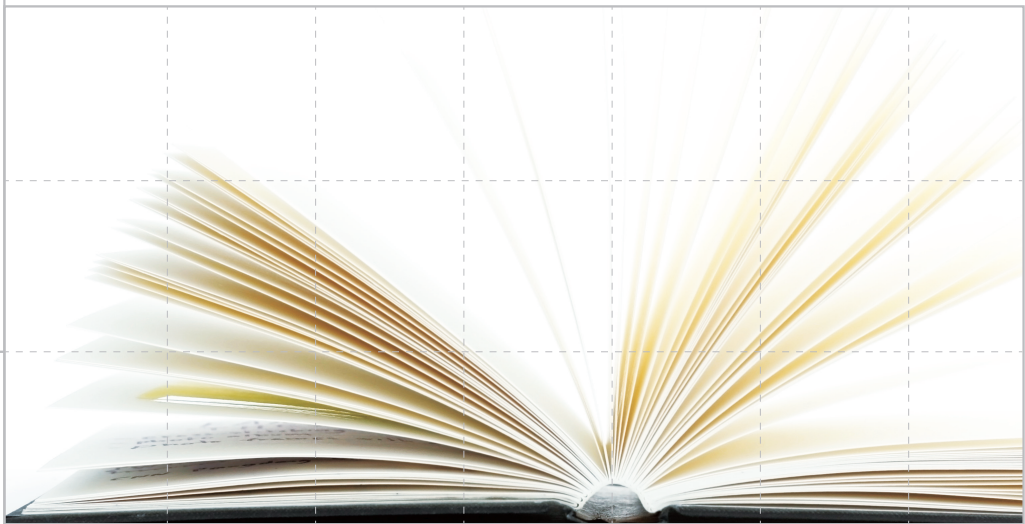


2009~2011

The List of Publications

2012



The List of Publications(2009~2011)

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Preface

The Korea Institute of Public Finance (KIPF) was established in July 1992 for the purpose of policy-oriented research and analysis in all aspects of taxation and public finance, assisting the government in formulating national tax policies and consequently contributing to the nation's economy.

Since its foundation, KIPF has played a critical role in the development of tax and budget policies and the improvement of tax administration. This success has been achieved thanks to KIPF's extensive research efforts and active recommendations of policy alternatives. With the grand opening of the Research Center for State-Owned Entities in 2009, there have been substantial changes and improvements to the management policies of state-owned enterprises.

During the recovery from the unprecedented economic downturn that resulted from the global financial crisis, tax and fiscal policies have acted as important tools in the implementation of sound economic decisions. This, in turn, raises the importance of in-depth research in producing creative policy alternatives within KIPF. Policy research on state-owned entities also becomes more crucial for maintaining sustainable economic growth, considering their roles within, and contributions to, our economy.

This publication provides studies and research conducted by KIPF in the areas of fiscal policy and taxation, which serve as the backbone of the nation's economy.

I sincerely hope this book, a product of hard work by our staff, will be beneficial to the government, various enterprises, citizens and researchers of this field.

President Cho, Won Dong

09-01	Effects of Public Transfers on Private Transfers and Consumption Expenditures	3
	<i>Myung-Jae Sung · Ki-Baeg Park</i>	
09-02	A Study on Income Deduction System of Personal Income Taxation in Korea	4
	<i>Myung-Jae Sung · Young-Jun Chun</i>	
09-03	Tax Credits and Medical Expenditure	6
	<i>Byung-Mok Jeon · Myung-Jae Sung · Hyun-Woong Shin · Young-Sok Shin</i>	
09-04	Rethinking the Taxing Rule on Direct Investment Abroad: Residence Principle vs Territorial Principle	7
	<i>Jongseok An · Jaeho Cheung</i>	
09-05	Determination of Tax Burden on Smoking, Drinking and Gambling	8
	<i>Sang-Won Park · Heechul Min</i>	
09-06	The Effect of National Pension Reform on Households' Savings and Labor Supply	9
	<i>Myung-Ho Park · Byung-Hill Jun</i>	
09-07	A Study on Measuring Government Expenditure Efficiency across Countries	10
	<i>Hyung-Soo Park · Deockhyun Ryu</i>	
09-08	Fiscal Policy Directions for Low-carbon Green Growth Industries in Korea	11
	<i>Seung-Rae Kim · Hosin Song · Jiyoung Kim</i>	
09-09	Macroeconomic Effects of Sectoral Government Expenditures in Korea	12
	<i>Seung-Rae Kim · Hosin Song · Woochul Kim</i>	
09-10	A Study on the Effective Asset-Transfer Taxation	13
	<i>Jin Kim</i>	

09-11	Intergovernmental Fiscal Relations Between Central Government and Large Metropolitan City	14
	<i>Junghun Kim · Hyun-A Kim</i>	
09-12	Policy Agenda for Performance-based Budgeting in Local Governments	15
	<i>No-Wook Park · Jonghak Weon</i>	
09-13	Policy Agenda for Improving Performance of Public spending on R&D Activities and of Performance Management System of R&D Programs	16
	<i>No-Wook Park · Hosin Song</i>	
10-01	The Way to Increase Tax Revenue after Financial Crisis	17
	<i>Jongseok An et al.</i>	
10-02	The Effect of Political Structure on the Fiscal Policy	18
	<i>Sang-Won Park et al</i>	
10-03	Changes in Korean Tariff Structure under the New Free Trade Agreements	21
	<i>Jaeho Cheung · Hongshik Lee</i>	
10-04	The Economic Effects of Deficit-financed Tax Cut in Korea	22
	<i>Seung-Rae Kim · Deockhyun Ryu</i>	
10-05	The Design and Economic Effects of Carbon Tax in Korea	23
	<i>Seung-Rae Kim · Jiyoung Kim</i>	
10-06	An Analysis of the Effect of “The Gas Price Tax Rebate” and “The Comprehensive Real Estate Tax Rebate” on Household Consumption Expenditures, with Policy Implications	25
	<i>Heonjae Song · Myung-Jae Sung · Sun Go</i>	

10-07	
A Study on Local Primary and Secondary School Finance in Korea	26
<i>Sun Go · Jin-Yeong Kim</i>	
10-08	
Current and Future Tasks for Desirable Fiscal Consolidation Policy	27
<i>Hyung-Soo Park · Hosin Song</i>	
10-09	
Application of Accrual Accounting and Full-cost Information in the Central Government's fiscal Management	29
<i>No-Wook Park · Hyung-soo Park · Hosin Song</i>	
10-10	
Long-term Projection of Social Insurances and Policy Reforms	30
<i>Byung-Mok Jeon · Eun-Kyung Lee</i>	
10-11	
The Introduction of Capital Gains Taxation on Financial Assets in Korea	31
<i>Beom-Gyo Hong · Jin-Soo Kim</i>	
10-12	
The Size of Underground Economy and Policy Implications	32
<i>Jongseok An et al.</i>	
10-13	
Tax Policy Direction on Financial Investment Product after the Enactment of Korean Capital Market Act of 2009	33
<i>Younghoon Ro</i>	
10-14	
Constitution and Fiscal Institutions	35
<i>Junghun Kim et al.</i>	
10-15	
Effectiveness and Redistributive Effects of Policies to Raise Fertility in Korea	36
<i>Joonook Choi · Heonjae Song</i>	
10-16	
Fiscal Decentralization and Regional Economic Convergence in Korea	37
<i>Junghun Kim</i>	

11-01	Changes in Economic Environments and the Reform in Tax System	38
	<i>Jongseok An · Young Jun Chun</i>	
11-02	The Effect of EITC on the Labor Supply and Welfare of Low Income Households in Korea	39
	<i>Heonjae Song · Young-Jun Chun</i>	
11-03	Joint Distributions of Income, Assets, and Debt and Their Policy Implications	40
	<i>Myung-Jae Sung</i>	
11-04	Global Financial Crisis and Housing Markets: Its Tax and Fiscal Policy Implications	41
	<i>Younghoon Ro</i>	
11-05	Studies on WTO Consistency of Tax and Fiscal Policies	44
	<i>Jaeho Cheung · Dukgeun Ahn</i>	
11-06	Reform Proposal on Korean Property Tax System Based on its Functions	45
	<i>Myung-Ho Park</i>	
11-07	An Analysis of Determinants of Taxpayer Compliance: An Experimental Approach	46
	<i>Myung-Ho Park · Byung-Hill Jun · Myeonghwan Cho</i>	
11-08	Welfare Financing Policy: Present and Future	47
	<i>Byung-Mok Jeon · Sang-Won Park</i>	
11-09	How to Finance Unification Costs	48
	<i>Joonook Choi</i>	
11-10	A Study on the Fiscal Impact of Demographic Change	49
	<i>Hyung-soo Park · Seung-Hyun Hong</i>	

11-11	
Impact of Aging on Elderly Health Care Expenditure in Korea	50
<i>Eunkyeong Lee</i>	
11-12	
A Study on the Fiscal Risk of Public Credit Guarantee	51
<i>Hosin Song · Seokjin Woo</i>	
11-13	
A Study on the Efficiency of Welfare Program(I)	
: Focused on Local Government and NPO	52
<i>Jonghak Weon · Wonik Son · Taekyu Park · Kwang-Seok Lee</i>	
11-14	
An Analysis of Local Government Amalgamation in Korea	55
<i>Junghun Kim</i>	
11-15	
Financing Structure and Pricing Mechanism of Public Enterprises	
: the Case of Korea Expressway Corporation	56
<i>Jiyoung Kim · Jung S. You · Junghun Kim</i>	
11-16	
The Managerial Autonomy and Performance of Public Enterprises	57
<i>Jiyoung Kim · Kyoung-Sun Heo</i>	
11-17	
Corporate Governance and Performance of SOEs in Korea	58
<i>Kyoung-Sun Heo · Young-Jae Ra</i>	
11-18	
Quasi-fiscal Activities of SOEs in Korea	60
<i>Joonok Choi</i>	

The Estimation of User Costs by Industries in Korea(1970~2006)	63
<i>Hak K. Pyo · Woocheol Kim · Eunkyung Jeon</i>	
Fiscal Policy Scheme for Small and Efficient Government	64
<i>Seong-Suhn Kim</i>	
The Influence of Disparity between Control and Ownership Rights on Book-Tax Reporting Differences	66
<i>Sang-Wook Lee · Bong-Geul Chun</i>	
Fiscal Indicators, Fiscal Coverage and Central Bank	67
<i>Dong-Suk Oak</i>	
Basic Study for Simplifying the Tax Law	68
<i>Wan-Souk Kim · Jin-Soo Kim</i>	
Income Reconstruction System and Tax Administration	70
<i>Yu-Chan Kim</i>	
A Study on Reform of Corporate Income Tax Law for the Adoption of International Financial Reporting Standards	71
<i>Tae-Sup Shim et al.</i>	
International Comparative Approach to the Effective Corporate Tax Rate	73
<i>Young Lee · Myeonghwan Cho</i>	
A Study on Income Contingent Loan Repayment and Related Issues	74
<i>Young Lee · Byung-hill Jun</i>	
Accounting and Tax Issues on the Carbon Cap and Trade Program	75
<i>June-Q Lee · Moonchyl Kim · Sang-Won Park</i>	
A Policy Recommendation for Proliferation of Charitable Contribution	77
<i>Won-ik Son · Soon-tae Lee · Sae-kyung Park</i>	
Performance Management and Intergovernmental Fiscal Relation : Focusing on Social Services	79
<i>Jonghak Won · Youngjin Yoon · Young B. Lee · Jaewon Lee</i>	
Rewriting Korea's Income Tax Law	83
<i>Wansouk Kim · June-Q Lee · Seong-Sik Lee</i>	
Tax-benefit Microsimulation Model: KIPFSIM10	85
<i>Myung-Jae Sung · Byung-Mok Jeon · Heon-Jae Song</i>	

A Study on Changes in Tax Administrations and Tax Laws of Major Foreign Countries When They Adopted IFRS <i>Tae-Sup Shim et al.</i>	86
Policy study for further improvement on designation and classification system of public entities <i>Jhungsoo Park · Taebeom Yun · Kyoungsun Heo</i>	87
A Study on the Tax System Related to Corporate Bankruptcy <i>Wan-Souk Kim · Ji-Sun Chung</i>	90
Performance Limit of Public Organization's Sustainability Management <i>Young-Jae Ra · Tae-Beom Yun</i>	93
A Study on Measures to Improve VAT Collection by Adopting Reverse Charge System <i>Jae-Jin Kim</i>	95
Privatization Index <i>Ki-Baek Park · Sang-Won Park</i>	97
Corporation's Quasi Tax Burden and Policy <i>Wonik Son</i>	98
Essay on the Productivity of Public Enterprises <i>Jiyoung Kim</i>	100
Privatization of State Owned Enterprises in Korea : Performance Assessment and Policy Direction <i>Jhung-soo Park · Seok-hui Park</i>	101
A Study on the Estimation of Corporate Tax Burden and Tax Base using Firm Level Data, and the Effect of Corporate Tax Burden on Firm's Investment Behavior <i>Hosin Song · Bong-Geul Chun</i>	104
About KIPF	107
Executives	108
▪ Research Staffs	108
▪ Research Fellow	110
▪ Associate Fellow	112
▪ Visiting Fellow	114



The List of Publications(2009~2011)

Research Papers

Effects of Public Transfers on Private Transfers and Consumption Expenditures

Myung-Jae Sung · Ki-Baeg Park

Over the last decade, government welfare expenditure sharply increased together with sharply increasing national burden to cope with rapidly expanding income inequality in Korea. It is generally believed that national burden increases as much as the increase in tax burden. Therefore, the recent increase in welfare expenditure has often been criticized for its overspeed with the resulting heavy fiscal burden.

Sometimes, it is quite possible that government or public welfare expenditures including public pension layouts crowd out private transfers rendered between relatives and/or friends to support living expenses, which are quite popular in developing countries where social security systems are not sufficiently established. If there exist strong crowding-out effects between private and public transfers, the overall net burden of individuals will not increase much when an increase in public welfare expenditures is financed by the tax increase since private transfers will decrease due to the crowds-out. In this case, the speed of tax increases may not be a serious problem, since total burden of individuals can increase at a moderate rate due to the decrease in private transfers. The only differences are reallocation of burdens between individuals and, also, who bears the costs of welfare transfers between government and individuals. In this sense, the political pressure or burden can be mitigated by the crowds-out between private and public transfers.

In practice, the government role of income redistribution could often be overvalued without considering the relation between private and public transfers, to the extent of redistributive effects of crowded-out private transfers.

In this report, we find that public transfers crowd out private transfers by about 13 percents in Korea, according to regression analysis using the Household Income and Expenditure Survey for the year 2008.

A Study on Income Deduction System of Personal Income Taxation in Korea

Myung-Jae Sung · Young-Jun Chun

Korean personal income tax (PIT) system can be characterized by its low levels of income deductions depending on individual demographic characteristics and also by its relatively large scales of other deductions. Therefore, PIT burdens hardly vary with the household sizes and do not show the economies of scale in Korea.

Low levels of such deductions generally yield limited effects on child-births and do not sufficiently encourage to foster big families with many young dependents, i.e. children, and/or the old. In this sense, it is recommended to reform the deduction structure of PIT to cope with the problems of low child-births and rapid population aging.

There exists a huge differential in PIT burdens between wage/salary income and business income of self-employed due to the asymmetric applications of income deductions. Only basic deductions depending on demographic characteristics are allowed to business income, whereas various income deductions including basic deductions are applied to wage/salary incomes. Differentials in income deductions between various types of incomes aim to balance consequential PIT burdens between incomes, due to the much lower income reporting rates of business income earners, while almost all wage/salary incomes are reported to the tax authorities in the course of tax filing with withholding taxes by employers.

Recently, however, the share of business income reported to the tax authorities has risen remarkably since 2000 when the National Tax Service introduced many systems to promote income reporting rates such as receipt lotteries and additional income deductions for credit card usages and cash receipts. Due to the recent changes in tax environment, PIT burden of business income becomes heavier than that of wage/salary incomes. In order to mitigate the revised differentials in PIT burdens, it is recommended to allow more income deductions to business income; a special deduction for medical expenses is a good candidate.

In the short-run, it is desirable to raise the income deduction rates applied

to high wage/salary income earners, because their PIT burdens are much higher than those of business income. Considering low-births and rapid aging problems, it is recommended to increase basic deduction levels together with the reduction of wage/salary income deductions.

Tax Credits and Medical Expenditure

Byung-Mok Jeon · Myung-Jae Sung · Hyun-Woong Shin · Young-Sok Shin

Income deduction of medical expenditure is introduced to relieve taxpayer's burden. This also induces unexpected increase of medical demand because of the price effect. The income deduction of medical expenditure decreases taxpayer's real price of medical services. This book estimates price elasticity of medical expenditure and explores policy alternatives to relieve taxpayer's medical costs. We also review income deduction of medical cost of advanced countries and derive short-term policy implications.

Using Korean household survey, we estimate price elasticity of medical expenditure. Change of tax price comes from income tax rate cut in 2005. When we use the data that can claim income deduction of medical costs, the elasticity is -0.16. Which is at the lower end of other countries case, -0.2 ~ -0.5 for U.S. and Canada. Though the elasticity is smaller than those of other countries, we can verify that income deduction of medical costs increases taxpayer's medical demand.

Considering other countries demand side policies, we propose a health saving account instead of income deduction of medical costs. New proposal can control additional increase of medical demand which comes from current income deduction policy. And this also improves equity among taxpayers.

This book also proposes several other policy alternatives. Under the current regime, we need to subtract medical cost paid by private insurance companies from the deductible medical expenditure. Secondly, the scope of income deduction needs to be reduced under diagnosis, cure or treatment, mitigation standards. Thirdly, income deduction of medical equipment purchasing costs may be reviewed. Costs for eye glasses, contact lens, hearing aid, etc are normal cost covered by basic deductions.

Rethinking the Taxing Rule on Direct Investment Abroad: Residence Principle vs Territorial Principle

Jongseok An · Jaeho Cheung

This study investigates the effects of changing the tax regime on direct investment abroad from the residence principle to the territorial principle in Korea. Theoretically, the residence principle is expected to be neutral to capital export and therefore to ensure the efficient resource allocation in the world economy. However, the tax practices in the real world are different from the ideal residence principle. Thus we examined the tax practices in Korea and other countries, discussed the problems of the practices, and tried to find the way to improve.

Specifically, we examined the effects of residence tax in Korea on international competitiveness of Korean multinational corporations and the repatriation of income from foreign affiliates of Korean multinational corporations. We also investigated the expected effects of change in taxing rule from the residence principle to the source principle on direct investment in low tax countries, tax revenue in Korea, and incentives for transfer pricing. And we concluded that the change may mitigate the problem of current tax system with little negative effects. In the last section, we discussed the way to move from the residence principle to the territorial principle in taxing income from foreign affiliates of Korean firms.

Determination of Tax Burden on Smoking, Drinking and Gambling

Sang-Won Park · Heechul Min

We study the rationale to levy tax on smoking, drinking and gambling and search for factors to explain tax burden on them, with examining the previous literature such as optimal taxation theory, Pigouvian charges to reflect external cost, paternalism and irrational consumption, demerit goods argument and political economy approach. Especially, through political economic model, it is shown that the change of social atmosphere and ethical value assessment can affect tax burden.

The case study of tobacco tax in U.S. and EU, and gambling tax in U.S. reveals that political concern for interested party and social perception can have large impact on tax burden on each goods. The empirical analysis using 40 countries data shows that the impact of government's fiscal need is significantly positive. The similar argument can hold for tobacco, liquor and gambling tax in Korea. With this understanding, it is suggested that government should establish better the purpose of imposing excise tax with focus on economic argument rather than fiscal need or political concern.

The Effect of National Pension Reform on Households' Savings and Labor Supply

Myung-Ho Park · Byung-Hill Jun

This paper investigates the effect of the National pension reform in 2007 on households' consumption, saving and labor supply behaviors. We employ a stochastic life-time utility maximization model with flexible labor supply to calibrate the effects of changes in the retirement income replacement ratio. Considering that the decrease in the replacement ratio varies by a person's socioeconomic conditions, the calibration is conducted at two rates of reduction in the replacement ratio: 20% and 50%. We find that saving increases over all ages but there are no substantial changes in labor supply after the fall in the replacement ratio. This result argues for the life-cycle model over the buffer-stock saving model. We conclude that a tax incentive is not quite necessary to encourage additional savings for retirement since households increase their savings voluntarily in response to reduced pension wealth.

A Study on Measuring Government Expenditure Efficiency across Countries

Hyung-soo Park · Deockhyun Ryu

The adequate measurement of government expenditure efficiency is a difficult empirical issue and the literature on it, particularly when it comes to aggregate and international data, is rather scarce. Our contribution in this study is threefold: first we discuss and survey conceptual and methodological issues related to the measurement and analysis of government expenditure efficiency. Second we construct both efficiency composite indicators and DEA(Data Envelopment Analysis) input-oriented efficiency scores of 8 functional government expenditures for 30 OECD countries. For health and education expenditure we also construct both for more than 100 countries. Third we combine efficiency scores with a Tobit analysis to see whether exogenous, non-discretionary factors play a role in explaining health and education expenditure inefficiencies.

On the second and third objective, the study finds that Korea's expenditure efficiency is top ranked for health and tertiary education expenditure, and also highly ranked for primary and secondary education, R&D, public order and safety, general public services and social protection expenditure. However Korea fills the middle rank for environmental protection expenditure and bottom rank for SOC infrastructure expenditure.

Fiscal Policy Directions for Low-carbon Green Growth Industries in Korea

Seung-Rae Kim · Hosin Song · Jiyoung Kim

In recent years, green fiscal reform becomes a credible option in the ongoing policy debate over how best to address global warming and to comply with implementing the national 'low-carbon green growth' agenda.

This paper explores how the government should reform the fiscal system to improve both the environment and industrial competitiveness in Korea. It provides a comprehensive discussion of environmental fiscal measures in OECD countries and discusses the economic implications of applying these policies. In particular, it focuses on how to design efficient tax and fiscal policies for promoting low-carbon green growth industries, and on how to recycle the revenues raised by the environmentally-related levies such as carbon taxes.

Macroeconomic Effects of Sectoral Government Expenditures in Korea

Seung-Rae Kim · Hoshin Song · Woochul Kim

This study is a step toward the quantitative policy evaluation for macroeconomic effects of sectoral government expenditures in Korea. First, it uses a structural VAR approach to estimate the macroeconomic impacts of fiscal stimuli in a few major government expenditure categories. Then, it explores an operational optimal control CGE model of the Korean economy to compute the detailed macroeconomic effects of nine government expenditures in the face of recent global financial shocks. In particular, it focuses on investigating what would be the optimal paths for the sectoral government expenditure policies to guide the shocked economy toward its desired goals as compared to the autonomous response of the system in Korea. For the initial recession in the Korean economy, the results indicate that the optimal mix of sectoral government expenditure paths for all target variables would outperform the autonomous responses of the economic system significantly.

A Study on the Effective Asset-Transfer Taxation

Jin Kim

We study several policy suggestions for the enhancement of the Korean inter-generational transfer taxations based on economic modelling, empirical analysis, and international comparisons.

We examine the effects of inheritance and gift taxes upon the economic behavior of asset transfers among generations, which has recently shown an increasing trend. We introduce a multi-stage decision model of transferring monetary and real assets among generations, formalize the ratio of the effective average gift tax rates over inheritance tax rates as the opportunity cost of inter-vivos gift choice relative to inheritance bequeath choice, and highlight the meaningfulness of tax rate change into gift-inheritance mix in asset transfer decisions.

By using international comparisons with the OECD countries, we obtain several policy implications for the enhancement of the Korean inter-generational taxation system. Firstly, we find that its tax rates are relatively high, thus it's meaningful to consider the reduction of tax rates. Secondly, it is to be considered that the minimal asset price level for 'zero' taxation should be reduced. Thirdly, Korea needs to increase the flexibility in evaluation methods and evaluation criteria for transferred assets. Fourthly, Korea needs to promote the transfer from the old generation to the young generation with more vital entrepreneurship.

We report that not only micro tax policies but also macro fiscal and monetary policies are important to enhancing the efficacy and effectiveness of the Korean intergenerational tax system.

Intergovernmental Fiscal Relations Between Central Government and Large Metropolitan City

Junghun Kim · Hyun-A Kim

The local public finance policy in Korea often depends on the concept of “local governments.” Policy debates on increasing the share of local tax revenue and local expenditures are typical examples. However the heterogeneity of local governments is very pronounced in Korea due to the economic dominance of the local governments in the Seoul capital region. Ignoring such heterogeneity results in mis-match between policy objectives and policy tools. Many the local public finance policy, including the introduction of Local Consumption Tax and Local Income Tax next year, results in enlarging the net fiscal benefit differentials Seoul capital region already enjoys. This report conducted an empirical study to verify that the heterogeneity of local governments in Korea is so large that the panel data analysis often adopted to analyze the local public finance in Korea is not permissible. A policy implication of this study is that the current effort to simply enlarge the local tax base is not desirable and the effort to enhance the linkage between fiscal capacity and expenditure responsibilities of the local governments in Seoul capital region is more important.

Policy Agenda for Performance-based Budgeting in Local Governments

No-Wook Park · Jonghak Weon

This paper develops policy agenda for introducing performance-based budgeting into local governments. The policy agenda is focused on the following areas: (1) developing performance information of spending programs, (2) developing relevant cost information of spending programs, (3) developing good program structure and (4) how to use performance information in budget allocation. The policy recommendations are derived experiences from performance budgeting in Korean central government and other OECD countries, while they reflect characteristics of local governments whose function is more focused on delivering public services than developing policies.

Policy Agenda for Improving Performance of Public Spending on R&D Activities and of Performance Management System of R&D Programs

No-Wook Park · Hosin Song

This study is carried out to develop policy agenda for improving the effectiveness performance management system of public R&D programs and of public spending on R&D activities. The first part of this study examines the effects of tax incentives and government subsidies for firms' R&D activities. Particularly, it empirically examines the effects of government subsidy on firms' R&D activities and develops policy agenda. The second part of this study examines issues involved in the performance management of R&D programs. It suggests that, for the purpose of setting priorities of public R&D programs, it is imperative to find an effective way of assessing the economic and social impact of R&D programs. In particular, it stresses that improving the objectivity of expert panel and using relevant quantitative performance information of R&D programs are important.

The Way to Increase Tax Revenue after Financial Crisis

Jongseok An et al.

After financial crisis, budget deficit sustainability became important issues in public policy. Government budget in Korea was surplus by 0.4% of GDP in 2007. However, it became to deficit by 4.1% of GDP. The national debt increased from 30.1% of GDP to 34% during the crisis. In addition, there are many other factors that are supposed to increase budget deficit: population aging; the strained relation between North and South Korea; and slow down of economic growth, etc. Considering these changes and factors, one can think that there may be a situation in the near future in which the government should increase tax revenue through changes in tax rules.

In this report, we investigate trends of tax revenue of national tax items: individual income tax, corporate tax, VAT, liquor tax, cigarette tax, energy and environmental tax, individual consumption tax, tax on capital gains, gift and inheritance tax, and customs tariff. We also analyze factors that affect revenue of these taxes and discuss future direction to increase tax revenue. We do not intend to prescribe policy measures for certain specific purposes or targets about government revenue or budget deficit but like to evaluate all the possible policy options and provide guidelines for tax reforms to increase tax revenue.

The Effect of Political Structure on the Fiscal Policy

Topic 1: The Role of the Legislature and the Executive in Annual Tax Changes

Sang-Won Park

This study aims to determine the role of the legislature and the executive in annual tax changes in Korea. Every year the ministry of strategy and finance in the executive announces the plan of annual tax changes and submits tax bills to the national assembly. The legislature examines them and modifies, rejects, or passes the bills. We compare the initial suggestion of the executive and the final tax bill passed by the legislature and find the followings. First, the tax abatement and exemption is the one which the legislature modifies the executive's tax proposal most. Second, certain items have been repeatedly at issue during amendment. Third, the legislature tends to cut tax burden relatively, Last, the frequency of the legislature's modification depends a lot on the ruling party's share in the assembly.

Topic 2: Estimation and Comparison of Income and Income Tax Distribution, and its Redistributive Effects by Each Administrative Governments in Korea

Myung Jae Sung

This paper is to estimate and compare the distributions of income and income tax incidence derived by the changes in related tax laws by the administrative governments from YoungSam (YS) through Dae-Joong (DJ) and Mu-hyeon (MH) to Myung-Bak (MB) administrative governments in Korea in terms of distributional characteristics and income redistribution. The administrative governments emphasizing equity and redistribution issues tended to change the related tax laws towards increasing progressivity of income tax burden, while those emphasizing efficiency and competition tended to relieve income tax burden. The redistributive effects through income taxation became smaller in the YS, DJ and MB administrative governments, while they were inflated in the MH administrative government.

The redistributive effects turned out to depend heavily on the changes in effective income tax rate. Unlike the perception conceived by the general public, the progressivity of tax burden is negatively correlated with its income redistributive effects. This is mainly because the progressivity of income tax is too high in Korea. High progressivity implies high concentration of income tax burden. In order to increase the redistributive effects of income tax, it is recommended to increase the income tax revenue especially of the middle income classes the effective tax burdens of which are quite low. This can be done by lowering the income tax exemption level. In this case, it is inevitable to face lowered progressivity and potentially severe tax resistance.

Topic 3: The Effect of the Elections on Government Expenditure in Korea

Hosin Song and Byung-Hill Jun

In this study, we attempt to estimate the effect of the elections on government expenditure in Korea. In particular, we focus on local government elections as well as the direct presidential elections. We find that the association between presidential elections and general government expenditure has been weakened and that some local government expenditures have shown cyclical behavior according to the timing of the election.

Topic 4: The Effect of the Political and Populational Structure on Introduction of Childbirth Grants of Local Governments.

Jiyoung Kim

This paper explains what determined the introduction of childbirth grants across local governments in Korea. The childbirth grant is a one-time cash grant that a local government provides to its resident who gives birth. In Korea, local governments make decisions on the childbirth grants autonomously. They decide the implementation and the budget size of the grants. And the funding is financed by local governments without supports from the central government. Many Korean

local governments in the rural area began to implement the childbirth grant in the early 2000s, and it is now widespread throughout the country. Consequently, 145 out of 230 local governments have adopted the childbirth grant. Using a cross-sectional regression analysis, I investigate the relationship between the introduction of the childbirth grants and the political characteristics of the locality. The result shows that the locality whose governor belonged to the ruling party had higher probability to adopt the childbirth grant. It was less likely to introduce the childbirth grants if one party was dominating the local government and the council. Also the share of the women in childbearing age affected the probability to introduce the childbirth grants.

Topic 5: Who should control the local government's fiscal policy under asymmetric information?

Myeonghwan Cho

This chapter studies the efficiency of the intergovernmental fiscal transfers under the asymmetric information. In the model, the local tax revenue is a private information to each local government. If the uncertainty of local tax revenues is high enough, the local governments have an advantage, and otherwise the central government has an advantage to determine the amount of intergovernmental transfers. In addition, if the central government cannot verify the local governments' announcements, they do not voluntarily disclose any information about their private information.

Changes in Korean Tariff Structure under the New Free Trade Agreements

Jaeho Cheung · Hongshik Lee

Korea has actively engaged in Free Trade Agreements(FTA) negotiations since the beginning of 2000. Currently FTAs with Chile, Singapore, EFTA, ASEAN and India have entered into force. Korea-U.S. FTA and Korea-EU FTA was signed and waiting approval for ratification by the Korean National Assembly.

This study focuses on the change in Korea tariff rates after Korea-U.S. FTA and Korea-EU FTA entering into force. Additionally this study analyzes the pattern of trade between Korea and U.S., EU, China and Japan during 20 years. Under Korea-U.S. FTA, Korea would expect trade diversion effect with decreasing the trade volume from China and Japan. However, under Korea-EU FTA, Korea may expect trade creation effect rather than trade diversion effect.

Using CGE model, this study analyzes the effect of reducing tariff rates on Korea economy under Korea-U.S. FTA and Korea-EU FTA. The result of this study suggests that Korea would lower tariff rates under Korea-U.S. FTA and Korea-EU FTA with maintaining current tariff structure. Since 1984, Korea maintains 8% tariff rate on most of its final output. Korea would lower its tariff rate slightly, and lower especially the tariff rate of the products incurring trade diversion effect under Korea-U.S. FTA and Korea-EU FTA. Significantly reducing the tariff rates induce to decrease the trade volume from the FTA partners such as U.S. and EU. Therefore it is not appropriate strategy under new FTA.

The Economic Effects of Deficit-financed Tax Cut in Korea

Seung-Rae Kim · Deockhyun Ryu

This study investigates the welfare and macroeconomic effects of deficit-financed tax cut in Korea, which is topic of considerable interest in both policy-making and academic circles. In particular, the economy-wide effect of changes in corporate income taxation is an important question, since the burden of this tax is not necessarily borne by those upon whom they are levied. As discussed in the literature, the tax burden is shifted through changes in supply and demand behavior and thus through in all prices and quantities, in the allocation of resources, and in the distribution of after-tax incomes in the entire economy.

Using a simple overlapping generations general-equilibrium model, this study explores the long-run dynamic consequences of the recent 5%p decrease plan in corporate income tax rates in Korea, and quantifies the macroeconomic effects and intergenerational redistribution effects of such a change.

The results imply that, while the overall positive effects of corporate income tax cut on economic efficiency would be significant in Korea, policymakers could need to balance the competing policy objectives between efficiency, fiscal soundness, and intergenerational distributive equity over time.

The Design and Economic Effects of Carbon Tax in Korea

Seung-Rae Kim · Jiyoung Kim

Korea recently set an ambitious goal of cutting greenhouse gas emissions by 30 percent below expected levels in 2020, and established the Comprehensive Act on Green Growth to meet the emission target and promote eco-friendly investment. The government also prepared for a variety of measures of the green growth and will put those plans into action.

Nonetheless, the government needs to consider further the full environmental costs and other external costs in setting tax rates on energy, phasing out various exemptions and environmentally harmful subsidies, and introduce a carbon tax to curb CO₂ emissions in the near future.

Based on experience in some OECD countries, Korea could gradually (but ultimately) shift more some of tax burdens from income to energy, while addressing properly their potential impact on international competitiveness and distributional concerns.

According to this study, the appropriate size of carbon tax revenue would be about 10 trillion Won (approximately 1% of GDP) that could be used to promote eco-friendly investment and development in Korea. However, from experience in countries that have already implemented eco tax reform in Europe, we may need a gradual phasing-in of the environmental tax reforms and the use of a public information campaign for stronger incentives.

Moreover, there are still ways to go, even though the government got off to a first step to eco-sound fiscal policies. Compared with other OECD countries, Korea has less energy-efficient industrial structures with complicated fiscal policies and large differences of tax burdens on each energy-demanding sectors. In order to implement the Korea's new scheme successfully, a key theme "green taxes" would be essential to provide a greater efficiency gain through helping to 'get the prices right' associated with their environmental externalities.

Also, it is required to consider secondary instruments such as direct compensation payments, price support and tax exemptions for unfair burdens of

low-income households and more energy-vulnerable sectors. All those approaches might be offset of distributional consequences as mitigating the harmfulness of eco-motivated fiscal policies.

Lastly, it is pretty obvious that the more we delay action, the more cost we pay. If we invest green technology in recent economic slowdown, we will have a global initiative that would make our economy more competitive in the long run.

An Analysis of the Effect of “The Gas Price Tax Rebate” and “The Comprehensive Real Estate Tax Rebate” on Household Consumption Expenditures, with Policy Implications

Heonjae Song · Myung-Jae Sung · Sun Go

This research investigates the effect of “the Gas Price Tax Rebate” and “the Comprehensive Real Estate Tax Rebate” on household consumption expenditures in the economic crisis. Different from the Japanese shopping coupon program and the U.S. 2008 tax rebates, the two rebate policies in Korea did not directly aim at stimulating consumption. However, the contemporaneous economic downturn allows us to study the effects of the tax rebates on consumption expenditures in the economic crisis. The difference-in-difference estimators using the National Survey of Tax and Benefit(KIPF fiscal) panel data show that the Comprehensive Real Estate Tax Rebate had little effect on stimulating consumption. In contrast, the DID estimation results support that the Gas Price Tax Rebate had sizable positive effect on consumption expenditures. This implies that tax rebates to stimulate consumption in the recession would be more effective when targeted at those who have tighter income constraints.

A Study on Local Primary and Secondary School Finance in Korea

Sun Go · Jin-Yeong Kim

Korean local governments have recently increased voluntary investment in local primary and secondary schools. To better understand local school finance, we need to investigate how the interests of local residents are associated with investment in local schools. Though per-pupil funding for primary and secondary schools is highly equalized in Korea, the levels of school inputs and outputs vary considerably within and across localities. This allows us to analyze the effect of school characteristics on the local residential property values. The regression results show that many school characteristics are indeed capitalized into the sale and rental price of the apartments in the neighborhood. The empirical findings here imply that a marginal increase in investment in local schools can raise local residential property values while improving school quality.

Current and Future Tasks for Desirable Fiscal Consolidation Policy

Hyung-Soo Park · Hosin Song

In this paper, we do in-depth research on fiscal consolidation experiences of many countries. In particular, we focus on OECD countries' policy experiences for fiscal adjustment with through studies as well as a variety of empirical analyses, from which we try to draw some implications on the implementation of Korea's current fiscal consolidation policy.

This paper consists of 5 chapters. Chapter 1 consists of three sections. In section 1, we analyze the recent fiscal problems of advanced countries, emerging countries and Korea based on vast works of literature such as fiscal policy reports, statistics, projections and research papers on fiscal adjustments from individual nations and international institutes such as the IMF and OECD. In section 2, we focus on OECD countries' debt-soaring experience, from which we learn that most countries failed to downsize their debt-to-GDP ratios once they experienced a large deterioration of public finances regardless of efforts toward fiscal consolidation. In section 3, we recommend some fiscal policy instruments which are believed to be critical for fiscal consolidation of Korea. First, fiscal policy authorities need to retrieve some of their temporary expansionary actions which were implemented to counteract the recent crisis. Fiscal authorities need to take into account age-related spending which will soon become the most serious threat to the soundness of Korea's public finance. Moreover, fiscal authorities need to improve the mid-term fiscal planning system, performance-based fiscal management system and enforce temporary fiscal rules for fiscal consolidation. For the revenue side, we believe an additional tax scheme or a statutory marginal income tax rate increase is not needed at this point. Instead, fiscal authorities have to downsize the tax expenditure by reducing redundant tax exemptions and strive to capture hidden sources of income. Furthermore, the statutory corporate income tax rate should be converted into a flat rate system along with eliminations of some tax expenditure which are unrelated to positive externality.

In chapter 3, we concentrate on the case studies of three countries, Finland,

Sweden and Japan. The implication from the study is that the time required to restore fiscal deficits to fiscal surplus after a fiscal crisis can be too variable to predict. The same applies to the debt-to-GDP level.

In chapter 4, we do vast empirical works using the data of 26 OECD countries. We aim in finding what are the determinants of fiscal adjustment implementation, successful fiscal adjustments and expansionary fiscal adjustments via discrete variable estimation methods. We also try to consider both successful fiscal adjustment and expansionary fiscal adjustment simultaneously via bi-variate probit estimation to allow for correlation between them. Furthermore, we try to test whether non-Keynesian effects can be found statistically. Lastly, we look into the determinants of the fiscal adjustment duration using the Weibull distribution duration model estimation.

In chapter 5, we conclude with Korea's future tasks for fiscal consolidation.

Application of Accrual Accounting and Full-cost Information in the Central Government's Fiscal Management

No-Wook Park · Hyung-soo Park · Hosin Song

After local governments had adopted accrual basis settlement in 2007, new national accounting standards will be applied to each ministry of central government from Fiscal Year 2011.

Recently, many researchers have been studying on the introduction of accrual basis accounting system and its expected effect, new national accounting standards. But there was seldom research on how to take advantage of various information produced under new government accounting system in the viewpoint of government high rank policy makers or members of the National Assembly. Specially, though there was this attempt partially about local government, central government dimension is wholly lacking real condition.

While analyzing experience and on-going issue of New Zealand, Australia, the U.K. that introduced accrual basis accounting and budgeting system earlier than our country, we tried to present suitable direction taking into account historic background and current practice of our own government accounting. We presented various practical use of accrual basis accounting information and developed many fiscal indicators for macro-fiscal management and performance-based budgeting.

Long-term Projection of Social Insurances and Policy Reforms

Byung-Mok Jeon · Eun-Kyung Lee

This book analyzes long-term expenditure of 4 social insurances and suggests policy reforms for financial sustainability. Specifically we covers national pension, health insurance, unemployment insurance, work injury insurance. Under certain macroeconomic assumptions, national pension system shows slightly improved financial situation, However, the reasons are unclear whether inclusion of new 3 year data or model difference play a significant role. We suggest that development of comparable models is important to improve or evaluate current very large and detailed government model. Future medical expenditure projections show similar numbers with previous researches and large fluctuations with the change of income elasticity. To improve long-term fiscal soundness, we need to adopt aggressive cost control measures and then to widen health insurance premium base and to consider increase of contribution ratio. Future expenditure level of unemployment insurance and work injury insurance are not significant compared to health insurance or national pension. Unfortunately, reserve fund of unemployment insurance will deplete in 2012, 2013 according to operation accounts because of expenditure surge. We propose more tight benefit control and contribution increase. Work injury insurance is expected to show smaller budget size than previous projections since the work injury rate has dropped significantly recently. Work injury and unemployment insurance provide very limited financial information compared with national pension or health insurance. We strongly recommend more transparent financial operation of the insurances.

The Introduction of Capital Gains Taxation on Financial Assets in Korea

Beom-Gyo Hong · Jin Soo Kim

The financial capital gains from neither listed stocks nor financial derivatives are taxable in Korea. Originally, this non-taxation policy was intended to develop our financial markets to raise funds and boost economic development. But as our stock and financial derivative markets are now at a world-class level in terms of trading volume and infrastructure, this type of tax assistance has become outdated. Rather to improve the fairness of our tax system, the introduction of capital gains tax on the gains from financial asset trading is necessary.

One of the most worrisome aspects of this change is the likelihood of negative impacts on the financial markets. If there are ways to measure those impacts reliably on the market in advance, it would be straightforward for the government to carry out this change. Unfortunately, it is almost impossible to predict those impacts in a reliable way.

Currently, the consensus is to introduce capital gains tax on financial assets, that provides enough reason for us to look for a successful way to introduce the system when the prediction of market impacts is infeasible. Fortunately the case of Japan demonstrates a good example. Japan is known as the only country that successfully converted its tax system from transaction tax to capital gains tax on stock trading. Japan has gradually transformed its system to alleviate the impact on the market. Korea currently has a transaction tax system on stock trading just like Japan has had many years ago. Based on the Japanese experience, we have suggested gradual steps to successfully introduce capital gains tax on financial assets in Korea.

We have also examined the possibility of replacing inheritance tax by capital gains tax, considering the issues of double taxation in the current inheritance tax system. However our current capital gains tax system is yet to be developed in many aspects, thus it would be proper to review the possibility of replacing the system only after our capital gains tax system has become more comprehensive.

The Size of Underground Economy and Policy Implications

Jongseok An et al.

The Underground Economy means the part of economy that is not included in official statistics for national economy. When the size of underground economy is very large, economic policy based on official statistics might not be effective. If the causes of underground economy are tax evasion or the intention to avoid government regulations in labor market or financial market, the underground economy damages the fairness of tax policy and other economic policies.

Since the underground economy means the economy that is not revealed, it is very difficult to estimate the size of underground economy. Researchers tried to estimate the size and causes of underground economy in many different ways under various assumptions. But there is no one method dominating others.

In this report, we tried to estimate the size of underground economy in Korea as percentages of GDP using three different methods. First, we estimated the size of tax evasion by comparing the survey data on household consumption and income produced by National Statistics Office with tax return data. Second, we also estimated tax evasion by comparing Input-Output Data produced by the Bank of Korea with tax return data. Lastly, we estimated a structural equation model based on DYMIMIC(Dynamic Multiple-Indicator and Multiple-Causes Model). We estimated a model structured specifically for Korean economy and used time series data rather than cross section data. And we found that the size of underground economy in Korea decreased significantly in last ten years. In the last section, we discussed about policy implications.

Tax Policy Direction on Financial Investment Product after the Enactment of Korean Capital Market Act of 2009

Younghoon Ro

With the enactment of Financial Investment Services and Capital Market Act(FSCMA, hereafter referred to as “CMA”) in February 2009, investment funds and structured equity products expanded their market capitalization dramatically in Korea. Contrary to the previous separate special laws on securities, forwards, derivatives, trusts, they are now consolidated under the FSCMA regulations. It is no wonder that the regulation of the broad range of financial products under one FSCMA law entailed the intense competition among financial companies and the possible neglect of investor protection.

This study examines both the financial consumer protection and tax policy issues on investment funds and structured products which became very popular in the Korean capital market after 2000s.

In general, the investment fund tax rules are dictated largely by a country’s overall tax regime for individuals and enterprises, and these tax regimes vary substantially among countries. In the context of these basic tax structure, the choice of tax rules for investment funds require balancing three objectives: first, not go impede the development of financial intermediaries; second, to devise tax rules that are compatible those that apply to other investments; and third, to adopt tax rules that can be administered and enforced. Among the four major different approaches of taxing investment funds, Korea adopted some mixture of tax-advantaged, pass-through, and surrogate prototypes. Investment fund is in essence characterized by two elements: collectiveness and intermediateness. Currently in Korea the income from an investment fund realized by an individual investor is categorized as dividend and taxed according to the genuine dividend income. But the tax treatment of dividend, interest, and capital gains at the investment fund level and at the level of the investors needs major reformatory change when the capital gains taxation on stock and shares under the progressive global income taxation is considered in future.

Since 2003 the Korean market of structured product became the huge business

for banks and security companies. For example, the most popular two-asset reverse convertible type equity-linked securities(ELS) with knock-in barriers in Korea could offer a utility gain only for retail individual investors with the symmetrical information and analyzing know-how as the issuers. But in reality the retail investors bear knowledge asymmetry risk against the issuer, and tend to overpay. Also, there exists a possibility that the issuer's unwinding of a delta hedge position puts downward pressure on the underlying stock price to the investors disadvantage at redemption dates.

As the protection measure of retail investors, we suggest that customers understanding of the product should be enhanced through the compulsory listing of some ELS on the stock trade exchange rather than banning structured products completely (as is currently discussed in some countries). Other boutique type ELS sold privately to institutional investors does not need that level of customer protection if the two parties of investment contract fully share the full information of the product prospectus. Also, it would be an idea to introduce independent ranking that enables specific type of investors to see whether structured products add value to their portfolio or not.

Constitution and Fiscal Institutions

Junghun Kim et al.

The impact of constitutional changes, which are currently discussed in Korea, on the welfare of people is significant. This report therefore investigates the implications of constitutional articles related to public finance and devolution. According to the analysis in chapter 2, it is desirable to reinforce legislative branch's power on budgeting and accounting. However it is also desirable to delegate to executive branch the power to control the total size of budget to avoid common pool problem. According to the analysis in chapter 3, the constitution of Korea is such that it makes Korea one of the most centralized countries along with Nordic countries and Japan. Given the sizes of economy and population of Korea, however, it is desirable to make the constitution in Korea to fit more with decentralized system. The recent constitutional changes in France, Italy and Switzerland offer good case studies in this regard. In chapter 4, it was shown that, in a country like Korea whether a majority political party is commonly established, delegation approach with regard to public financial management is more desirable than contract approach, which is more suitable for a country where a coalition government is more commonly established. Therefore the analysis of chapter 4 supports the conclusion of chapter 2 which recommends the balanced power between legislative and executive branches in dealing with budgetary issues.

Effectiveness and Redistributive Effects of Policies to Raise Fertility in Korea

Joonook Choi · Heonjae Song

Although policies aimed at encouraging birth rate of Korea has been widely discussed in recent years, only few studies have been presented on the cause of low birth rate and the effectiveness of the policies. Hence, the fundamental issue still could be what factors determine fertility in Korea. It is essential to understand the cause of fall in birth rate of Korea. Nevertheless, the data could be improperly interpreted. This study first aims to analyze change in birth rate in Korea more precisely and to investigate the cause of sharp decrease. Next, we try to draw some policy implications to raise fertility based on our empirical analysis.

The lack of public awareness of the issue is a matter of concern because policies responsive to low birth rate may have a economic and social effect on our society. Among many considerations of that issue, the effectiveness of redistribution of fiscal policies responsive to low birth rate will be examined, as there have been few domestic studies.

Section II presents the model of determinants of birth rate in Korea using panel data. We find that private educational expenditure in household is an important factor in determining fertility decision. Section III examines the change and causes of a decrease in birth rate of Korea, and seeks for practical uses of fiscal policies which can be responsive to low birth rate. Section IV illustrates the effectiveness of childbirth grant policy. According to our empirical analysis the child birth grant affects potential mothers' new birth planning. Section V draws several implications relevant to policies responsive to low birth rate as well as the effectiveness of fiscal policies such as income redistribution.

Fiscal Decentralization and Regional Economic Convergence in Korea

Junghun Kim

This report analyzes the tripartite relationship between fiscal decentralization, regional economic growth and regional economic disparities. Its empirical research finds that per capita local tax revenue is the most significant control variable that affects regional economic convergence in Korea. What is surprising about this result is that the impact of per capital local tax on regional economic growth is positive rather than negative. The reason behind this counterintuitive result lies in the fact that local tax rates in Korea are the same across all local governments. The factors therefore that create different levels of per capita local tax revenue are tax exporting and property transaction taxes which are determined by the frequency of property transactions rather than local production or local income. What is required for more efficient and equitable regional economic growth in Korea is therefore local tax system reform which makes local tax revenue more proportional to local income.

Changes in Economic Environments and the Reform in Tax System

Jongseok An · Young-Jun Chun

This study investigates changes in economic environments which seem to affect tax policy and discusses effective measures to cope with the changes. Current literature referred to aging of population and globalization as the most important changes related to tax policy. In addition, we included welfare reform and unification of Korean Peninsula as important economic environments. In Korea, enlargement of social welfare and preparation for unification are subjects of animated controversy in these days.

The most important issue in tax policy raised by economic environment changes is increase in expenditures. Aging, enlargement of social welfare and the unification demand are expected to increase public expenditures. Adding up the numbers estimated in existing literatures we expect government expenditures to increase by 20% of GDP until 2050 compared to that in 2009. It means that the tax burden ratio should be doubled during the next fifty years. This study examined ways to cope with the increase in expenditure demand.

In addition, this study investigates the effects of the changes in economic environments on tax system of individual tax items. Especially, it examined the effects of aging and globalization on capital income tax at both individual and corporate level. It provided and discussed reform plans for individual income tax and corporate tax in the context of an aging and globalized society.

The Effect of EITC on the Labor Supply and Welfare of Low Income Households in Korea

Heonjae Song · Young-Jun Chun

EITC (Earned Income Tax Credit) was paid in 2009 for the first time in Korea. This study analyzes the effect of the EITC on the work incentive and welfare of the low income households in Korea. First, empirical analysis is exerted using National Survey of Tax and Benefit. Empirical results show that EITC induced more labor participation and working months of the households which belong to phase-in range, whereas it worked oppositely to the households in the plateau and phase-out range. Second, general equilibrium analysis is employed to complement the limitations of the empirical study. Policy simulation results based on general equilibrium model suggest that current EITC system generally raises employment with enhancing part-time labor, but it somewhat reduces full time employment and disposable income. However, if we focus on the lowest income group of households, EITC has all positive effects in terms of employment rate, full time labor, disposable income and household asset. Furthermore, policy simulations recommend rather increase of maximum EITC amount with the extension of the phase-in range than increase of phase-in rate to maximize the effect for the low income households. Comprehensively, the results of the empirical study and general equilibrium analysis imply that policy makers should consider extension of the phase-in range, increase of phase-in rate and increase of maximum EITC amount in order to design a new better policy.

Joint Distributions of Income, Assets, and Debt and Their Policy Implications

Myung-Jae Sung

This report estimates the joint distributions of income, consumption and assets using the National Survey of Taxes and Benefits (NaSTaB) compiled for the years 2007 through 2009, and analyzes short- and long-term effects of taxes and benefits. Distributional inequalities of assets and debts are much larger than that of income, although their inequalities shrink significantly if their orders are rearranged in line with that of income. This comes from the differences in the determinants of income versus assets/debts. It turns out that inclusion of imputed rents for assets reduces overall income inequality slightly. Personal income tax for wage and salary income and business income turns out to have positive income redistributive effect. On the contrary, consumption taxes have negative redistributive effects, although their absolute sizes are quite small in general. Due to the lack of necessary information contained in the NaSTaB, the distributional effect of property tax is not explicitly analyzed. However, it may not have negative effect, according to the findings of past studies. The relative inequality of long-run income derived by summing up incomes of three years is estimated to be much lower than that of annual income; the long-run income is less dispersed than the short-run income mainly due to the dilution of short-run income inequality caused by age differences or different location in a life-cycle. However, because there exist the asymmetry of life-cycle income paths for each income percentile and, also, because the income mobility declines over time, it is quite possible for the relative inequality of long-run income to increase in the very long run.

Global Financial Crisis and Housing Markets: Its Tax and Fiscal Policy Implications

Younghoon Ro

This study examines the 2008 Global Financial Crisis (hereafter called 'GFC') and its subsequent recessions' impact on housing markets in different countries, and tries to find the fiscal and tax policies to alleviate the negative after-effects.

In general, housing is not only a consumption good but also an investment asset with the potential to generate capital gains. That is, housing has the dual role of providing consumption services and being the form of capital asset in which the household puts its accumulated wealth. While the investment motive of housing capital demand becomes more important than the housing service consumption motive during a housing boom, the latter dominates the first when the market takes its downturn. So, in Chapter II we tried to figure out whether the apartment market in Seoul metropolitan area shows some sign of capital asset efficient market hypothesis. It was shown that the arbitrage condition of total returns consisting of capital appreciation and income returns holds at least in the Seoul metropolitan apartment market by comparing the sales price index series with its rental price index series during the period of years 1999 to 2011. The rental-to-sales price ratio (implying the degree of consumption goods price weight among its capital market value) tends to decline after the October 2001 when the sales price sharply climbed up, but it started to rise when the sales price was stabilized after the outbreak of GFC. It should be noted that the ratio itself was surveyed for each sample apartments independently from the denominator of the ratio, i.e., sales price.

Chapter II also explored what happened to both the sales and rental housing markets in Korea and other major advanced economies after the Global Financial Crisis in 2008. First, we made an international comparison study of housing price index movements among U.S., U.K., Japan and Korea before and after the GFC. We found that the volatility in housing price movements in Korea is much less than those of other major metropolitan cities in other countries. Aside from the differences in compiling the housing price index in Korea, we noted some institutional

factors leading to Korea's insufficient market price adjustment after GFC. Chonsei, Korea's unique form of housing lease contract in which landlord and tenant swap house and deposit money agreeing to net-out of rent and interest payments during the lease period, can be called 'Housing Repo'. With the Chonsei's dual role of housing loan and implicit rent in mind, it is believed to have some role in preventing many distressed houses from turning into foreclosures during the housing downturn in Korea. The so-called 'under-water' houses with its owner's equity being wiped out as price falls could not easily be abandoned by the owners because he is personally liable to both the mortgage lender and the tenant. With its incomplete sales market corrections, Korea is not predicted to possibly see troughs in 2012, and many households prefer the rental tenure mode of Chonsei rather than becoming home-owners. Since the two modes of Chonsei and monthly rental markets are substitutes and connected to each other, the recent high demand for Chonsei tenure led to the sharp increase in Chonsei deposit amount and also the landlord tried to convert Chonsei to monthly rental mode due to the low interest rate.

With the new view of Chonsei deposit money in mind, we emphasized the importance of neutral taxation of rental income between the two modes, and suggested some policy directions.

In Chapter III we compared the household net wealth change before and after the 2008 Financial Crisis in both the U.S. and Korea. U.S. Fed re-interview SCF (Survey of Consumer Finance) data showed that the GFC was a major blow to household net wealth during the 2007 and 2009 period. More than two-thirds of Americans saw their net worth decline during the recession, suffering a median drop of 18% according to the Federal Reserve study. When we compared the 2006 and 2010 Korean Household Survey's ten thousands families' balance sheets, the average net wealth, which is defined as a household's total asset minus their debts, decreased 4.8%, while the median wealth rose 8.5%. However, the lowest (1st) and the second income quintile family group suffered 20.5% and 14.9% loss of average net wealth which is equivalent to 46 months and 14.7 months worth of current income respectively. The similar figures of 21% and 12.1% loss of median net wealth were observed for the bottom two income family groups respectively. This differential impact of GFC on household net wealth according to the family income implied the necessity of property tax relief measures towards the low-income house-owners with high debt burden. To better understand the influences of Korean families' homeownership and tenure mode on their economic positions after the GFC, we regrouped the sample households on the basis of their house-ownership

and tenure mode into the following 4 sub-groups: ① single-house owning owner-occupying households, ② multi-house owning owner-occupier families, ③ renter families owning houses elsewhere, ④ renters without any house ownership. Wealthy households with high housing asset experienced a greater net wealth decline compared with Chonsei rental households with less real estate assets in their portfolio. Chonsei rental families performed the best in terms of keeping their net wealth intact. Their net wealth increased by 20%, while the owner-occupiers and the house-owners suffered 3.6% and 1.9% loss of net wealth respectively. The renters with the monthly rent contract lost 25.2% of their net wealth. Among the above 4 categories of families, two-thirds of the multi-house owning families and renters owning one house elsewhere had some form of borrowings, and the lowest two income quintile families had debt-service ratios of more than 22%. Especially, low-income renter families owning a house elsewhere had more Chonsei deposit debts than their current occupying home's Chonsei deposit claim to the landlord, which tends to restrict their mobility.

With these findings of GFC's impact on housing market and households, we proposed the following four major tax policy recommendations: ① abolition of the burdensome housing capital taxes based on gross property valuation and progressive property taxation of the aggregated housing value on the multi-house owners, ② introduction of property tax relief measures for the low-income families like the various U.S. states' circuit-breaker programs, ③ tax incentives bestowed for the highly mortgage debt-ridden families toward their deleveraging efforts, ④ solutions to the current problem of non-neutral income taxation on the Chonsei deposit's implicit rent and monthly rent.

Studies on WTO Consistency of Tax and Fiscal Policies

Jaeho Cheung · Dukgeun Ahn

This study aims to analyze tax and fiscal policies in a broader framework so as to draw policy implications for the future implementation in a more consistent manner with the WTO Subsidy Agreement.

Government support programs can be divided into two broad categories: tax incentive programs and fiscal policies. This study reviewed various tax programs and proposed the reform actions for tax exemption on overseas dividend incomes, tax credit systems, corporation tax systems, and value added tax systems. With regard to R&D programs that is currently the most prominent government support programs, we conclude that grant or direct subsidy programs may be more effective for fundamental research activities while tax incentive programs may be more efficient and WTO consistent for “near-market” or commercial research activities. Moreover, although R&D programs need not be completely abandoned due to potential legal problems under the WTO Subsidy Agreement, the government should be aware of the lesson that excessive promotion of governmental roles in R&D policies may induce unnecessary trade conflicts with trading partners in the WTO system.

Reform Proposal on Korean Property Tax System Based on its Functions

Myung-Ho Park

This study investigates reform proposals on Korean property tax system which are designed based on the main functions of property taxation. The main functions of property taxation are specified as follows: one is to finance public services by the benefit principle of taxation and the other is to improve the income redistribution. According to the analysis, the current property tax system is not aligned with these two functions. When we reconstruct the property tax system as a local tax under the benefit principle of taxation, tax rates may vary a lot among local governments because of differences in tax bases across local governments. In order to reduce local variations in the property tax rates, this study suggests the necessity of sharing tax bases among local governments at the provincial or national levels. When we reconstruct the property tax system toward improving the income redistribution function, property tax relief programs such as the 'circuit breaker' are necessary because of the regressivity of the property tax. This study shows, however, that the property tax system with progressive tax rates as well as the 'circuit breaker' program may improve the Gini index of income inequality a little, but much less than income tax does.

An Analysis of Determinants of Taxpayer Compliance: An Experimental Approach

Myung-Ho Park, Byung-Hill Jun and Myeonghwan Cho

This paper studies the effect of a non-pecuniary factor on tax compliance behavior. As a preliminary work, we consider a model in which taxpayer's utility is affected by non-pecuniary factors as well as by the after-tax income. In this model an individual with a high level of satisfaction is shown to evade less income if the non-pecuniary component is represented by taxpayers' satisfaction level with a current system. An experiment is designed and conducted to empirically test this hypothesis. Each subject is randomly assigned to one of four subgroups. Each subgroup is characterized by a tax schedule and a way of determining a tax schedule. More specifically we consider two tax schedules (a flat tax and a progressive tax) and two ways of determining a tax schedule (a majority voting and a dictatorship). In this set-up a heterogeneous treatment in a way of determining a tax schedule is expected to cause a difference in a satisfaction level among subgroups. Results from the experiment show that on average a taxpayer tends to report more income when a tax schedule is decided by a majority voting, which agrees with our anticipation. Despite the clear answer to the effect of the majority voting, results from our experiment does not provides a unified explanation on how the majority voting improves tax compliance behavior. In some cases a majority voting seems to lessen dissatisfaction when a less preferred tax schedule is imposed while in other cases a majority voting seems to reinforce integrity when a preferred tax schedule is imposed.

Welfare Financing Policy: Present and Future

Byung-Mok Jeon · Sang-Won Park

This book suggests a welfare financing policy based on current welfare expenditure, future burden, and experience of advanced countries. Korea's welfare expenditure is smaller than advanced countries' despite of individual income and tax burden adjustment. Korea shows similar income-welfare expenditure growth pattern as Japan. The pattern is not changing whether expenditure through State-Owned Entities is included. Considering the growth of income and the change of old age people share, Korea would confront significant welfare demand. Unfortunately, welfare demand cannot be met simply by increasing tax because the welfare expenditure difference is bigger than tax burden difference with other advanced countries.

Other advanced countries' financing experiences imply that social trust or national agenda can be important factors. Sweden shows that social trust can play an important role in tax increase. Joining EU system or reunification is the pivotal factor of Italy's and Germany's tax increase. Japan without them failed tax increase and suffered serious budget deficit. Foreign experiences also suggest that we need to be cautious on increase of old age expenditure during economic recession.

Efficiency, equity, and foreign experiences suggest that top priority of welfare financing policy would be individual income taxation and social security contribution. Then increase of consumption tax would be an option for efficiency and employment purpose. Additional ear-marked tax on alcohol, tobacco and gambling for welfare would not be a strong option since we have already other ear-marked taxes and current tax level is high enough. Improving governance structure of social insurances is also important to reduce economic incentive for expenditure increase.

How to Finance Unification Costs

Joonook Choi

In spite of the importance, few studies have dealt with the issue of financing unification costs in Korea in detail. Uncertainties about the ways and timing of unification is one of the reasons to make the discussion on the issue difficult. Even though this study can not overcome the inherent difficulty, this study tries to make one step forward in the discussion of the issue.

In Chapter II, we survey some of the previous studies relevant to the issue, and show the direction that should be pursued in further discussion. Chapter III lists options of financing unification costs and compare the pros and cons of each option. We also discuss whether funding before unification is necessary or rational. Chapter IV questions whether financing method should be different depending on the ways of unification. Chapter V contains more detailed discussion on the ways of financing unification costs, assuming that the unification is rather more sudden. Chapter VI summarizes the discussion.

A Study on the Fiscal Impact of Demographic Change

Hyung-soo Park · Seung-Hyun Hong

This study investigates the effects of declining population and ageing society on the overall public finance in terms of economic growth, income level, labor market, consumption-saving behavior etc. Since the demographic changes we are experiencing are naturally associated with slower growth in revenue and spending, we focus more on changes in structure rather than changes in the levels of revenues and spendings.

Two major factors that influence tax revenues are changes in the tax base and the tax system. Since change in the tax system is hard to predict, this study analyzes how future changes in the tax base will affect tax revenues, especially focusing on the qualitative changes in the diverse taxes. Both volume factors income, consumption, wealth and price factors interest rate, stock index, real estate price that affect tax revenues are considered in this analysis. Results show that demographic change will bring a higher level of income-related tax revenues, a moderately higher level of consumption-related tax revenues, but a decreasing or at least stagnant level of asset-related tax revenues.

In addition, long-term projections (until year 2050) under the current system are provided regarding major public pensions, public health insurance fund, expenditures on social safety net and public education etc. Our results show that public pension and health insurance costs will grow faster than their revenues, becoming a major burden on future fiscal management. To cope with this problem, authors suggest that governments continue its efforts to increase tax revenues and economize spending in the future.

Impact of Aging on Elderly Health Care Expenditure in Korea

Eunbyeong Lee

With Korean population rapidly aging, the growing health care expenditure for the elderly imposes a major financial burden on the country's public health care sector. This paper empirically examines how chronic diseases (hypertension, diabetes, heart disease, cancer etc) affect health care expenditure for the elderly in Korea. Using the first two waves of a panel data, KLoSA(Korea Longitudinal Study of Aging), I find that one increase in the number of chronic conditions increases one's annual out-of-pocket costs by 700,000 KRW (about \$700) and Insurer's financial burden by 1,050,000 KRW (about \$1,050). If the elderly population reduce the number of chronic conditions by 10% (0.114), the Health Care Fund(Insurer) can save 646,200 million KRW (about 646.2 million U.S. dollars), which amounts to 1.9% of the public health care expenditure in 2010. For robustness check, Korea Patient Sample and Korea National Health and Nutrition Examination Survey are used, and results are consistent.

The best policy to prevent sharp increases in the elderly health care expenditure is prevention of chronic diseases. Based on the KLoSA, I find that smoking and heavy drinking leads to the increase in the number of chronic conditions by the same amount, 0.17, while obesity increases the number of chronic conditions by 0.29. Therefore, obesity is the leading cause of chronic disease. For policy implications, I suggest a mechanism for reducing unhealthy behavior such as smoking, drinking and obesity. In addition, primary care system should be strengthened to prevent and manage chronic diseases. Coordinated care system would provide cost-effective care for those with multi-chronic conditions.

A Study on the Fiscal Risk of Public Credit Guarantee

Hosin Song · Seokjin Woo

In this paper, we investigate on the fiscal risk of public guaranteed credits with two approaches. One is done with use of aggregate data. The other is done with use of firm level data. We project how much public money will be injected into the 5 public credit guarantee agencies for 2011-2014 based on some specific scenarios as well as baseline scenario with the former approach. With the latter approach, we perform survival analysis for individual firms which have applied for credit guarantee. The results show that marginal firms which have received public guaranteed credits tend to have lower survival probability than those which have not. Moreover, we suggest how to assess the fiscal risk of public guaranteed credits using the results from the survival analysis.

A Study on the Efficiency of Welfare Program(I): Focused on Local Government and NPO

Jonghak Weon · Wonik Son · Taekyu Park · Kwang-Seok Lee

It is expected that the expenditure to social welfare service has been rapidly increased, which occupies 30% or more among the total Korean budget. The point is that the welfare budget is enormous and increasing rapidly, which leads to the speculation of the efficiency of the welfare budget. Considering the balance of budget in the policy making in the economy, the necessity of making efficient welfare administration is crucial to the universal welfare which results in expenditure increasing. Therefore the efficiency analysis of welfare projects is essential for the building of Korean-type welfare state.

The discussion on welfare efficiency can be categorized into two kinds: one is built-in-project, which derives from the difference between the people who pay welfare cost and the ones who benefit without contributing in other words free riders. The other is the inefficiency in the process of administration. The reason for noticing inefficiency in the process of administration is that even though the budget scale spending on welfare projects have increased, the welfare satisfaction has not kept up with, which is the result of inefficiency in its welfare administration. Welfare administration in this research is understood as welfare delivery system. Therefore this research categorizes the efficiency of the delivery system as the one in the inter-governmental relation (i.e. central government and local governments) and as a result some projects have been privatized which were coordinated by the government previously.

This research focuses on some cases in Kyungsangbuk-Do. It shows that on few levels such as central government, upper local government, lower local government and the front-line administrative unit prevent welfare projects from efficiency. In addition, as there is no control center in welfare projects, it is confirmed that welfare distortion occurs in the welfare administration such as leakage, welfare dependency, income conversion etc.

In order to rectify such welfare distortion caused by problems in the delivery system, this research suggests some alternatives: firstly, there should be a control

center which leads to consultation among governmental departments related to welfare projects. Secondly, welfare information data base should be utilized in the welfare policy-making. In addition, in the selection of beneficiaries made by the government, the standard set should be clear and consistent. Also welfare policy monitoring system should be introduced in order to overview the estimation of the policy outcome. Finally, the personnel who deal with welfare and work in local governments should increase work force in order to reduce the so-called funnel effect.

The third part of this report deals with an efficiency of the social welfare program performed by NPO. The social welfare service performed by NPO can be classified into 8 different areas; children-adolescent, the disabled, the elderly, low birth-rate, general social welfare, health, baby-toddler care, etc. The service for the elderly has the largest proportion (32.2%) among 8 different areas. The second largest is the area of children-adolescent with 24.6%, the third largest is the area of the disabled.

The result derived from the analysis of a case study shows that the tool of contracting-out to NPO for the social welfare service has an advantage of preventing undesirable expansion of the government organizations. Another advantage of the contracting-out to NPO is to guarantee a high quality service by selecting NPO through steep competition. It is also found that inefficiency of the social service may occur if a number of NPO is not enough to compete in the market. This type of inefficiency may not occur at the level of the wide-area local government, but it may occur at the level of the narrow-area local government due to lack of enough numbers of NPO.

A case study is performed to measure the efficiency and performance of the baby-toddler care service in Korea. The cost function for the baby-toddler care service is estimated to analyze the efficiency of the service. The connectivity between the government supports and evaluation results is also examined to evaluate the effectiveness of the evaluation system for the service. It is also confirmed that the government support for the baby-toddler care facilities has loose connectivity with the evaluation results for the facilities.

The policy recommendations are made to improve efficiency of the social service performed by NPO. The efficiency of social welfare service can be partly improved at least for the short-run by providing proper education and performance management for the facilities even if a steep competition among NPOs is not possible due to lack of enough NPOs. For the long-run, it is necessary for the

central government to establish a standard evaluation system and enforce the local governments to use the evaluation results for the allocation of budget of the social welfare service to achieve the efficiency of the services.

An Analysis of Local Government Amalgamation in Korea

Junghun Kim

The size of local governments in Korea is among the largest in OECD countries. Its average population is about 170,000 whereas that of many OECD countries the average remains below 50,000. However the high demand for local government amalgamation has given rise to the creation of a special law and a special committee. This report analyzes the reason as to why political demand for amalgamation is so strong in Korea. There are two main factors behind this movement. Firstly, the elasticity of population of Korea's local public services is low as the central government is responsible for "population-elastic" public services such as social services, health, police, education etc. Secondly, small-sized local governments in Korea-of mostly rural areas-have relatively weaker economic and fiscal resources than the city governments. Compared to similar-sized local governments in Europe and Japan, fiscal resources of local governments in Korea with population below 50,000 are almost one-fifth or one-tenth weaker than those in Europe and Japan. Ideally, the benefits of local autonomy may be greater with small-sized local governments. However, the economic reality in Korea indicates that local government amalgamation is indeed a necessary step not only for economic efficiency but also for the effectiveness of local autonomy.

Financing Structure and Pricing Mechanism of Public Enterprises: the Case of Korea Expressway Corporation

Jiyoung Kim · Jung S. You

This study provides the theoretical model for the optimal financing structure and pricing mechanism of a publicly-provided good. When a public enterprise produce a good, a government has to make two decisions. First, it determines the amount of a subsidy for the public enterprise. Then it designs the price system to cover the rest of the production cost. Under this setting, we suggest the optimal cost-sharing rule between the public enterprise and a government and the pricing mechanism which can achieve the budget balance of the public enterprise and the maximization of social welfare. Then we apply our model to the case of Korea Expressway Corporation. Korea Expressway Corporation is the public enterprise which constructs and operates the tollway in Korea. We show how our model can be used to derive the optimal price level by estimating the demand and cost function of the tollway.

The Managerial Autonomy and Performance of Public Enterprises

Jiyoung Kim · Kyoungsun Heo

Managerial autonomy and accountability are two important factors for operating public enterprises. As the performance of public enterprises are more emphasized, the role of managerial autonomy becomes more important. However, there are few research or government policy on managerial autonomy of public enterprises. This study analyzes how managerial autonomy of public enterprises affects their performance efficiency. First, we review the laws and the policies which affects managerial autonomy and regulates public enterprises. Korean government exercised powerful control over public enterprises in early period. But it changed to induce the efforts and accountability of public enterprises over time. From this institutional review, we chose the variable that can be used as an index for intensity of regulation since intense regulation prevents managerial autonomy of firms. Using this index for intensity of regulation, we made an empirical analysis for the relationship between regulation and firm performance. The results show that the performance level of public enterprises tend to decrease as the intensity of regulation is stronger. Especially, managerial autonomy has negative relationship with the firm profitability and growth. We conclude that managerial autonomy should increase to improve the performance efficiency of public enterprises, and derive policy implications for expanding managerial autonomy of public enterprises.

Corporate Governance and Performance of SOEs in Korea

Kyoungh Sun Heo · Ra Young-Jae Ra

Corporate governance of deals with conflicts of interests between the owners and the managers, the shareholders and the stakeholders, and customers and investors. To mitigate or prevent these conflicts of interests, various kinds of processes, customs, policies, laws, and institutions have been developed. Well-defined and enforced corporate governance provides a structure that, at least in theory, works for the benefits of both the State and the public interests by improving the strategic decision making and the accountability of the management. In recent years, corporate governance has received increased attention as it is considered as one of the critical policy intervention to increase transparency and performance of SOEs (State-owned enterprises).

This study assessed the current status of corporate governance of SOEs in Korea and suggested recommendations for improving corporate governance. As a result, this study confirms that the nomination and resignation process of board members, and the autonomy of the board practice are the most concerned issues regarding corporate governance of SOEs in Korea. Particularly, the functioning of non-executive board members is quite problematic even though it was allowed quite enough trial-and-error periods. This study also compared the current status of corporate governance of SOEs in Korea with OECD Guidelines on Corporate Governance of State-Owned Enterprises, which is being used worldwide as the global standard of corporate governance of SOEs. The result showed that SOEs in Korea have accepted most of the OECD guidelines. This is because the corporate governance reform in 2007 introduced many of OECD guidelines into corporate governance of SOEs in Korea. Centralizing ownership function into Ministry of Strategy and Finance and empowering board of directors are good examples of corporate governance reform in 2007. However, issues are still remained. Clarifying ownership function, separation between ownership function and other regulation function, and the autonomy of board of directors are found still problematic. Another significant issue in corporate governance of SOEs in Korea is that the gap between

the legal and regulatory frameworks for corporate governance of SOEs and the way how they are working are quite large. The practices of corporate governance in the real world is not able to catch up the advancement of legal and regulatory frameworks for corporate governance reform of SOEs.

This study suggests three recommendation bases on the analysis of corporate governance of SOEs in Korea. First, encouraging the function and the accountability of the board of directors is needed. Second, an action plan should be prepared in order to face the international pressure on competitive neutrality. Third, regular assessment and feedback on the practices of corporate governance should help improving the corporate governance of SOEs.

Quasi-fiscal Activities of SOEs in Korea

Joonok Choi

SOE(State Owned Enterprise)s sometimes carry out some activities that should originally be a part of government's role. Even though they have the characteristics of public finance, those activities, especially activities by SOEs with commercial nature, are often not shown in public finance data. In that sense, they are often called quasi-fiscal activities. They often incur significant impacts on the financial situation of SOEs, and may cause economy-wide influence. Nevertheless, few studies have dealt with those issues in Korea.

This study analyzes the quasi-fiscal activities by state owned enterprises. Discussion on basic concepts are followed by more detailed analysis of the financial situation of major SOEs. Because the scope of the quasi-fiscal activities by SOEs can be wide, this study focuses on one those of SOEs in the energy sector. Since the hike of oil price in 2008, government involvement in energy sector have increased in Korea, and SOEs often have become tools to achieve government policy. Even though the scope depends on how we define "quasi-fiscal activities by SOEs", this study deals with the tariff of electricity and natural gas. This study deals with the various impacts of curbing the rise in the price in spite of the rise in the input costs, and discuss alternative policy tools.



The List of Publications(2009~2011)

Issue Papers



The Estimation of User Costs by Industries in Korea(1970~2006)

Hak K. Pyo · Kim, Woocheol · Eunkyung Jeon

This paper suggests an alternative method for computation of user costs based on the rate of returns derived under the assumption that the total value of capital services is equal to capital income. Applying the data from KIP(2008), we calculated the user costs for 11 different assets along with 72 industries. Our results show a downward trend of the average user costs over the whole period which is attributable to the decreasing rate of returns and corporate income tax rate. User costs of service industry are found to be higher than those of manufacturing industry that have been favored by some tax system including the investment tax credit or accelerated depreciation. Their differences, however, is decreasing gradually, as government does not rely on an aggressive industry policy any more.

Fiscal Policy Scheme for Small and Efficient Government

Seong-Suhn Kim

This report investigates theoretically and empirically the growth effects of fiscal policy which intend to find desirable tax and spending policy scheme for small and efficient government in Korea, which uses annual data for Korea 1970-2007 and OECD panel data 1990-2006. The OLS, GMM, and Vector autoregressive method are used to find out short run and long run dynamic effects as empirical analysis tools.

The results show that increases in both fiscal variables-total government spending and tax revenue- may be detrimental to the per capita economic growth rate. It means that fiscal adjustments implemented by cutting spendings and tax rates have an expansionary effect on the economic growth.

It also attempts to estimate the economic growth effects of sectoral government spending by function classification in order to find out the growth effects of the composition and efficiency/quality of public sector. So I break down into several sectors with various criteria; 2 sectors: Government consumption and Government investment; 2 sectors: Productive and Nonproductive public spending; 2 sectors: Economic spending and Social spending; 10 sectors: General public service, Defence, Public order and safety, Economic affairs, Environment protection, Housing and community amenities, Health, Recreation, Culture and religion, Education and Social protection. The results show that the composition and efficiency/quality of public sector are important to the economic growth. Government consumption has significant negative effect on growth while Government investment has positive or negative; Productive spending has weakly positive effect on growth while Nonproductive spending has significantly negative; Economic spending has insignificant effect but Social spending has significantly negative effect on growth; Among 10 sectors, Education, General public service, Public order and safety, Defence, Recreation, Environment protection and Economic affair sectors have positive productive effects on economic growth while Social protection sector has negative nonproductive effects on economic growth. But Health, Housing and

community amenities are inconclusive on growth effect. These overall results seem to be consistent with the theoretical prediction but not some.

The regression analysis implies that, although a smaller public sector can be good for growth, it is necessary to look beyond size; the composition and quality/efficiency of the public sector are equally important. The policy lesson is that a smaller government share in GDP, a reallocation of funds away from nonproductive public consumption to productive public investment, and an improvement in government quality/efficiency can become engines of economic growth over the long run.

Also they show that the vitalization of private investment and the cultivation of human capital are most important for long run economic growth in Korea since private investment and average schooling year have been relatively more efficient than fiscal policy factors such as public spending and tax cut policy have.

The Influence of Disparity between Control and Ownership Rights on Book-Tax Reporting Differences

Sang-Wook Lee · Bong-Geul Chun

In a Korean business group, there is a great deal of intra-group shareholdings among the affiliated firms, and such shareholdings separate voting rights from cash flow rights. It is argued that the difference between voting rights and cash flow rights gives controlling power to seek private benefits at the cost of outside shareholders.

The owners of large business conglomerates should conform their book-tax income to minimize tax-related costs. However, book-tax reporting conformity may impose non-tax costs. Using a unique dataset from the Korea Fair Trade Commission, we examine the effects of disparity between control and ownership rights on book-tax reporting differences. This study finds that, on the whole, the difference between control and ownership rights does not have an effect on book-tax reporting differences. On the contrary, the difference affects the firm's performance. That is, higher difference between control and ownership rights has a negative effect on the firm's performance. From a tax policy perspective, our results suggest that the government may not need to consider directly the disparity between control and ownership rights when it formulate or revise a tax policy.

Fiscal Indicators, Fiscal Coverage and Central Bank

Dong-Suk Oak

The fiscal targets and indicators used most commonly in maintaining aggregate fiscal discipline are the fiscal deficit and fiscal debt, which many countries have laws and rules to restrict fiscal policy. The establishment of explicit fiscal targets allows the government to state clearly its fiscal policy and enable the legislature and the public to monitor the implementation of government policy, and ultimately, making the government politically as well as financially accountable.

In order to measure the fiscal deficit, the government needs, among other things, to determine the coverage of public finance in a sufficient and appropriate manner. Determining the coverage of public finance implies that the government should decide which public institutions, funds and accounts are to be included in measuring the fiscal deficit and the fiscal debt. Which public institutions, funds and accounts are to be included in measuring the fiscal targets?

It is desirable for the fiscal statistics to follow the conventions and classifications in constructing the national accounts for the entire economy, as laid out in the United Nations' A System of National Accounts 1993(SNA). The IMF's Manual on Government Finance Statistics(GFSM) harmonized with sectorization of the SNA, defines the coverage of the statistics to be a country's general government sector, which is defined on the basis of institutional units. The coverage can also be extended to the public sector by including the quasi-fiscal activities of public corporations.

The coverage of the consolidated government finance in Korea is traditionally recognized according to the criteria of accounting and fund units such as General Account, Special Accounts and Funds. The coverage of the government accounting and fund units, however, do not correspond with that of the general government sector in the SNA, being defined on the basis of institutional units not of the administrative, legal or accounting types. This study aims to raise some issues, especially on the dividing line between general government institutions and public corporations, in determining the coverage of public finance in Korea.

Basic Study for Simplifying the Tax Law

Wan-Souk Kim · Jin-Soo Kim

Although a tax law is the most frequently and closely related to the everyday life among any other fields of law, it is said to be too difficult for the taxpayers to construe and understand.

Therefore, it is necessary that the tax law should be rewritten to be systematical and simple so that taxpayers may easily construe and understand it. The easily understandable tax law could not only guarantee legal stability and predictability in taxpayers' economic activities, but also increase the level of voluntary compliance of taxpayers whereas decrease the compliance cost of the taxpayers and the administration cost of the Internal Revenue Service. An effort to make the tax law easily comprehensible is deemed to be a significant task in the field of a tax law in the foreign countries as well as in Korea.

However, that work is a long-term task which needs highly trained specialists and a lot of budget so that systematic and elaborate rewriting plan of the tax law should be prepared in advance. This study suggests specific schemes to make the tax law easily understandable as the followings.

First, that work should be processed in the method which keeps the substantial contents of the tax law present, but changes the existing legal system and legal sentences to be easily understandable. It is ideal that the substantial contents of the tax law should be amended together, not only form, system, or expressions of the tax law in order to be easily understandable. However, since it is difficult to promote it in two directions, the latter method should be processed in advance.

Second, a package solution, which approaches all the amending processes of the tax law and comes to an end at the same time, is practically hard to take. Therefore, that work should be accomplished in step method, which means the tax law should be amended in part and at intervals in the yearly amending process.

At first, it is recommended that after accomplishing rewriting work concerning an income tax for two years in 2010 through 2011, the other tax statutes relating process should be followed in 2012 through 2016 for five years on the basis of

an experience and the former work.

Third, that work should be focused on making a meaning of the law clear in that the substance of the statute is concrete and detailed, for too much compressed and simple law makes it hard to understand and causes legal vacuum to hamper taxpayers' legal stability and predictability.

Fourth, a project team to execute the basic study of the revision of the tax law should be established in Korea Institute of Public Finance. This team should include not only a consulting committee and the working level team, but also professionals such as policy makers, tax officials, professors in tax law, public finance and accounting specialists, lawyers and certified public accountants, certified tax accountants and other relevant experts.

Fifth, a detailed guide of the revision of the tax law system and the process of rewriting the tax law should be established, which could be the basis of that task. Concerning this, this paper suggests a detailed guideline of tax law establishment, an introduction of a general provision, a reform of index of provisions, connection of the enforcement ordinances and the statutes, definition provisions, and limitation of delegated legislation. And it also suggests the detailed guideline of accuracy and definiteness of expression, translating into easy expression, avoidance of repeated exception clauses, maintenance of appliance clause, legal devices helping the understanding of the statute and simplification and maintenance of writing forms of the tax law.

Income Reconstruction System and Tax Administration

Yu-Chan Kim

Income reconstruction system in Korea induces some troubles for tax administration and raises its costs, because of unclarity of provisions. In case calculated income of income reconstruction system is lower or not so higher than that of ordinary booking tax payers usually prefer the former. Therefore we need new structure for income reconstruction system in the future. The methods of income reconstruction would be divided in two cases, in the process of tax return and of tax investigation. In the process of tax investigation as a methods of income reconstruction the proportional method must be applied and additionally the cash-flow method and the bank account method.

A Study on Reform of Corporate Income Tax Law for the Adoption of International Financial Reporting Standards

Tae-Sup Shim et al.

The purpose of this report is to make suggestions on reforming Korean corporate income tax law for the adoption of International Financial Reporting Standards(IFRS). After reviewing the differences among the K-IFRS(IFRS adopted into Korean corporates in 2011), the current Generally Accepted Accounting Principles(K-GAAP), and the current Korean corporate tax law, this study analyzes several tax issues and then suggests amendments for those issues.

Some reforms needed after adopting the K-IFRS are as follows;

First, K-IFRS apply the fair value evaluation method when they measure the values of the tangible and intangible assets, etc. However, the tax law needs not adopt the fair value evaluation, because the profits and losses from changes in fair value are yet not realized and therefore not taxable.

Second, there are several expense items that firms should reflect on their financial statements in order to make them tax-deductible. There are differences in recognition criteria of these expense items between the corporate tax law and K-IFRS. After the adoption of K-IFRS, firms face tradeoffs between tax savings and potential benefits from not violating K-IFRS. To resolve these such problems, some tax codes are needed to be revised so that the recognition differences can be adjusted through tax reconciliation.

Third, it is reconsidered that the Korean tax law continues to apply the accounting standards after the adoption of K-IFRS. Because IFRS are basically principle-based standards, so the same transactions are not usually recorded in the same way, and this impairs the fairness of tax laws. Therefore, there should be some revisions on the current tax codes that uses the accounting standards.

Fourth, the Korean tax law needs to adopt the functional currencies, since the current K-GAAP and K-IFRS has already done so. Specific provisions need to be enacted as to decide the range of application and methods in computing taxable income associated with the functional currencies.

Finally, the format of financial statements should be more clarified in the

tax laws, because there are no officialized formats under the K-IFRS. Therefore, the Korean tax law should make standard financial statements for tax reporting purpose. Also, separate financial statement, not consolidate financial statement, should be used as primary statements for calculating taxable income, and the tax law should clearly specify this point.

There are also many tax codes different from K-IFRS that should be reconsidered. If necessary, these items need to be amended soon.

International Comparative Approach to the Effective Corporate Tax Rate

Young Lee · Myeonghwan Cho

The purpose of this report is to estimate the effective rates of corporate tax and compare them by countries, industries, and periods. In addition, this report aims to analyze the determinant factors of the effective rates of corporate tax.

To this end, we used OSIRIS data provided by Bureau van Dijk Electronic Publishing. OSIRIS data contains financial data and other information for the companies from over 130 countries. Using OSIRIS data, we estimated the effective rate of corporate tax and measured the effect of depreciation allowance on corporate tax burden for each country. We found that, compared with other countries, the effective rate of corporate tax in Korea is moderate but the depreciation allowance is less favorable to the companies. Considering that the depreciation allowance system in Korea has not been changed since 1995, the less favorable depreciation allowance implies that Korea may need to modify its depreciation allowance system to be more favorable to the companies.

We also estimated the factors that determine the elasticities of capital stock. Other than the previous studies, we considered the openness multiplied by corporate tax rate as an explanatory variable. From the estimation, we found a tendency that the elasticity of capital increases as the openness of economy increases. This yields a policy implication that it is reasonable for more open country to have a low corporate tax rate.

A Study on Income Contingent Loan Repayment and Related Issues

Young Lee · Byung-hill Jun

This study investigates issues on newly introduced income-contingent loan(ICL) system. From other countries' experiences, elements essential to the successful introduction of ICL system are sought. Some controversial issues in managing ICL system are discussed and practical suggestions for these issues are provided based on lessons from other countries and previous researches. Numerical simulation is also conducted to evaluate the current repayment schedule and an alternative repayment scheme. Simulation results show that improving repayment rate is most important in sustaining ICL system successfully. In this regard, a decision on treatment of full time housewives' loan is very significant. In conclusion, this study suggests that at the early stage the eligibility for ICL should be limited and a further expansion should be suspended until answers to the above-mentioned issues are prepared at a satisfactory level.

Accounting and Tax Issues on the Carbon Cap and Trade Program

June-Gyu · Moonchyl Kim · Sang-Won Park

If a cap and trade emissions program is introduced, accounting guidance for emission rights should be provided by accounting standards setters such as IASB and FASB. However, no accounting standards for emission rights have been provided so far.

This study examines accounting issues for emission rights under EU-ETS and suggests accounting methods on emission rights. Specifically, we review several alternative accounting methods which have been suggested for emission rights and evaluate the respective accounting consequences. Especially, we focus on two main accounting issues about emission rights. First, we evaluate the nature of emission rights allocated by government, that is, whether they satisfy the definition of an asset and if so, what kind of asset they are. Second, we discuss accounting treatments for the credit if issued emission rights are accounted as an asset.

We conclude that emission rights satisfy the definition of an asset and suggest that they can be classified as an financial instruments and their fair value changes are recognized through profit and loss. Alternatively, emission rights could be classified as an intangible asset on the condition that all changes in the asset's fair value are recognized directly in profit and loss. In regard to accounting for the credit if emissions rights are initially recognized, we suggest that the credit account should be treated as a conditional liability. The accounting methods we suggest can make some contributions for resolving accounting mismatch problems which have been pointed out in the accounting for emission rights so far.

Also this article reviews the tax issues arising with relation to the introduction of the carbon cap-and-trade program and the carbon tax as means of regulating carbon emissions under United Nations Convention on Climate Change(UNCCC) and suggests ways to improve the taxation as follows;

First, value added taxes(VAT) on emission allowances under the cap-and-trade program should not be taxed since tax consequences are temporary rather than permanent by allowing a deduction of input tax to a purchasing company, and

non-tax treatment can be justified for the purpose of supporting efforts of reducing carbon emissions.

Second, in case that the allowance is allocated free, the value of the allowance is included in income for the purpose of corporate tax. However the allowance should not be included in income since the allowance does not render a benefit, but a burden, and penalizes a company which reduces carbon emissions.

Third, in case that allowance is acquired by participating or investing in Clean Development Mechanism(CDM), it is recommended that the acquisition cost of the allowance be the fair market value of the allowance and the remainder of the total investment be treated as the acquisition cost of the CDM investment for the purpose of corporate tax.

Fourth, in case that more than two allowances are acquired in an identical tax year, average method should apply for the corporate purpose. However free allowances allocated originally and other types of allowances such as purchased allowances and CDM allowances should be separately treated each other where the free allowances are stated as zero.

Fifth, carbon taxes should not be included in income or deduction for the corporate tax purpose. However, the payment of carbon taxes where the taxes are not received at sales should be deducted.

A Policy Recommendation for Proliferation of Charitable Contribution

Won-ik Son · Soon-tae Lee · Sae-kyung Park

This research adopts diverse approaches seeking political improvement for proliferation of charitable contribution. After-effects of global financial crisis damaged fiscal soundness of various nations. The paper focuses on new political legislations and discusses ways to vitalize culture of charity.

Growing economy and constant changes in society lead to a phenomenon that public activities which the society requires cannot fulfill different demands of people. As a result, Non-Governmental Organization (NGO) begins to substitute partial functions of government and NGO's role becomes significant. In consideration of current small-government favored attitude, a bigger role of NGO is anticipated.

This paper, first of all, ensures current status of South Korea's charitable contribution based on analysis of diverse resources and comparison with other countries. In addition, the research organizes different legal institutions related to charitable contribution by areas. To promote this sharing atmosphere, authors examine legal issues concerned with procedures of collecting donations and usages and suggest improvements.

For proliferation of sharing culture through a donation or charity, the government can take two different directions in improvement of legislative system. First, legislation could lower regulation on contribution's "give and take activity." Another idea is legislative reformation in establishment of Non-profit foundation that receives financial supports and human resources from community members.

The study also analyzes South Korea's volunteer activity and its setbacks from a perspective of supporting policy. Based on the analysis, new political issues and setting up a role model of the government driven organization are addressed and proposed. Strategies for enlargement of invigorating voluntary works can be classified into two parts: A) spread of social and cultural supports on volunteer services and B) specialization and enhancement of management system in voluntary activities. To find effective manage methods and to promote volunteer services,

a plan for case study of AmeriCorps, a U.S. federal government program which organizes and manages volunteer activities, and its applicability in Korean society is conducted.

Performance Management and Intergovernmental Fiscal Relation: Focusing on Social Services

Jonghak Won · Youngjin Yoon · Young B. Lee · Jaewon Lee

This study is composed of three parts, such as approaches for performance management of social services, cases of the advanced countries, and intergovernmental relationship for social service performance management.

This study explores issues on performance management model for social services. The issues provided are as follows. First, what should be chosen as the unit of performance evaluation and analysis? Among organization, individual, policy, and program, program is considered to be appropriate as the unit of performance evaluation. Second, how should the indicators for performance evaluation be designed when considering the categories of social services? Third, which indicators should be chosen for input, activity, output, and outcome? And what indicators should be emphasized?

This study suggests four principles to design the performance management model for social services. Those are principles of differentiation, flexibility, discretion, and simplicity. These principles reflect the characteristics of social services such as non-rivalry and divisibility of personal services.

The performance management model for social services is based on that of Service Efforts and Accomplishments proposed by GASB in U.S.A. The model is consisted of three parts, which are service efforts, service performance, and the relationship between service efforts and its performance.

Recently, Korea has experienced a dramatic increase in demand for social services due to the demographic and social changes such as aging, increased work participation rate of women, and the changes in family structure. However, the Korea government has not paid its attention to performance management of social service provision while focusing only on the increasement of social service supply. Thus, to provide insights into performance management system of social services, this chapter investigates the performance management system of social service provision in major OECD countries: U.S., Australia, and U.K..

These countries have a long tradition of social service provision and show a systematic performance management. They are all liberal welfare states, which focus low-middle income as target group and limit their roles on subsidizing not-for-profit or profit providers in service provision. These characteristics are corresponding to those of Korea making the benchmarking more suitable.

First, in case of U.S., the most distinguished characteristic of performance management system of social service provision lies in strategic planning stage. In the U.S., strategic planning stage is much emphasized than other phases of performance management process. In planning stage, the government urges every implementers and providers to align their activities onto the long- and short-term program goals. Also, in implementation stage, the U.S. system requires minimum legal regulation, while providing as large discretion as possible in designing and implementing social service programs. Through this discretion, they want to ensure enough flexibility of program implementation into the changing implementing environment. In terms of performance evaluation, the U.S. system is based on the two pillars: Government Performance Results Act (GPRA) in 1993 and Program Assessment Rating Tools (PART). The federal government evaluates state social service programs and, sequentially, state government has its own evaluation system corresponding to that of the federal government. One characteristic of program evaluation is a weak linkage between performance evaluation and budgeting process. We interpret this phenomenon for being based on the selectivism of social services of the U.S. system.

Second, in case of Australia, performance management of social services focuses on service quality provided by mainly profit service providers. Australia has a long tradition of providing social services with distinct responsibilities among the federal and local governments, and the market. The federal government takes charge of cash benefit and state and local governments provide social services for the general public. One characteristic of Australian social service provision is in the heavy reliance on the markets such as private or for-profit organizations or institutions as service providers. The service provision is already standardized and the content of standardization includes service procedures, service costs, and service quality. Thus, the service provision does not focus on the strategic planning but on fluent flow of subsidy and enhancement of service quality.

The management of service quality in Australia is conducted by accreditation system. Several quasi-governmental accreditation organizations are in charge of service quality evaluation and monitoring by service areas. For example, Aged

Care Standard and Accreditation Agency (ACSAA) manages the quality of the elderly services, while National Childcare Accreditation Council (NCAC) takes a responsibility in managing the quality of childcare services. In general, quality management consists of 3 different steps. First, each provider conducts self-evaluation and submit the report to the relevant accreditation organization. In the second step, the accreditation organization reviews the report and decides the implementation of spot review. Once the spot review is decided, one team with 3 members visits provider to conduct spot review.

Finally, the UK has a very similar system to that of Australia in that the UK emphasizes service quality management rather than performance management. The delivery system of social services in the UK is mainly led by the market, and the role of government is limited to the provision of subsidy to the market and the enhancement of service quality to the customers.

One characteristic of the UK social service provision lies in the rigorous quality management. To this goal, the UK adopted a detailed system of service quality management. In 2000, the UK enacted Care Standards Act, which clarifies obligatory registration of all social service providers, the application of national minimum standard, the installment of several service quality management institutions like Commission for Social Care Inspection (CSCI), General Social Care Commission (GSCC), and Social Care Institute for Excellence (SCIE). Currently all service providers in the UK should register in CSCI and have to take 2 obligatory quality review annually. CSCI conducts a detailed review of service quality over 40,000 providers annually.

In conclusion, performance management of social service provisions shows a wide deviation depending on the characteristic of social services in nation, and the delivery system and finance system. For example, social services are provided universally in a nation, there is a tendency that performance management is emphasized. On the other hand, if services are provided partially based on selectivism, then a country tends to emphasize quality management rather than performance management. Also, a country with private delivery system comparing to that with public system tends to have a weak notion of performance management.

In social welfare policy area, traditionally, centralized policy governance has been established. However, decentralization approach is important in social service policy, considering the diversities of everyday citizen's life. New framework is required in governmental fiscal relations for social service policy.

According to new classical economics, especially public choice theory,

decentralization policy was propelled to reduce federal welfare expenditures. But new public management has focused to result-oriented performance and responsibility with welfare contractualism in government fiscal relationship.

Recently, Korean government has enlarged social service expenditure with central governmental initiatives. In the 2009 general account budget of Minister of Health and Welfare (MHW), 61.9 percent of budget was implemented through central subsidy programs and two-third performance indexes were managed by categorical subsidy to local government. However, MHW has not alternative approaches of intergovernmental fiscal welfare relation.

For result-oriented social service policy, two policy tools are required; such as, social service block grant program managed by regional level government and new policy governance sharing the performance responsibility between central and local government.

Rewriting Korea's Income Tax Law

Wansouk Kim · June-Q Lee · Seong-sik Lee

Considering the Income Tax Law is the most frequently and closely related to the citizens' usual life among any other fields of law, an ordinary citizen should be able to easily understand and comply with the Income Tax Law in performing various economic activities, such as doing a business, being employed, lending and borrowing, disposing an asset.

However it is said to be too difficult and complicated even for the tax professionals to construe and understand. This difficulty and complexity hinder legal stability and foreseeability, lower the level of tax compliance, and incur higher administration costs.

A method of solving the difficulty and complexity of the income tax law could be a tax reform, such as a flat tax discussed in the United States of America. However this kind of tax reform is subject to the various criticism such as tax equity. Thus it is practical and effective to focus tax law rewrite with the substance of tax law untouched for the simplification of the income tax law, as in England and Australia.

This report suggests rewriting the income tax law as a method of solving the difficulty and complexity arising from a format, structures and expressions on the income tax law, which includes coordination with other tax laws, consistency in the legal format, reformation of structures, improvement of words and expressions on the income tax law and avoidance of abbreviation and abstraction. The study has been performed by the literature review on the results of prior research and the details suggested in this report are as follows;

First, the income tax law is to be divided into five parts; the outline of the law, general rules, tax liability for the resident, tax liability for the non-resident, supplementary rules.

Second, the article numbers are to be given by branch numbering system so that the history of changes in the provision could be maintained for the easement of applying, interpreting and revising the law.

Third, the article numbers of corresponding presidential decrees and ministerial decrees are to be identical to those of the income tax code. In case of the section of corresponding presidential decrees and ministerial decrees is not singular, branch numbers are to be given.

Fourth, overview provisions are to be included in the introduction of the law, each chapter of the law, each paragraph of the chapter for the enhancement of understandability and readability.

Fifth, definition provisions are to be included in the introduction of the law so that a reader can easily understand the terminology used in the law.

Sixth, all elements required to be assessed are to be prescribed in the income tax code so that legislations of comprehensive authorization by the National Assembly can be avoided.

Seventh, clear and definite concepts are to be used so that the law reflects the intention of legislators accurately and, thus, there is no room for different interpretations.

Eighth, the text of the law is to be written by use of words and terminology which are easy to understand and by use of short sentences. Duplicate exceptions are to be abolished, and references and citations are to be definitive and clear.

Ninth, formulae, flow charts, tables, references are to be included, if they are required to enhance readability of the law.

Also, this report presents the full text of the income tax code at the Chapter 4, Paragraph 3 of this report, which is rewritten in accordance with above mentioned guidance.

Tax-benefit Microsimulation Model: KIPFSIM10

Myung-Jae Sung · Byung-Mok Jeon · Heon-Jae Song

This paper aims to construct a government tax and fiscal expenditure related micro-simulation model by broadening the former primitive model once developed by Sung et al (2008). This model allows behavioral changes, broadens its scope of analysis from income and several excise taxes on some alcoholic beverages and tobacco products to in-kind benefits such as benefits from education, childcare, housing and national health insurance services in addition to the above mentioned range covered by the former model.

A policy simulation of income tax cut implies that its direct redistributive effect is negative by reducing the changes in Gini coefficients between before- and after-income-tax-incomes, and also that its indirect redistributive effect on the market income distribution is negative and exceeds the scale of the direct redistributive effect. Therefore, it is necessary to comprise both direct and indirect effects.

A Study on Changes in Tax Administrations and Tax Laws of Major Foreign Countries When They Adopted IFRS

Tae-Sup Shim et al.

The purpose of this report is to study the changes in tax administrations and tax laws of some foreign countries when they adopted International Financial Reporting Standards (IFRS). This study researched the processes of IFRS adoption and changes of tax laws in the United Kingdom, Australia and Italy, considering that those countries had some similarities with Korea in regard with the relations between tax accounting and accounting standards and the IFRS implementation scope.

This study makes suggestions for Korean tax administration after the IFRS adoption in two dimensions, the field of tax administration and tax law.

In tax administration, first of all, the Korea tax administration should announce the principles and the time schedule of tax law changes. Second, it should make the committees consisted of IFRS specialists, and reflect the suggestions of those committees. Third, in the long time perspective, the relationship between tax codes and accounting principles should be reconsidered. Fourth, the Korea tax administration should actively prepare some measures needed to adopt the IFRS, and provide some exceptions in the first year of IFRS adoption.

In tax code change, first, when the Korean tax administration changes tax codes, it should consider various factors which are affected by the changes of tax law, especially tax compliance cost and global competitiveness of Korean corporations. Many countries, which had adopted IFRS earlier than Korea, did not change some tax codes that may significantly affect their corporations' competitiveness. Second, the Korea tax administration should reflect the suggestions of the academic research or recommendations of Korean corporations.

We hope this study contribute the successful reform of tax law according to the adoption of IFRS in Korea.

Policy study for further improvement on designation and classification system of public entities

Jhungsoo Park · Taebeom Yun · Kyoungsun Heo

In general, public entities are defined as entities that are established, owned or sponsored by government for the purposes of providing public services or goods. The public policy on designation and classification of public entities has an actual effect on each public institution's governance and management system including evaluation method.

This study has been conducted under the following five topics - (i) Theoretical background discussions on classification system and management models; (ii) Analysis on management systems being operated by five developed countries; (iii) The status quo of Korean classification and management system; (iv) Legal and practical problems of Korean system; and (v) Suggestions for future development.

Under the first topic, the report addresses the importance of establishing designation and classification system, which determines the corporate governance model and evaluation method of public entities. Unlike private corporate, public entities can fall into pitfall of 'soft budget constraint' on account of being effectively protected from bankruptcy and ownership deprivation. Furthermore, transparency of the financial accounting reports and level of information disclosure do not reach the standard of private sector. For this reason, there have been much attention towards the development of management system and corporate governance models for public entities especially among international organizations such as OECD and IMF. Many theories demonstrates that the main factors to be considered are ownership structure, marketability, publicness and economic scale of entities.

Secondly, case studies on public entities have been conducted to analyse management systems of United Kingdom, France, Sweden, New Zealand and Singapore. The common features are - (i) These countries have developed centralized management structure in which a particular ministry is responsible for administrating core public entities; (ii) There are two separate underlying rationales for maintaining designation and classification systems of public entities. One is to record statistical report in accordance with international accounting standard, and the other is to

enhance administrative efficiency in determining the appropriate governance and accountability, including the degree of ministerial influence. The classification systems designed under these two rationales are often different to each other; (iii) Strategically and economically important public entities are owned, controlled and managed by special government unit; (iv) The classification of quasi-governmental public entities varies from country to country. They are often not defined as SOEs, but carrying out executive functions of government; (v) Ownership functions and managerial responsibilities of quasi-governmental public entities are fulfilled by various ministries depending on each entity's industrial specification.

In December 2006, South Korea enacted the Act on the Management of Public Institutions("the Act"), which became effective from April 2007. Under the Act, among the 598 entities, 298 were designated as public entities in 2007. These public entities were comprised of 24 SOEs, 77 quasi-governmental entities and 197 non-classified public entities. The classification is determined by number of employees and nature of revenue income. The entities with less than 50 employees are non-classified public entities whereas the entities with more than 50 employees are either SOEs of quasi-governmental entities. The entities with at least fifty percent of entire income being self-generated from their own business operations are classified as SOEs, whilst the entities with their income sourced from government assistance for the provisions of public goods or services are treated as quasi-governmental entities.

The Act categorizes public institutions into five smaller segments according to their main sources of funding - (i) entities with financial support from government as a main sponsor; (ii) entities with at least fifty percent of their income from government grants; (iii) entities fully financed by government as a major shareholder; (iv) entities in a form of joint venture; (v) entities re-sponsored or re-invested by government.

The analysis on the problems of our designation and classification system has been undertaken from legal and practical perspectives - (i) The Act does not stipulate the concept of public entities and the purpose of maintaining the designation and classification system; (ii) The Act only emphasizes the 'ownership' of public entities with lack of efforts to reflect the 'characteristics of goods and services' supplied by public entities; (iii) The current designation rule under the Act has critical defects as it often excludes several entities with strong nature of publicness and legal monopoly. Also the rules determining 'publicness' and 'marketability'

of each entities appear to be incomplete as they do not provide clear view of the symmetrical positions; (iv) The group of non-classified public entities needs further categorizations due to its large number and wide varieties; (v) The designation of public entities is updated every year, which results in frequent alterations of classification as well as changes of governance and evaluation methods; (vi) There is an absence of concrete guidelines suggesting appropriate corporate governance model for each group of public entities.

A survey has been conducted to identify more practical problems of current designation and classification system as of August 2010. The validity of theoretical classification model has also been assessed. The result has shown that the classification according to the main determinants (i.e. ownership structure, publicness, marketability and scale of each entity) does not reflect the unique nature of each entity in comprehensive manner.

Consequently, this study suggests the following amendments to the current system - (i) The Act should clearly outline the concept of public entities and the purpose of maintaining the designation and classification system; (ii) The classification rules needs further systemization and segmentation with a view to respect the wide ranges of public entities with various attributes; (iii) The assessment on publicness needs more specified and detailed criteria, which would enable more balanced and accurate discernment between publicness and marketability; (iv) The unstable structures detected in the course of frequent alterations and updates can be mitigated if the designation process is carried out in different timeframe with intervals between each group; (v) A specific guideline on suggestible corporate governance model for each group of public entities should be supplemented in the Act. This would maximize the effectiveness and efficiency of the classification system; (vi) The uniform rules applied to the non-classified public entities needs to be re-designed as they require more detailed segmentation respecting individual entity's specification. For examples, the subsidiaries of Korea Electric Power Corporation and university hospitals should not be hastily treated as non-classified public entities. In other words, more specific criteria for comprehensive examination on their unique functions and special structures should be made available in the Act.

A Study on the Tax System Related to Corporate Bankruptcy

Wan-Souk Kim · Ji-Sun Chung

Corporate bankruptcy includes both the rehabilitation procedure aiming to achieve rehabilitation of a corporation which is in financial ruin but can rehabilitate and the bankruptcy procedure in which properties of a corporation which is in financial ruin and can not rehabilitate are realized and disposed. Corporate bankruptcy is governed by the Debtor Rehabilitation and Bankruptcy Act.

The main part of a bankrupt corporation rehabilitation plan involves the debt restructuring in which a huge amount of debt is liquidated and the corporation continues under a new business structure and financial structure. But since the passive method in which existing shareholders and management are maintained and some debts are exempted while others are allowed an extended due date still has the risk that such corporation becomes bankrupt again, an active rehabilitation method using M&A, etc. are generally adopted. In such bankruptcy process, various tax issues such as taxation of debt-exempted earnings, taxation of asset capital gains in reorganization, succession of tax loss carryforwards and handling of tax claims in the bankruptcy procedure or rehabilitation procedure occur.

The problems of, and solutions for, debt exemption, capital gains, succession of tax loss carryforwards and handling of tax claims can be summarized as follows.

First, where it is desirable that debt-exempted earnings occurring in individual business operator's bankruptcy be expressly prescribed as non-taxable income in the Income Tax Act. Also, it is desirable that debt-exempted earnings not related to a business be expressly excluded from the object of gift tax or be expressly prescribed as non-taxable in the Inheritance Tax and Gift Tax Act.

Second, for debt-exempted earnings of a bankrupt corporation tax deferral is currently made by the method of earnings deferrable in three years with a three-year grace period, but it would be reasonable to change it to a method where reduction adjustment is made from the acquisition price of inventory assets or fixed assets of such corporation. And since equity-converted debt-exempted

earnings provides more advantages such as securing of equity capital to the corporation's rehabilitation, it may be necessary to allow a special tax treatment bolder than the general debt-exempted earnings.

Third, in order to achieve equality among creditors in the rehabilitation procedure and achieve rehabilitation of bankrupt corporations by expanding the scope of applicable debt-exempted earnings, where a juridical person having received approval of rehabilitation plan is exempted from part of the debt, a claim belonging to a non-financial-institution creditor also has to be granted special tax treatment.

Fourth, requirements for tax deferral of capital gains are separately prescribed for corporate merger, corporate division, etc. in Korea but since it is unreasonable to prescribe separate criteria of tax deferral for what is substantially the same, a unified provision is necessary. Also, for comprehensive stock exchange and transfer, it is better to enact permanent tax deferral provisions in the Corporate Tax Act than to enact temporary provisions in the Special Tax Treatment Restriction Act.

Fifth, for a bankrupt corporation, it is necessary to establish a separate criteria of tax deferral by importing into the tax statutes the distribution of payment received to creditors in the case of reorganization conducted under a rehabilitation plan and it is also necessary to allow succession of tax loss carryforward only when certain requirements are met.

Sixth, it is necessary to exclude tax claims from claims against bankruptcy estate in the bankruptcy procedure in principle but if such method is hard to implement, it is necessary to have a legislative improvement where, at least as regards priority of payment among claims against bankruptcy estate, claims for litigation expenses for common interest of the creditors of a bankrupt and the expenses for bankruptcy estate management, realization and distribution shall be paid in priority over other claims against bankruptcy estate including tax claims. Also, it is desirable to delete provisions which recognize, in bankruptcy procedure, claims that can be collected by the example of national tax collection as claims against bankruptcy estate and it is desirable to specifically list in the provision for claims against bankruptcy estate only those which need to be treated as such by individually reviewing the claims in the individual statutes.

Seventh, current statutes which basically treats tax claims as rehabilitation claims in the rehabilitation procedure and maintains balance between priority of tax claims and principle of equal treatment of creditors by considering priority of tax claims only in part is basically reasonable.

Lastly, since treating additional charges as claims against bankruptcy estate

or public interest claims materially infringes on other creditors' rights, it would be reasonable to exclude additional charges from claims against bankruptcy estate or public interest claims.

Performance Limit of Public Organization's Sustainability Management

Young-Jae Ra · Tae-Beom Yun

Sustainability management and Corporate social responsibility are accepted as appropriateness and inevitable issue, and not a problem of declaratory slogan any more in all organizational management and supervision including not only the private business sector but also public sectors. However, the approach to Korea's SM and CSR is mainly led by large enterprises, which vitally enter the international market, and public enterprises related to SOC and energy business. Especially, viewing the period of SM introduction of public institutes, except for partial leading public organizations, in case of late started public organizations, it can be interpreted that they performed moral management or CSR with the intention to correspond to government environment and ethical management policy.

SM began as social responsibility of business in the 1950s, and currently, it is not limited just to businesses, and it is used as a broader concept. SM does not consider only the performance of financial status or economic aspect, but considers various aspects such as environment, labor, human right, civil society, consumer, etc. SM is actively performed as international trend ranging from private business sectors to even the international organization UN and OECD, EU, World Bank, etc. And ISO announced ISO 26000 in Nov, 2010 to establish a new international standard regarding SM.

Public organizations in Korea are not having revitalized SM yet. The index which shows the degree of SM can be viewed in the publishing of SM report, and by the end of October of 2010; there were 42 public institutes which published SM report. There are 19 public corporations, 25 quasi-government organizations, and 13 miscellaneous public organizations which have joined the UN Global Compact which can be considered as at least SM performing organization, though in a lower degree than publishing SM report.

As a result of analyzing the relation of GRI G3 index and public institute management evaluation among SM indexes based on the public institute management evaluation standard in 2010, GRI G3 profile and management system, economic

performance showed relevance to management evaluation of public organizations, but GRI G3 environmental performance and social performance contain an aspect of not having been reflected to the management evaluation of public organization. As a result of empirical analysis, public institutes which published SM report obtained higher management evaluation scores. Viewing the result regarding the effect of SM, 90.2% positively responded in the survey asking whether SM or CSR of public organizations aiming to the second half government administration of Lee Myung-Bak's government, "fair society" correspond with the discussion about fair society. Regarding the greatest difficulty public institutes go through while performing SM, 43.3% answered insufficient professional manpower, 32.3% answered insufficient government interest and support, and 18.3% answered insufficient will and interest of the head of the organization, in order.

As a model for simultaneously pursuing publicity and business, the characteristics which public organizations should basically contain regarding SM or CSR in the sphere of policy of responsible ministries and offices related to public organizations or government authorities, and also in the practical sphere of each public organization, the following proposal in terms of policy is suggested.

First, for public organizations' SM, the government's role should be strengthened, and a SM model should be made.

Second, there is a need to review reflecting SM to management evaluation of public organizations.

Third, public organizations' CSR should be strengthened, and the head of each organization should judge the merits and deficiencies of each organization, which after SM examination and evaluation, the following; establishment of strategy, designing of organization, operation of manpower and business should be enabled.

Fourth, development of CSR model and application index for small sized quasi-government organizations and miscellaneous public organizations is required.

Fifth, there emerges integrated management of data and index regarding disclosure of management, SM report, annual report, and report of management evaluation result that are required.

A Study on Measures to Improve VAT Collection by Adopting Reverse Charge System

Jae-Jin Kim

Value-added tax(VAT) is an indirect tax collected by intermediary (such as merchant) from the person who bears the ultimate economic burden of the tax(such as the consumer). Therefore, convenience in tax payment for intermediary and their commitment to carry out the responsibility: transferring the collected tax to the taxation authority are most essential aspects in carrying out a successful VAT in the tax system.

South Korea's VAT was introduced in 1977. Since its introduction, economic environment affecting the VAT's effectiveness, such as the size of economy and the dynamic between intermediaries and tax-bearers, have changed significantly from that of the origin. However, so far, studies and tax policy regarding VAT in Korea has been heavily focused on such topics as the scope and standard of VAT and the tax rate than its effectiveness in operating cost and collection structure.

In theory, for VAT, personal end-consumer is the ultimate tax-bearer and merchants simply transfer the collected tax to the tax authority without taking further tax responsibility. However, in Korea, it maintains relatively high arrear payment rate as large number of merchants fail to remit the collected tax to the authority.

In order to have VAT as a sound periodic tax item for Korea, it is essential to reform VAT law to catch up with the changes in economic environments, such as merge of electronic finance. Furthermore, in order to improve the VAT collection structure, it is essential to understand changes in transaction settlement system as the system is closely related to implement a better measure to collect VAT.

The tax authority could introduce 「Reverse Charge System」 to address problems existing in the current VAT system. Whilst, in order to apply 「Reverse Charge」 effectively, it must consider the nature of transaction: 「B2C」 or 「B2B」.

It is merchant's responsibility to be acting as intermediary for VAT in a 「B2C」 transaction. However, in a 「B2B」 transaction, similar to the withholding

taxes, it is important to choose which party involved in transaction to carry out intermediary responsibility. The decision must be flexible considering likelihood of party's commitment to honor the responsibility and convenience available.

However, if 「Reverse Charge System」 is adopted for all types of transactions, it would cause confusions among tax payers who are accustomed to the existing system. Therefore, 「Reverse Charge System」 must not be used as an alternative to defy the existing “Tax Credit Method” but to be used for some specific industries that could carry out the taxation responsibility with confidence.

This study examines characteristics, overall system and problems in Korea's VAT. Based on that, it provides ways to overcome these impediments the existing tax system faces today, in Korea. Especially, it focuses on VAT's collection structure and its related issues.

If the tax authority successfully addresses such related issues by implementing proper measures like 「Reverse Charge System」, it is expected to raise tax revenue. Moreover, the tax authority would be able to predict VAT revenue more accurately, which helps preventing VAT revenue losses caused by omission and arrear payments. Also, it would reduce tax administration costs and enhance social welfare by promoting fair trading in Korea.

Privatization Index

Ki-baek Park · Sang-Won Park

This study aims to suggest which elements we should look at to determine privatization of a public enterprise. To do this work, we analyzed the actual experience in Korea. In 1993, Korea government announced the extensive privatization plan which mentioned 68 public enterprises. Some firms have been privatized ever since, but others have not. In addition, there are noticeable difference in terms of privatization period.

In a binary choice model on whether privatization of each firm has occurred or not, we showed that high rate of return and loss in profit have a positive effect, while industrial concentration has a negative one. An ordered dependent variable model where the order of privatization is the dependent variable also showed the similar results, that is, positive effect from high rate of return and loss in profit, and negative one from industrial concentration. In addition, low debt ratio and relevance to low income consumers also have a negative effect.

These results, specially coefficient values, can provide a good criterion of privatization decision in the future.

Corporation's Quasi Tax Burden and Policy

Wonik Son

This research aims for analyzing corporation's quasi-tax burden aside from regular taxation and for measuring its size. A scope of quasi tax is categorized in broad and narrow senses and development of quasi tax is examined. The paper scrutinizes importance of quasi-tax on GDP and tax revenues and how it changes over time. By examination of quasi-tax's percentage on corporate taxation and net profit during the term, the study discusses a scale of quasi-tax that corporation actually covers.

The paper conducts a survey with businesses to grasp a size of involuntary contributions. Based on the results, volume of quasi-tax subscriptions was calculated by each donation types. The estimated contributions were included in broad and narrow sense of quasi tax for measuring the size of total quasi tax. Discretionary donations are classified and reviewed by diverse categories: donations, sizes of corporation, listed or unlisted businesses, and industrial fields.

Various reports indicate that estimated corporation's quasi-tax reaches 94.3 million Korean won by using responses that donation is 'compulsory' or 'somewhat coercive.' Contributions in quasi-tax amount to 357.3 million Korean won when companies that involuntary donation is 'neutral' are included.

Scale of quasi-tax in broad sense reaches approximately 32.4 trillion won, equivalent to adding up social insurance costs borne by business owner's, 20.7 trillion won, Corporation's cost of burden, 11.5 trillion won, and involuntary contributions, 94.3 billion or 357.3 billion won. In narrow sense, overall quasi-tax amounts to about 23.1 trillion won. The total amounts are consisted of social insurance cost of company owners, 20.7 trillion won, corporation's cost of burden, 2.4 trillion won, and involuntary contributions, 94.3 billion or 357.3 billion won.

In a broad perspective, accurate analysis of quasi-tax and its volume could provide the government with significant implications related to management on policies that include future taxation and diverse costs of burden because the examination assures financial burdens other than taxation. In a microscopic

viewpoint, on the other hands, suggestion of alternative policy about cost of burden included in quasi-tax is needed. In a case that cost of corporation's financial burden works against its intention, new policy is also required.

The paper intends to address diverse social benefits followed by endeavors on quasi-tax reduction. The tax deduction will ease companies' burdens of taxation that establish better industry favored environment and strengthen the competitiveness. In addition, converting expenses discrepant from the traits of cost of burden into tax allows the government to impose tax based on 'no taxation without law' and to determine governmental expenses within allocated budget. As a result, the study anticipates precise causes of taxation and expenditure and improvement of financial transparency.

Essay on the Productivity of Public Enterprises

Jiyoung Kim

This paper examines the determinants of the productivity of public enterprises. Especially it focuses on the effect of public ownership on the total factor productivity and labor productivity. The empirical analysis utilizes the panel data which contains the individual firm data for both public and private enterprises.

The results show that the total factor productivity of public enterprises is not statistically different with that of private enterprises in most industries. Also I could find the same results on the labor productivities. In addition, I investigate the effect of performance evaluation system on the labor productivity of public enterprises. Performance evaluation system turns out to have significant effects on the labor productivity of public enterprises, but its effects vary across the size of public enterprises. It increases the labor productivity for the public enterprises with large size of capital and labor costs, while it has negative effect on the labor productivity for the public enterprises with small size of capital and labor costs. Besides the empirical analysis, this paper provides a brief exploration on the difference between the productivity index of performance evaluation system and the productivity measure.

Privatization of State Owned Enterprises in Korea: Performance Assessment and Policy Direction

Jhung-soo Park · Seok-hui Park

During last 30 years or so, privatization of SOEs has attracted so many countries' policy leaders, academia, and produced a lot of improvements in economic performance in many significant industries. However, there are some opinions that the utility of privatization policy is not any longer relevant, so privatization policy of SOEs does not make much sense in current developed countries. Even though, still, many countries including Korea, as a national agenda, privatization policy always has one of top priorities whenever government changes. Why this dual and contradictory characteristics of privatization policy has been sustained in Korea and many other countries is main research question and motive for this study.

Privatization has broad and flexible perspectives; traditionally it is defined as selling stocks to the private sector and change hands of its shares of ownership. However, in broader sense, it is possible to be considered as part of privatization, which is set up more competitive environment and allow more autonomous decision making power to SOEs' CEOs. Therefore, we can call it as a future policy agenda, not only past or present one.

This study critically reviewed literature and empirical studies done by western world and developing countries (such as China and India) as well which covers logic and limitation of the argument. There are some evidences which found negative and limitation of the privatization policy, however, in general, majority of the studies found that ownership transfer to the private sector enhances productivity and efficiency as a performance. Surely, there are differences on performance for industry by industry, for the level of development of the nation, and culture and history of the nation which they share. In addition to that, the quality of process management is very important determinant of the success of privatization policy.

The privatization policy, which influence diverse stakeholders' interest and is strongly influenced by political decision making rather than economic analysis,

is followed path dependent from the past. Therefore, we need to learn from our privatization history and their success and failure experiences and make them as a base for future development. These are major purpose of this report that reviews before Kim Dae-jung government, Roh Mu-hyun government and Lee Myung-bak government's privatization policy performances. We reviewed in-depth industry-wise case study as well as time series analysis. Generally, past privatized enterprises are mainly distributed through mining, manufacturing, construction/transport and finance/insurance industry and are heavily focused on the manufacturing industry in particular. Past privatization policy of Korea is evaluated as successful in general and we could drive policy suggestions that recommend as market structure and characteristics of the industry should be fully considered for increase of the possibility of success to future privatization potential enterprises selection, scope, range, method, and priority.

We have learned that the privatization policy is not panacea at all through the review of international case studies. Some cases are successful and the others are not. It depends upon the industry and market structure. Even though, we could drive policy implication that we have to consider the development level of the nation and cultural characteristics of the society influence the privatization policy's impact and technical development could lead overcome the limitation of the industry's scale of the economy, so currently the privatization policy includes energy industry and network industry as well.

Before and after empirical analysis of the privatization shows that Posco, Daehan oil pipeline corporation, Samsung general chemicals Co. Ltd. cases are quite successful. Mainly, they are manufacturing companies which were high market concentration and high supplier market share induce improvement of productivity and efficiency. Therefore, industry based approach is much more important than the classification of the firm or ownership type approach. Indicator based analyses found that mainly behavioral change of efficiency-wise is much more significant than that of growth-wise approach. This implies that SOEs were focused on the sales maximization strategy rather than profitability or productivity. The impact analysis of the privatization policy found that productivity and efficiency are all proved much better performance in privatized firms. Therefore we could conclude that still, we can expect national economic benefit from further privatization policy if we can.

We suggest following policy alternatives. First, enlarge the management autonomy in SOEs as far as we can. We already have started this pilot project

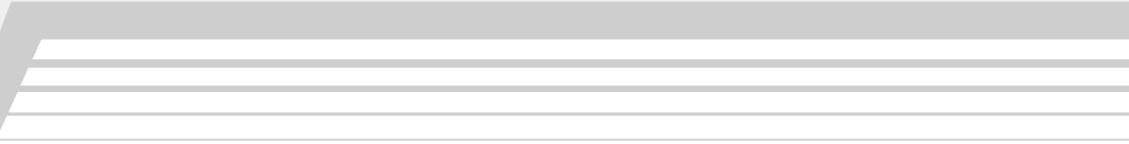
from 2010 and the performance evaluation of this project has been reported as quite good. So we need full scale project of governance reform for market based SOEs for further autonomous management. Second, for the selection of the potential privatization firms should not be limited to small scale as Lee Myung-bak government tried. We could consider favorably for privatization to electricity industry, railroad industry, energy industry including gas supply, SOC industry and finance industry as well. It is based upon the industry based case analysis and past performance review, empirical analysis, and international comparative analysis as a whole. Privatization policy still is quite attractive alternative to improve competition enhancement and overcome the difficulties of SOEs management which we are experiencing.

A Study on the Estimation of Corporate Tax Burden and Tax Base using Firm Level Data, and the Effect of Corporate Tax Burden on Firm's Investment Behavior

Hosin Song · Bong-Geul Chun

In this paper we proposed to estimate the corporate tax burden and tax base using the information in financial reports at firm level. Furthermore, we confirm how well the proposed method works since the firm-level data of the actual corporate tax burden and the corresponding tax base during 1998~2002 are available. The results show that the estimates of tax base have little deviation from the actual tax base, while the estimates of tax burden have very large deviation. In addition to the estimation of corporate tax burden and tax base, we empirically investigate how corporate tax burden is determined and how corporate tax burden affects firms' investment such as net investment and R&D investment.

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