disparities between municipalities for municipal income tax and municipal income tax used since the Shoup Report, which is the premise of this discussion. Section 3 discusses the unification of the two tax bases and the relation between the actors. Section 4 discusses compensation to offset the fall in revenue subsequent to the unification of the two tax bases and the relation between actors. Section 5 covers the concluding remarks.

## **2. A twofold choice tax base and burden disparities between municipalities**

Before discussing the unification of the two tax bases, let us look at municipal income tax system used since the Shoup Report that is the premise of this discussion. The system of municipal income tax was a fivefold choice tax base that also included the

principle in the 3 types of tax bases based on the Shoup Report. Out of the 5 types, 3 were abolished, changing it into a twofold tax base comprised of the principle and the exception. In the end, the two tax bases were unified into the principle.

Fig. 1 shows images of the principle and the exception for municipal income tax. The tax base in the principle is calculated by making various kinds of deductions from the gross income. Whereas, in the exception, only the standard deduction is made. Therefore, the tax burden of the latter is higher compared to the former despite the gross income being the same. The base tax rate to be used by the municipalities was regulated by the Local Tax Law, and the specific tax rates were determined by the regulations of the municipality. Also, the method of calculating the tax base was modified in FY 1962<sup>2</sup>.

A depiction of the tax burden disparities between the municipalities based on the above - mentioned tax bases and base tax rate as the household base is shown in Table 1. If we look at a standard household (husband and wife, 3 children) of a salaried employee with an annual income of 500,000 yen, the tax amount was 2,630 yen when it was calculated according to the base tax rate under the principle, while in the case of the base tax rate using the exception it was 4,830 yen about 1.8 times as high as the principle. As pointed out in my paper from 2008, many municipalities using the exception adopted excessive taxation that was higher than the base tax rate and because of this; there were some municipalities where the tax burden of municipal income tax was more than 3 times the municipalities using the base tax rate. Additionally, there were some municipalities that carried a burden as high as 6 to 7 times that of municipalities using the base tax rate under the principle as shown in Table 2<sup>3</sup>. Furthermore, it is obvious from Table 3 that most of the taxpayers of municipal income tax in the municipalities that adopted the exception were low income earners with no national income tax liabilities.

The relatively heavy tax burden under the exception was particularly observed in the grant-receiving towns and villages of ordinary local allocation tax (OLAT) grants. Table 4 shows the number of municipalities of adoption of the principle and exception. As this table illustrates, roughly 80% of the municipalities adopted the exception, and among them, many grant-receiving small municipalities of OLAT grants adopted it.

The problem of tax burden disparities between municipalities was raised by the Government Tax Commission in 1962 and investigations were carried out. In the deliberation process, many investigations were carried out regarding questions such as why the residents under an elected head were bearing such a heavy tax burden, what would be the effects of disparity rectification on the finances of municipalities etc. But

since these questions are closely linked with the local administration, tax system, and grants and so on, it was decided that a conclusion should be reached after receiving an adequate clarification about the definite situation of excessive taxation by the municipalities and the state of finances. Therefore, a solution to the problem was passed on at the report in December of the same year<sup>4</sup>.

### **3. Unification of the two tax bases and relation between actors**

In the following year (1963), the Government Tax Commission discussed the unification of the two tax bases and implementation of the standard tax rate and the limited tax rate in great detail. Unifying the two tax bases as well as implementing the standard tax rate and the limited tax rate had been conducted over the span of 2 years starting in 1964, but even prior to the modification of the system, the Ministry of Home Affairs had been guiding the municipalities regarding the adoption of the principle and base tax rate. However, the remarks by Shibata (the Head of the Local Tax Bureau of the Ministry of Home Affairs) at the Regional Administration Committee of the House of Councilors pointed out the fact that the Ministry of Home Affairs was aware that the basic problems could not be solved by such guidance<sup>5</sup>.

In the guidance process, the Ministry of Home Affairs had an uneven allocation of OLAT grants by adjusting the standard financial need with increasing the modification coefficient<sup>6</sup> and provided compensation in the form of a special local allocation tax (SLAT) grants, to counter the fall in revenue subsequent to the adoption of a base tax rate for the municipalities imposing excessive taxation<sup>7</sup>. However, this did not really help in increasing the number of municipalities that switched to the principle and base tax rate. This led the Ministry of Home Affairs to reconsider if municipal income tax could be reduced by increasing the general finances with an uneven allocation of OLAT grants, and conducted a survey of the municipalities in FY 1963<sup>8</sup>.

According to Shibata (1975), the unification of the two tax bases was on a predetermined course since 1962 when Mr. Shibata joined the Local Tax Bureau of the Ministry of Home Affairs that holds jurisdiction over the local taxes, and its preparations were underway<sup>9</sup>. As mentioned above, in the report by the Government Tax Commission the same year, the unification of the two tax bases was postponed but according to the remarks made by Mr. Shinoda, Minister of Home Affairs and Mr. Shibata, Head of the Local Public Finance Bureau of Ministry of Home Affairs at the Regional Administration Committee, the Local Tax Bureau of the Ministry of Home Affairs continued to conduct investigations regarding the unification of the two tax

bases for further modification of the system<sup>10</sup>. Moreover, prior to the aforementioned announcement of the actual results of the survey of municipal income tax by the Government Tax Commission, Mr. Hayakawa, the successor to Mr. Shinoda, Minister of Home Affairs, stated in a press conference after the cabinet meeting that "We need to unify the two tax bases of municipal income tax under a multi-year project"<sup>11</sup>. The Ministry of Home Affairs had strong views about resolving the tax disparities between municipalities under a long-term plan of 3 to 5 years. A long-term plan was chosen because if implemented in the short term, the fall in revenue would have been huge in each fiscal year. In addition to that, no financial compensation was expected due to the anticipation of strong resistance by the Ministry of Finance, which opposed to the compensation due to a decline in revenue for the central government. In the worst case, it was considered to be implemented as a 5-year plan without any compensation by the central government. Moreover, there was an emphasis on the reduction of electricity and gas taxes during this time due to appeals by the industrial world and inclinations by Prime Minister Ikeda. If the tax reduction was implemented, the compensation for electricity and gas tax reduction would become problematic and would overlap with the compensation for municipal income tax. The implementation of 2 tax reduction compensations seemed to be difficult<sup>12</sup>. Although the Ministry of Home Affairs was planning to unify the two tax bases in this way, it was considered to be difficult due to the problem of providing compensation for the decrease in revenue.

A few days after the announcement made by Home Affairs Minister Hayakawa, on August 15, Prime Minister Ikeda invited Mr. Izumi, Head of the Tax Bureau of the Ministry of Finance to his official residence, instructing him to draft a tax break for the promotion of exports. At the same time, he emphasized the necessity of resolving the tax burden disparities between municipalities subsequent to the reduction of municipal income tax. He expressed his opinion that in case of pressure on the local government finances due to this tax reduction, the deficit must be covered by increasing the treasury payment, but on the other hand he showed a negative attitude towards a substantial reduction of the national income tax<sup>13</sup>. In a cabinet meeting the following day, it was decided to conduct research with the intention of unifying the two tax bases. Later at a press conference held after the "public session of Cabinet (public hearing related to government affairs)" at Aomori City, Prime Minister Ikeda again stated that "We most certainly intend to reform the local tax system. Although there are views that national income tax reductions should be implemented first, it is irrational to burden the low-income households, who cannot even pay the national income tax, with a heavy municipal income tax"<sup>14</sup>, deeming it important to resolve the burden disparities between

municipalities for municipal income tax.

Although the 200-billion-yen tax reduction pledged by the Liberal Democratic Party (LDP) in the general elections of November 1963 mentioned in my paper from 2008 influenced the progress made in the investigations related to the unification of the two tax bases that were being carefully investigated, it was Prime Minister Ikeda who played a significant role in the unification.

While the unification of the two tax bases was still under investigation, the survey results of the actual conditions of municipal income tax was announced by the Government Tax Commission on August 23. The results confirmed that the tax burden of the municipalities that were using the exception was considerably heavy and there were considerable burden disparities between the municipalities. The survey results of the actual conditions revealed that there was a heavy burden on the residents of these municipalities and yet these municipalities had a low level of administration<sup>15</sup>. In contrast to the survey results of the actual conditions, the majority of opinions in the local tax system sectional meeting of the Government Tax Commission was that a certain level of burden disparities in municipal income tax is not that problematic and it is not necessary to rush with the unification<sup>16</sup>. The Ministry of Finance affirmed that the predominant negative opinion was expressed by the overwhelmed committee members who believed that it was not easy to find a solution for the problem of alternative finances<sup>17</sup>. Later, the Government Tax Commission collected reports stating that "With regard to municipal income tax, in view of the present situation inflicted by considerable disparities between the tax burdens of different municipalities, this time measures shall be taken to resolve the burden disparities in a span of 2 years. This shall be carried out mainly by unifying the two tax bases with the principle. Also, measures will be taken to avoid excessive taxation in the future, while at the same time aiming for a rationalized revision of the existing base tax rate into a standard rate"<sup>18</sup>. However, at the beginning of the investigation, unifying the two tax bases was not considered to be that crucial.

However, the Government Tax Commission did not play a very big role in the realization of unifying the two tax bases. As mentioned earlier, the LDP made a public pledge of implementing a 200-billion-yen tax reduction as their slogan for the general elections, and stated that "We will reduce the burden by resolving the burden disparities between municipalities by unifying the municipal taxes with the principle"<sup>19</sup>. This is what "actually decided the framework of the budget compilation of FY 1964"<sup>20</sup>.

Before the 200-billion-yen tax reduction was decided, Finance Minister Tanaka consulted Prime Minister Ikeda on October 14, and mentioned that the Budget Bureau

of the Ministry of Finance was insisting on a 150-billion-yen tax reduction plan while the Tax Bureau was inclined towards a 200-billion-yen tax reduction, and sought his decision on the matter, however Prime Minister Ikeda put the decision on hold<sup>21</sup>. The next day, Mr. Izumi, Head of the Tax Bureau of the Ministry of Finance and Mr. Sato, Head of the Budget Bureau presented the 150-billion-yen as well as the 200-billion-yen tax reduction plans respectively at the Prime minister's official residence and explained that in view of the finances, adopting the 200-billion-yen tax reduction plan would make the next fiscal year's budget compilation very difficult<sup>22</sup>. However, Prime Minister Ikeda still decided to go ahead with the 200-billion-yen tax reduction plan and announced the tax reduction structure at a press conference<sup>23</sup>.

Moreover, Finance Minister Tanaka made an appearance at the general meeting of Government Tax Commission held two days later on October 18th, and explained the policy stating that "As for the local taxes, since there will be a considerable natural increase in local revenue during the next fiscal year, we shall resolve the burden disparities between the municipalities with a municipal income tax and shall aim for a reduction in the electricity and gas tax"<sup>24</sup>. The presence of a Minister of Finance at the general meeting of Government Tax Commission was unprecedented<sup>25</sup>. Furthermore, in his financial address at the 44th extraordinary Diet session held later that afternoon, he committed to resolving the disparities between municipal income tax and stated that "In order to further stabilize the daily lives of citizens, in the next fiscal year we intend to reduce the national income tax and resolve the disparities of municipal income tax burden, reduce the real estate acquisition tax and property tax in order to facilitate house construction, as well as reduce the electricity and gas tax. (Omission) From the above perspective, we intend to implement a tax reduction to the scale of nearly 200-billion-yen next fiscal year through national and local taxes<sup>26</sup>. "

In this way, the government and the ruling party promoted the modification of the system in preparation for the general elections, and the Government Tax Commission made extraordinary arrangements for conducting detailed investigations in accordance with the tracks that had been laid out for them. On the basis of the reports of the Government Tax Commission presented at the end of the annual budget assessment by the Budget Bureau of Ministry of Finance, the Budget Bureau and the Tax Bureau negotiated and examined the allocation of financial resources. However, this year's decision process was different from the other years<sup>27</sup>. During this time, the LDP Research Commission on the Tax System was in the process of determining the outline after the report by the Government Tax Commission, and it is believed that it was not the LDP Research Commission on the Tax System but the Tax Bureau of the Ministry of

Finance under the Government Tax Commission and its secretariat that was controlling the initiatives of the tax system reforms<sup>28</sup>. The Head of the Government Tax Commission, Mr. Nakayama stated that "We are committed to the 200-billion-yen tax reduction"<sup>29</sup>, but the unification of the two tax bases was decided before the Government Tax Commission gave its report and the deliberation of the Government Tax Commission and its report presented to the government was a mere formality.

#### **4. Compensation to offset the fall in revenue subsequent to the unification of the two tax bases and relation between actors**

The greatest problem in unifying the two tax bases was finding a way to compensate for the fall in revenue of the municipalities that were using the exception for municipal income tax. As mentioned earlier, initially the Ministry of Home Affairs had expressed a strong preference for implementing a 3-5-year plan for resolving the burden disparities between the municipalities levying a municipal income tax. This was due to the anticipation of strong opposition by the Ministry of Finance which opposed to the idea of providing compensation to offset the decline in revenue. However, the Ministry of Home Affairs complied with the policies of Prime Minister Ikeda and decided to unify the two tax bases with a short-term plan of 2 years, and introduce the grants to offset the decrease in revenue<sup>30</sup>. The Local Tax Bureau of the Ministry of Home affairs had intended to finally unify the grants with the local allocation tax (LAT) grants, but the discussions with the Local Public Finance Bureau of the Ministry of Home Affairs were not fruitful so instead, they made a budget request for the Ministry of Home Affairs plan for issuing the grants gradually decreasing over 5 years<sup>31</sup>.

On the other hand, since unification of the two tax bases was carried out under the direct instructions of Prime Minister Ikeda, the Budget Bureau of the Ministry of Finance was not able to defy it directly<sup>32</sup>, but opposed to the idea of compensation for the decrease in revenue of the local governments subsequent to the unification<sup>33</sup>. Moreover, in a press conference following the cabinet meeting held on August 16, Finance Minister Tanaka showed his approval for the unification of the two tax bases, but disagreed with the Ministry of Home Affairs regarding the compensation for the fall in revenue<sup>34</sup>.

On the basis of the following points, the Ministry of Finance expressed its reluctance towards the compensation to offset the decline in revenue demanded by the Ministry of Home Affairs<sup>35</sup>;

- 1) Theoretically, the decrease in revenue due to the abolition of the exception



should be covered with adjustments such as an uneven distribution of LAT grants

- 2) With the anticipated increase in the quota of LAT grants from a natural increase in revenue from the national tax as well as municipal tax in the next fiscal year, the decline in revenue can be compensated to some extent
- 3) On the other hand, it is difficult to appropriate a huge sum as a grant since a fairly large chunk of the budget will have to be used on public investments, social security, etc. in the next fiscal year

Owing to the conflicting opinions of the Ministry of Home Affairs and Finance, no conclusion was reached upon in the Government Tax Commission as well. The report drafting committee setup by the Ministry of Finance on November 19 carried out investigations on the local tax reduction. In the meeting, the Ministry of Home Affairs presented (1) Compensation for municipal income tax reduction by the central government, (2) original tax reduction plan based on a no reduction in the electricity and gas tax, and this led to heated discussions in the meeting<sup>36</sup>.

As for the conflict between these ministries, the LDP supported the ideas of the Ministry of Home Affairs as mentioned in my paper from 2008, but why did LDP do so? The answer to this question is the influence of the National Association of Towns and Villages. As validated in Table 4, eighty percent of the towns and villages were using the exception and the big question was whether or not any compensation would be available against the fall in revenue subsequent to the unification of the two tax bases. Therefore, after investigations into the tax base unification, the National Association of Towns and Villages demanded that the LDP provide grants to offset the decrease in revenue.

Even before Prime Minister Ikeda had expressed his intention of unifying the two tax bases, in April 1963, the National Association of Towns and Villages had expressed their opinion stating that "The alternative financial resources to counterbalance the fall in revenue resulting from restoring to a base tax rate or the principle will not simply appear from the pretense of local taxes that center on the existing principle of independent tax"<sup>37</sup>. However, after the announcement of the unification of the two tax bases by the Prime Minister, they requested for the unification of the two tax bases and the introduction of grants to offset the decline in revenue in their "Opinion on the revision of a local tax system in FY 1964"<sup>38</sup>. The Chairman, Mr. Yamamoto attended the hearing held on September 27 by the LDP Research Commission on the Tax System for the representative of the Six Major Organizations on Local Government. A gist of his opinions on the unification of the two tax bases is given below<sup>39</sup>.

The first problem for which measures should be taken in the next fiscal year is the state of municipal income tax. Although it is common knowledge that the burden of municipal income tax has created considerable disparities between the municipalities, the problem arises due to the irony that the weaker the financial strength of the municipality, the heavier the burden.

This irony of a relatively heavy burden with a low level of administration is extremely unfair. It leaves no options for the residents to choose between the administrative service and tax burden.

This can be attributed to the defect in the local public finance system itself. The problem will not get resolved by itself just by reinforcing the financial strength of the weak municipalities. Therefore, we should first aim to reduce the tax burden and then aim to resolve the accompanying problems with the help of various financial measures.

The problem is our ability in not being able to find the perfect measures against the reduced tax revenue for municipalities. It is impossible to get the weak municipalities to generate annual revenue deficit and further cut down the administrative level. Although an uneven allocation of LAT grants is a basic countermeasure, it differs with the nature of a trade-off against the impending fall in revenue. In the long run, direct and concrete supplementary funds are a prerequisite for the weak municipalities that face tax reductions. This is the reason behind our strong demand for the introduction of grants for tax reduction as the transitional measure.

The reduction of municipal income tax burden will eventually lead to fiscal problems. I feel that acknowledging this point is the first step towards reforms.

After the general elections, Chairman Kawazu, successor to Chairman Yamamoto and Chairmen of all prefectural association of towns and villages jointly made a request to the local elected members of the House of Representatives regarding the unification of the two tax bases, stating that "We request the central government to take necessary financial measures for resolving the disparities of municipal income tax and for reducing the burden, and at the same time ensuring that the tax base unification will not create an annual revenue deficit in the towns and villages"<sup>40</sup>.

Furthermore, the National Association of Towns and Villages held a policy research council meeting on December 10 to setup the "Extraordinary Diet session countermeasures head office" that year and by the end of the year, it was actively engaged in the operations for its realization. After the meeting, Chairman Kawazu and policy research council members proceeded to the House of Representatives and requested that at the LDP local administration sectional meeting, the LDP is to "give thorough consideration to the development of local authorities and securing finances for the weak municipalities". The following day (11th), the concerned Diet members were

invited for a breakfast meeting at the National Association of Towns and Villages auditorium, also attended by the Executive Director of the National Association of Towns and Villages and the policy research council members, and the same demands were made<sup>41</sup>.

Meanwhile, the National Association of Towns and Villages was informed regarding the negative attitude of the Ministry of Finance regarding the compensation to offset the fall in revenue subsequent to the unification of the two tax bases. With the anticipation of the budget hearing running into rough waters, the municipalities using the exception in all prefectures started sending telegraphic petitions from December 10, to their local Diet members requesting them to secure 24 billion yen as grants for municipal income tax reduction<sup>42</sup>.

After the unofficial announcement of the budget 4 days later, a "General assembly of the National Association of Towns and Villages demanding the grants for tax reduction" was held jointly with the National Association Chairmen of Town and Village Assemblies on December 24 at Sabo Kaikan in Hirakawacho, Tokyo, in which Home Affairs Minister Hayakawa, Head of Local Administration of LDP, Nakajima, etc., were invited as guests and it was resolved to "secure grants for municipal income tax reduction". After the general assembly, under the leadership of the chairmen of each prefectural town and village and chairmen of the town and village assemblies, petitions were submitted at the LDP local administration section meeting and to Mr. Kurogane, the Chief Cabinet Secretary<sup>43</sup>. This kind of a general assembly had never been held before<sup>44</sup>. Later, the National Association of Towns and Villages further intensified its movement. A summary of the movement since the unofficial announcement of the budget on December 20 is given in Table 5. Upon receiving the progress details of the budget negotiations from the Local Public Finance Bureau of the Ministry of Home Affairs, the National Association of Towns and Villages continued submitting petitions to the government and the ruling party. It submitted 3 petitions to the Executive Council, including the chairman of the LDP General Council, and 2 to Finance Minister Tanaka and Mr. Kurogane, the Chief Cabinet Secretary<sup>45</sup>.

This kind of strong pressure by the National Association of Towns and Villages is said to have served as the background of the support extended by the LDP to the Ministry of Home Affairs at the time of budget negotiations. In order to increase their likelihood of getting elected, it was necessary for the Diet members to obtain the support of the National Association of Towns and Villages, by providing compensation to offset the fall in revenue to the 80% of the towns and villages that were using the exception.

After the problem of compensation for the decline in revenue became extremely challenging during the restoring negotiation process, the decision was left to be taken in the final stage of cabinet negotiations to be held in the government departments on December 28. After nearly 4 hours of negotiations, it was decided to unify the two tax bases and to establish a standard tax rate system over a 2-year period through the fiscal years 1964 and 65. It was also decided that bonds in the amount of 15 billion yen would be issued over 2 years and the principal and interest payments of bonds would be subsidized by the central government<sup>46</sup>. During the cabinet negotiations, the LDP presented a proposal that instead of the grants, the municipalities should issue the local bonds. This was accepted by the Ministry of Home Affairs, thereby settling the cabinet negotiations<sup>47</sup>. The LDP's General Council also decided that "The Chairman and Vice President of Policy Affairs Research Council will be present, as the party representatives, for the cabinet negotiations on budget compilations" to be held on December 28<sup>48</sup>. Thus, the Chairman and Vice President of the LDP's Policy Research Council were present for the cabinet negotiations, and this seemed to have helped in reaching the said compromise<sup>49</sup>.

It was the strong pressure on the LDP by the National Association of Towns and Villages that led to the decision of providing compensation subsequent to the unification of the two tax bases.

## **5. Concluding remarks**

In this paper, I have analyzed the factors that led to the unification of the two tax bases. A summary of the contents of this paper is given below.

Before the unification of the two tax bases, it was mainly the municipalities with weak financial strength that were using the exception. Unifying the two tax bases was based on the policy objective of resolving the problem of burden disparities between the municipalities for municipal income tax. The driving force of unification was the public commitment of tax reduction made by the LDP in view of the general elections of 1963, as well as a strong inclination by Prime Minister Ikeda for the same. Prime Minister Ikeda played a prominent role in accomplishing the unification of the two tax bases. Accepting Prime Minister Ikeda's policy, the Ministry of Home Affairs implemented the unification of the two tax bases that was being cautiously examined until then, over a period of 2 years, and acted upon the policy related to the introduction of the compensation. With the support of the LDP under pressured petitions from the National Association of Towns and Villages during the budget

negotiation process, compensation to offset the fall in revenue which were opposed by the Ministry of Finance were introduced, and the two tax bases were unified.

In this way, the standard tax base and tax rate that is one of the features of local taxes in Japan was formed.

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The principle

Tax base	Dependents deduction	Life insurance premium deduction	Social Insurance premium deduction	Medical deduction	Casualty loss deduction	Standard deduction
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× municipal income tax rate (base tax rate)

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Tax credit	Municipal Income tax amount
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The exception

Tax base	Standard deduction
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× municipal income tax rate (base tax rate)

=

Tax credit	Municipal Income tax amount
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Fig. 1. Images of the principle and the exception for municipal income tax

Source: Government Tax Commission (1964), p.486.



Table 1. Number of municipalities using each tax base and their tax burden  
vis-a-vis in FY 1963

	Under SA	SA×1.0	SA×1.0- SA×1.5	SA×1.5- SA×2.0	SA×2.0- SA×2.5	SA×2.5- SA×3.0	Over SA×3.0
The principle	15	538	59	25	16	5	0
The exception	85	653	811	562	403	184	61

Notes: (1) The standard amount (SA) of a standard household is calculated according to the base tax rate. Each cell in the table represents the comparison to SA.

(2) Amounts represent the number of municipalities under each regime.

Source: Institute of Local Finance (1964) (ed.), p.111.

Table 2. Ranking of heavy tax burden municipalities for municipal income tax  
in FY 1963

Rank	Prefecture	Municipality	Population	Financial capability index	Municipal income tax amount (yen)	% higher than standard amount
1	Shiga	Adogawa	12,555	0.44	18,120	689
2	Shimane	Nita	14,032	0.32	17,790	676
3	Shimane	Tonbara	6,006	0.19	17,290	657
4	Nagano	Shimojo	5,016	0.21	17,140	652
5	Niigata	Kariwa	6,594	0.33	16,830	640
6	Niigata	Yoshikawa	11,005	0.29	16,580	630
6	Nagano	Takagi	8,422	0.24	16,580	630
8	Akita	Inaniwakawatura	14,607	0.20	16,540	629
9	Nagano	Kijimadaira	7,735	0.23	16,500	627
10	Niigata	Nishiyama	10,926	0.36	16,470	626

Notes: “% higher than standard amount” represents the percentage for municipal income tax amount of a standard household of a salaried employee with an annual income of 500,000 yen in the case of a base tax rate under the principle.

Source: Institute of Local Finance (1964) (ed.), pp.112-3.

Table 3. Number of people with national income tax liabilities in FY 1963

	Tax liabilities	No tax liabilities	Total
The principle	10,618	1,129	11,747
The exception	3,678	3,990	7,668
Total	14,296	5,119	19,415

Notes: (1) "Tax liabilities" means people with national income tax liabilities. "No tax liabilities" means people with no national income tax liabilities.

(2) Amounts represent thousand of people.

Source: Institute of Local Finance (1964) (ed.), p.114.

Table 4. Number of municipalities adopting the principle and exception in FY 1963

		The principle			The exception			Total			TDB
		GR	NGR	Total	GR	NGR	Total	GR	NGR	Total	
City size	More than 500,000	6	4	10	0	0	0	6	4	10	0
	More than 50,000	90	61	151	107	3	110	197	64	261	0
	Under 50,000	59	10	69	206	7	213	265	17	282	1
Towns and villages		364	65	429	2,405	36	2,441	2,769	101	2,870	0
Total		519	140	659	2,718	46	2,764	3,237	186	3,423	1

Notes: (1) "GR" means the grant-receiving municipalities of OLAT grants. "NGR" means the non-grant-receiving municipalities. "TDB" means the taxation on a differential basis in the same municipality.

(2) Amounts represent the number of municipalities.

Source: Government Tax Commission (1964), p.487.

Table 5. Transition of movements by the National Association of Towns and Villages  
(December 21~27)

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[December 21]

The Director of the Local Public Finance Bureau, Ministry of Home Affairs explained the draft of unofficial announcement of each ministry to the Six Major Organizations on Local Government. Promised to explain the daily transitions henceforward.

[December 24]

"National Association of Towns and Villages general assembly demanding tax reduction supplementary funds" held.

Petitions submitted by heads towns and villages in Kinki and Chugoku regions

[December 25]

Petition submitted to the LDP's Executive Council (Chairman Kawazu, Mr. Sugiyama the Chief of Secretariat)

Appeal to all prefectural town and village assemblies to send telegraphic petitions to the LDP's policy council and all members of the Executive Council.

Chairmen of all prefectural town and village assemblies from Hokushin and Tokai regions, as well as heads of towns and villages went to Tokyo to submit petitions.

Petition to Mr. Kurogane, Chief Cabinet Secretary and Home Affairs Minister Hayakawa (Chairman Kawazu, Mr. Sugiyama, Chief of Secretariat)

[December 26 (morning)]

Early morning, Chairman Kawazu and the Head of the National Association of Town and Village Assemblies, Mr. Maeda submitted a petition to Finance Minister Tanaka.

[December 27]

Vice President Ichikawa (Head of Yamagata prefectural towns and villages) and 22 other heads of Yamagata prefectural towns and villages proceeded to Tokyo. Petition submitted to Mr. Kurogane, Chief Cabinet Secretary, and then to the elected Diet members of the same prefecture

Mayors of Nishiyama and Yuzawa Town in Niigata Prefecture submitted a petition to Finance Minister Tanaka.

Mr. Nakano, Chairman of Aomori prefectural towns and villages petitioned to Mr. Morita, Head of Local Government Committee of the House of Representatives.

Mr. Koiso, Chairman of Kanagawa prefectural towns and villages submitted a petition to Mr. Fujiyama, Chairman of LDP's Executive Council

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Source: National Association of Towns and Villages (1964).

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<sup>1</sup> Miyazawa et al., (1965), p.174. Among them, Morioka stated "To put it correctly, I think it is a huge revision since Shoup, after the tax system reforms of FY 1954. As many people know, the reason behind the reform of FY 1954 was that subsequent to the abolition of the municipal police, all the police expenses were transferred to the prefectures, and since the local government finance was significantly worsening at the same time, there was emphasis on strengthening the prefectural finances."

<sup>2</sup> Fujita (1978), pp. 317-319, Maruyama (1985), pp. 526-528, and Imai (1993), pp. 60-1. According to the Ministry of Home Affairs (1964), the tax system of the prefectural income tax was also going to be revised along with the modification of this system. The calculation method will also be revised and similar to the principle of municipal income tax, the gross taxable amount, which will be calculated by deducting the various kinds of taxes from the gross income. According to Fujita (1978), the division of gross income was implemented for the prefectural income tax and the tax rate was also standardized.

<sup>3</sup> Institute of Local Finance (1964) (ed.), pp. 110-1

<sup>4</sup> Iwami (1963), pp. 36-7.

<sup>5</sup> Government delegate Shibata's (local tax bureau director, Ministry of Home Affairs) answer to the question asked by committee member Suzuki at the 43rd ordinary Diet session, House of Councilors Regional Administration Committee held on March 19, 1963 (System for the Minutes of the Diet).

<sup>6</sup> As a prerequisite to the adoption of modification coefficients, municipalities were divided into "areas" according to the degree of urbanization. Up until FY 1968, each municipality had been divided into 20 levels, from area 1 to area 20, based on the population, economic structure and average price index of housing and land of the municipalities.

<sup>7</sup> Compensation for the fall in revenue by SLAT grants was implemented when the fivefold choice tax system was being used, before the system modification. The base tax rate was implemented in 1957 but in order to mitigate the drastic changes in the municipality finances caused by all this, SLAT grants was issued using the prescribed calculation method.

<sup>8</sup> Government delegate Shibata's (Director, Tax Bureau of the Ministry of Home Affairs) and Presenter Matsushima's (Minister of Home Affairs, government secretariat councilor) answers to the questions asked by committee member Suzuki at the 43rd ordinary Diet session House of Councilors Regional Administration Committee held on March 19, 1963 (System for the Minutes of the Diet).

<sup>9</sup> Shibata (1975), p.333.

<sup>10</sup> Home Affairs Minister Shinoda's and government delegate Shibata's (Director, Tax Bureau of the Ministry of Home Affairs) answers to the questions asked by committee member Suzuki at the 43rd ordinary Diet session House of Councilors Regional Administration Committee held on March 19, 1963 (System for the Minutes of the Diet).

<sup>11</sup> "Asahi Newspaper (evening edition)", August 2, 1963.

<sup>12</sup> Kinzai Institute for Financial Affairs (1963a), p.8.

<sup>13</sup> "Yomiuri Newspaper (morning edition)", August 16, 1963

<sup>14</sup> "Yomiuri Newspaper (morning edition)", September 8, 1963. Furthermore, according to the "Asahi Newspaper (morning edition)", September 7, 1963, the "Public session cabinet" is a hearing of the real orders, wishes of the public on general or government matters. It was held the same day at Aomori prefectural gymnasium at 9:30 am and lasted for 3½ hours. It was broadcast nationwide for approximately 1 hour by NHK TV and radio. Those present included Prime Minister Ikeda, Finance Minister Tanaka, Construction Minister Kouno, and Agriculture Minister Akagi. Moreover, according to the "Asahi Newspaper (morning edition)", September 8, 1963, the "Public Cabinet" held at Aomori City was the 2nd such cabinet, with the 1st held in October, the previous year

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at Okayama City. The news item stated the remark of a senior who said that "It is the first time since the visit of Emperor Meiji that so many cabinet ministers have gathered in the Tohoku region." and stated that "Just as the Prime Minister and his cabinet members had secretly hoped, this visit seemed to have quite positive results as an election campaign strategy".

<sup>15</sup> Usui et al., (1963), p.8, Nakaoki (1963), p. 93, Institute of Local Finance (1964) (ed.), pp.65-6.

<sup>16</sup> "Asahi Newspaper (morning edition)", August 24, 1963.

<sup>17</sup> "Yomiuri Newspaper (morning edition)", August 8, 1963.

<sup>18</sup> Zaisei Kenkyukai edition (1983), p.838.

<sup>19</sup> Institute of Local Finance (1964) (ed.), p.12, p.50.

<sup>20</sup> Zaisei Chousakai edition (1964), p.13.

<sup>21</sup> "Yomiuri Newspaper (morning edition)", October 15, 1963.

<sup>22</sup> "Asahi Newspaper (morning edition)", October 16, 1963.

<sup>23</sup> "Asahi Newspaper (evening edition)", October 16, 1963.

<sup>24</sup> "Yomiuri Newspaper (evening edition)", October 18, 1963.

<sup>25</sup> Kinzai Institute for Financial Affairs (1963b), p.14.

<sup>26</sup> Finance Minister Tanaka's speech on financial affairs at the 44th extraordinary Diet session House of Representatives, plenary session on October 18, 1963 (System for the Minutes of the Diet).

<sup>27</sup> Kinzai Institute for Financial Affairs (1963d), p.14.

<sup>28</sup> Sato and Matsuzaki (1986), pp.112-4, Kishiro (1985), pp.47-9.

<sup>29</sup> Kinzai Institute for Financial Affairs (1963d), p.14.

<sup>30</sup> Kinzai Institute for Financial Affairs (1963a), p.8.

<sup>31</sup> Institute of Local Finance (1964) (ed.), p.13, Shibata (1975), p.333.

<sup>32</sup> Kinzai Institute for Financial Affairs (1963d), p.14.

<sup>33</sup> Kinzai Institute for Financial Affairs (1963c), p.14.

<sup>34</sup> "Asahi Newspaper (evening edition)", August 16, 1963.

<sup>35</sup> "Asahi Newspaper (morning edition)", November 7, 1963.

<sup>36</sup> "Yomiuri Newspaper (morning edition)", November 20, 1963.

<sup>37</sup> National Association of Towns and Villages (1963a), p.3.

<sup>38</sup> National Association of Towns and Villages (1963b), p.1.

<sup>39</sup> National Association of Towns and Villages (1963c), p.1.

<sup>40</sup> National Association of Towns and Villages (1963d), p.1.

<sup>41</sup> National Association of Towns and Villages (1963e), pp.1-2.

<sup>42</sup> National Association of Towns and Villages (1972), p.205.

<sup>43</sup> National Association of Towns and Villages (1964), pp.12-3.

<sup>44</sup> National Association of Towns and Villages (1964), p.8.

<sup>45</sup> According to the Secretariat of the House of Representatives (1961), Mr. Kurogane, the Chief Cabinet Secretary was elected from the old Yamagata district.

<sup>46</sup> Institute of Local Finance (1964) (ed.), p.14.

<sup>47</sup> Shibata (1975), p.334.

<sup>48</sup> Murakawa (1986), pp.103-4.

<sup>49</sup> Murakawa (1986) stated that this is an opportunity for the further realization of policy objectives of the LDP during the budget compilation, and has paved the way for the budget compilation under the leadership of the LDP.