

# **FISCAL DECENTRALISATION IN VIETNAM: A PRELIMINARY INVESTIGATION**

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## **Abstract**

Fiscal decentralisation is a complex theoretical and practical issue. The literature is currently divided on whether there is a positive or negative relationship between fiscal decentralisation and economic growth, and it appears that this is in large part due to inconsistent measures of fiscal decentralisation. In this paper, fiscal decentralisation in Vietnam will be examined, with a view to developing a fiscal decentralisation index that accounts for both the fiscal autonomy and fiscal importance of subnational governments to compare the degree of fiscal decentralisation in Vietnam with that of a range of other countries. This will facilitate subsequent (and hopefully definitive) investigations of the relationship between fiscal decentralisation and economic growth.

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## **I. Introduction**

Vietnam is a developing country in the South East Asia region with per capita income of US\$ 542 in 2004 and a public sector that accounts for about one quarter of the national economy. The country has faced many challenges in relation to the process of economic growth as a fully independent nation since liberation on 30 April 1975 and the proclamation of the Socialist Republic of Vietnam on 25 April 1976. The economy had been thoroughly run down after 30 years of war with two completely different economic systems: the North with the highly centralised and planned regime and the South with the market regime. Since reunification, Vietnam has attempted to integrate itself further with the world economy.

The objective of this paper is to examine fiscal decentralisation in Vietnam, with a view to developing a fiscal decentralisation index (FDI) to compare Vietnam with a range of other countries. The paper is organised into seven sections. Following this Introduction, Section II briefly discusses the history of Vietnam and the current structure of the Vietnam State. Also, economic growth and fiscal changes in Vietnam are briefly discussed. The distinct notions of fiscal autonomy and fiscal importance of subnational governments (SNGs) – two cornerstones of fiscal federalism literature - are discussed in section III. Section IV examines the current arrangement of fiscal decentralisation in Vietnam and provides preliminary comments on its current situation. Development of the FDI is outlined in section V. Then, the FDIs for Vietnam and selected ASEAN and OECD countries are calculated in section VI. Main conclusions are included in section VII.

## **II. Fiscal changes and economic growth in Vietnam from 1975 to 2004**

### **1. Vietnam's history and the current structure of the government**

Vietnam's history has reflected many political, social and economic transformations. However, until the mid nineteenth century, the single defining historical feature was the successive sequence of feudal dynasties. In all these feudal dynasties, highly centralised administrative structures were prominent. However, this long historical tradition was fundamentally changed in 1858 when France colonised Vietnam. On the 2 September 1945, Democratic Republic of Vietnam was established and the French colonialists invaded the country again. The war of resistance between 1945 - 1954 was ended by the defeat of the French in the famous battle of Dien Bien Phu. As a result, the Geneva Agreement on Vietnam was signed in 1954. According to this Agreement, the country was temporarily partitioned into two parts (North Vietnam and South Vietnam) by the seventeenth parallel and should be reunified within two years through a general election held all over Vietnam. However, this did not eventuate and the country was remained divided. National reunification and independence were realised on 30 April 1975. Socialist Republic of Vietnam was subsequently formed on 25 April 1976. The history of the nation has turned into the new page, with the last 30 years of the century of peace time largely devoted to developing the economy.

Vietnam is a socialist country with the leadership of the Vietnamese Communist Party. The present structure of the State system in Vietnam is defined by the Vietnamese Constitution (1992) and a range of non-constitutional statutes. The National Assembly is the highest representative office of the people, the highest institution of state power of the Socialist Republic of Vietnam. The National Assembly has 450 members who are popularly

elected for the five-year term. Among these members, the National Assembly appoints the President. The President is the Head of the State who represents the Nation in internal and foreign affairs and is elected among members of the National Assembly. The President acts as the head of the State. The head of the government is the Prime Minister who is proposed by the President and elected by the National Assembly.

The administrative structure of the country at local authority level is organised into three different sub-levels: province, district and commune. There are currently 64 provinces, in which five large cities are granted a provincial status. They are Hanoi, Ho Chi Minh City, Haiphong, Danang and Cantho. These provinces are divided into 611 districts which are, in turn, subdivided into 10,602 communes (Martinez-Vazquez, 2004). At every level of subnational governments, there is legislative authority - People's Council, and executive authority - People's Committee, who is appointed by the People's Council at the same level of governments. Although the People's Council and the People's Committee are set up as two different bodies, they usually have the overlapping members (i.e. some members at People's Council are also members at People's Committee, except for some positions).

## 2. Summary of economic growth and fiscal changes from 1975 to 2004

Changes in fiscal environment embodied in the history of economic growth in Vietnam can be reviewed for specific segmented periods. The following periods are considered because there have been significant changes in economic and fiscal policies. Also, after reunification, the government prepared and implemented "Five-Year Socio-economic Development Plan" (FYP) for every five years, starting from 1976.

### 2.1 Economic growth for the period from 1976 to 2004

For the period from 1976 to 1985, Vietnam was a centrally planned economy. This period was represented by the FYPs from 1976 to 1980 and from 1981 to 1985. The broad objectives of these plans were to create the transformation of the economy from small-scale to large-scale production with the emphasis on heavy industry and agriculture. In addition, these plans were also intended to stabilise and improve living standard, reorganize and develop production (Vo, 1990). These goals were seen as over ambitious and infeasible. The results for economic growth for these FYPs can be found as follows.

TABLE 1  
ECONOMIC GROWTH RATES

	Percentage rates of growth		
	GDP	Agriculture	Industry
FYP 1976 - 1980			
Plan	13 - 14	8 - 10	16 - 18
Actual	0.4	1.9	3.3
FYP 1980 - 1985			
Plan	4.5 - 5.0	6 - 7	4 - 5
Actual	6.4	5.3	9.3

Source: Fforde and De Vylder (1996, p. 167) and Arkadie and Mallon (2003, p. 28).

In December 1986, intensively comprehensive programs of economic reform were initiated as represented by the FYP for the period from 1986 to 1990. This reform explicitly recognised the irrelevance of the centrally planned economy in Vietnam. Since then,

Vietnam has been characterised as a multi-sector economy which follows market-based operations. Between 1991 and 2000, there was a period of extended and comprehensive economic reform. This period was represented by two FYPs from 1991 to 1995 and from 1996 to 2000. The goals were to increase the annual growth rate to around 7.5% and double capita income by 2000 from the 1990's level (MOFA, 2003).

Economic growth and inflation over the period of the FYPs in Vietnam (1976 – 2000) can be seen in Table 2:

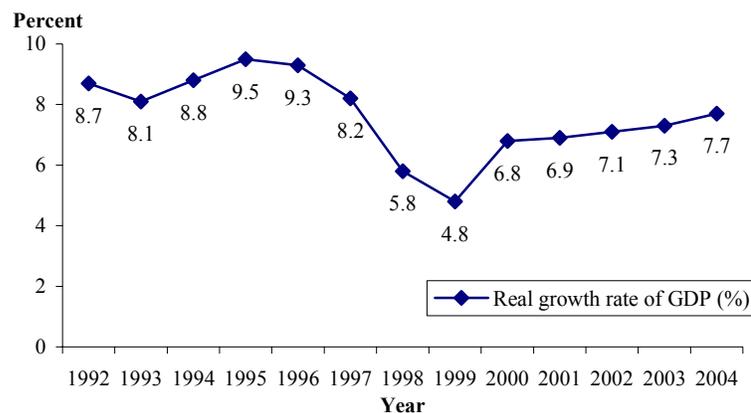
TABLE 2  
GROWTH & INFLATION OF THE FIVE YEAR PLANS

Period	Inflation (CPI)	GDP	Agriculture	Services	Industry
1976-1980	21.2	0.4	1.9	-0.1	3.3
1981-1985	74.2	6.4	5.3	4.7	9.3
1986-1990	298.7	3.9	3.7	8.7	4.7
1991-1995	23.5	8.2	4.3	9.5	12.6
1996-2000	3.4	7.0	3.9	7.3	12.2

Source: Arkadie and Mallon, (2003, p. 28).

Since 2001, the economy was marked as the period of industrialisation and modernisation with the goal to become an industrialised country by 2020. It is expected that GDP in 2010 will be doubled that of 2000, with a strong transformation of the structure of the economy, particularly focusing on industry, construction and services. For the transformation of the structure, by the year 2020, agriculture accounts for 16-17% GDP, industry from 40-41% GDP and approximately 42-43% GDP for services. In addition, it is expected that the ratio of domestic saving rises over 30% of GDP (IMF, 2004).

FIGURE 1  
ECONOMIC GROWTH IN VIETNAM



## 2.2 Significant fiscal changes in Vietnam for the period from 1976 to 2004

The degree of fiscal decentralisation in Vietnam has changed over the last 30 years as laws and regulations have been altered. The most fundamental legislative initiation to influence fiscal decentralisation can be traced back to Resolution No. 108/CP on 13 May

1978 in the Five Year Plan (FYP) for 1976 – 1980. Under this regulation, SNGs' revenues, which were constrained by their spending responsibilities<sup>2</sup>, included fixed owned source revenue and shared taxes. In the case of shared taxes, the tax sharing rates with jurisdictions were predetermined by the national government. Fiscal transfers were arranged if SNGs were in need after using up all revenue from their owned source and shared taxes. As a result, revenue and spending from SNGs increased by 43.5% and 1.5% in 1980 compared with those in 1976. In short, the first FYP after national reunification laid the foundation for fiscal decentralisation by assigning significant expenditure responsibilities to SNGs but it did not assign commensurate taxing powers to them.

Resolution 138-HDBT on 19 November 1983 in the FYP for 1981 to 1985 could be seen as a challenge. SNGs' revenues, which were no longer constrained, were determined by the economic capability of locality. If SNGs revenue collected exceeded the assigned amount, SNGs' budgets received more from the exceeded amount. Tax sharing rates were the same across provinces. However, localities in financial difficulty were eligible to receive more revenues from shared taxes by increasing the sharing rates. With this regulation, 24 provinces were financially independent from the national government in 1988. In the FYP for the period from 1986 to 1990, Resolution 186/HDBT on 27 November 1989 was important for fiscal decentralisation because it turned to ensure that SNGs spending would be assigned based on their fiscal capacity of taxing powers. Also, tax sharing rates were different across provinces because a simple formula has been used depending on the SNGs' owned source revenue and spending assignment. When SNGs revenue is greater than their spending responsibilities, the surplus must be transferred to the national government. As a result, there were 14 out of 44 provinces contributed to the total consolidated government budget.

1996 can be considered as the first year in its fiscal history when Vietnam issued and implemented the first Law on State budget<sup>3</sup>. This Law is effectively seen as a fiscal constitution for budget management in Vietnam. Law 1996 stated revenue and spending responsibilities for the national government as well as for subnational governments. Two years after issuance of the State budget law, in 1998, a revised budget law was issued. There were almost no changes of principles of the issue. The only changes were that the assignments of revenue and spending responsibilities to subnational governments were extended. The Law did not mention spending responsibility and tax revenue for SNGs at district and commune levels. This was implicitly understood that the government at provincial level had to make all these related decisions.

Various recent policies have confirmed the extent of fiscal decentralisation process in Vietnam. Some typical ones are Decree No. 93/2001/ND-CP on 12 December 2001 which allowed Ho Chi Minh City to implement the policy of management decentralisation as the pioneering city in Vietnam. In addition, with Decree No. 141/2003/ND-CP on 20 November 2003, the issuances of urban bonds from SNGs governments at provincial levels are officially permitted. This is the basis and official foundation for subnational borrowing. After that, by many regulations, after the success of pioneering program from Ho Chi Minh

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<sup>2</sup> It means that SNGs revenue was not decided based on respective jurisdiction's capacity of fiscal resources but it was determined based on assigned spending responsibilities to the jurisdiction from the national government.

<sup>3</sup> In this context, this means total consolidated government budget.

City, further decentralisation of taxing powers and spending responsibilities have been assigned to Ho Chi Minh City, Hanoi and Haiphong – the three largest cities in Vietnam.

In conclusion, since the first Five Year Plan after the national reunification, Vietnam's fiscal arrangements have become progressively more decentralised. The process initially focused on the assignment of expenditure responsibilities, it then turned to the taxing power assignments to subnational governments. Once these two important and first- order issues have been implemented, fiscal transfers from the national government and SNGs borrowings were also considered. Starting with the largest city in terms of size, economic growth, per capita income, and population, Ho Chi Minh city, Vietnam has shown its prudent steps to the process of fiscal decentralisation. Experiences from Ho Chi Minh city have then been applied to other selected cities before popularly implemented for the whole nation.

### **III. Fiscal federalism: Fiscal autonomy and fiscal importance**

#### **1. Background**

Tiebout's classic article "A pure theory of local expenditures" was published in 1956. Over the next half a century, the field of fiscal federalism has developed substantially and contributed to a large body of literature on fiscal decentralisation. Seminal studies by Tiebout (1956), Musgrave (1959) and Oates (1972) laid the foundation for the significant discussions of fiscal decentralisation. Tiebout (1956) introduced the notion of local public expenditures to demonstrate that, in a fiscally decentralised country, perfect mobility of citizens between localities will result in competition among localities in providing goods and services; and, as a result, production efficiency will be enhanced. In short, Tiebout saw fiscal decentralisation as a mechanism for overcoming the problem of free riding in public economics. Three years later, Musgrave (1959) laid the general foundations for modern public finance theory, stressing that the best allocation of scarce resources will be achieved whenever preferences and tastes of local citizens have been met. In addition, Oates (1972) argued that there should be variations in the provisions of public goods and services from the governments since inhabitants have different tastes in their consumption patterns. From this perspective, subnational governments (SNGs) will better understand their local citizens in comparison to the national government which always provides the same bundles of goods across regions without regard to regional variations in tastes and preferences. In addition, if the national government is the only provider of public goods and services for the community, there will be no incentive for it to improve production efficiency due to non existence of competition, whereas subnational governments have to face the fierce competitions from neighbourhoods. Oates formalised treatment of the issue by developing the first *decentralisation theorem*:

"For a public good – the consumption of which is defined over geographical subsets of the total population, and for which the costs of providing each level of output of the good in each jurisdiction are the same for the central or the respective local government – it will always be more efficient (or at least as efficient) for local governments to provide the Pareto-efficient levels of output for their respective jurisdictions than for the central government to provide *any* specified and uniform level of output across all jurisdictions" (Oates, 1972, p. 35).

For whatever expectations on fiscal decentralisation are, one of the most important goals needs to achieve from and by fiscal decentralisation is to attain economic growth. Recent researches have attempted to clarify the possible relationship between the two variables of interest – fiscal decentralisation and economic growth. In these studies, two different methodological approaches - The endogenous growth model of Barro (1990) and Augmented Solow (1956) model of economic growth; and diverse designs of fiscal decentralisation dimensions have been used. There have been around six cross-country studies and several ones on particular economies: three for China, two for the US, one for India, one for Germany, one for Russia (Breuss and Eller, 2004). However, in general, evidences from both theoretical and empirical analyses have provided mixed results.

The main basis for supporting fiscal decentralisation centres on the economic efficiency gains. Efficiency may basically come from an efficient allocation of scarce resources as well as fierce competition among subnational governments. Efficiency improvement will clearly increase GDP. However, it is unclear whether this result is a one-off increase in GDP but no on-going increase in the growth rate, or both a one-off increase and on-going increase in the growth rate. Static economic theory provides a compelling case for a one-off increase in GDP, the case for economic growth as well depends on dynamic issues and dynamic theory which is less well established because many different factors may influence to economic growth.

## 2. Fiscal autonomy and fiscal importance

Subsequent to Oates' theorem, discussions on fiscal decentralisation have centred on four main areas: the assignment of expenditure responsibility; revenue assignment (taxing powers); intergovernmental fiscal transfers; and subnational borrowing<sup>4</sup>. Conceptually, these topics can be divided into two broad categories: (i) fiscal autonomy of subnational governments; and (ii) fiscal importance of subnational governments. In this regard, fiscal autonomy of SNGs mainly deals with the assignment of taxing powers, including supplementary tools such as intergovernmental fiscal transfers, subnational borrowing and the assignment of responsibility for public provision of goods and services, whereas fiscal importance is directly connected with the level of expenditure responsibility of SNGs relative to the level of all government expenditures.

### 2.1 Fiscal autonomy of SNGs

Agreement on the distribution of taxing powers is difficult since the players (national government and SNGs) approach their respective powers from two different perspectives. While the national government continues keeping important tax sources for economic stabilisation and income redistribution, SNGs focus on taxing powers to generate stable revenue to implement their duties in provision of public goods and services which are fundamental to community welfare such as healthcare, education and public order<sup>5</sup>. If tax assignment is extensive, the gap between spending responsibility and taxing power of SNGs will be minimised or eliminated, leading to fiscal autonomy of SNGs<sup>6</sup>. Fiscal autonomy of

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<sup>4</sup> See in Bird (1999 and 2000), Martinez-Vazquez (2001), McLure and Martinez-Vazquez (2004), Musgrave (1983), Shah (2004), Ter-Minassian (1996).

<sup>5</sup> See also in Bird (1999 and 2000); McLure (1998) and Musgrave (1983).

<sup>6</sup> If debts of SNGs are zero, then fiscal autonomy is associated with SNGs expenditures being fully funded from owned source revenues.

SNGs implies that, to some extent, SNGs can arrange their owned source revenue by exercising their taxing powers to cover costs occurring in the provision of public goods and services. As a result, intergovernmental fiscal transfers will no longer be a significant source of revenue for SNGs. It should be noted, however, that even in the absence of fiscal transfers (“grants”), SNGs will not enjoy full fiscal autonomy if they receive taxes or revenue shares directly from the national government when all tax bases and rates are centrally determined (McLure, 2001). The necessary condition for a significant level of fiscal autonomy is that SNGs themselves have the discretion to set the tax rates and/ or bases (so that they can adjust their revenue by varying the rates and/ or the bases) in response to fiscal demand for publicly provided goods and services. If this is not the case, flexibility and the potential for creativity by SNGs for the efficient provision of public goods and services is limited.

In transition periods for developing countries, “piggybacking” is a common practice to grant fiscal autonomy for SNGs by allowing them to set the rates as the surcharge on the bases which are determined by the national government. Also, tax rates set by SNGs are only allowed to vary within the band centrally determined which obviously acts as a bounded constraint on SNGs’ fiscal autonomy, resulting in only partial fiscal autonomy. However, piggybacking can be difficult to implement in developing countries, mainly because the marginal tax rates of the national government are usually set very high, so that there is no room for an additional SNG “surcharge” on the same tax bases.

In the event of a long-period mismatch between SNGs’ spending responsibility and revenue capacity, vertical fiscal imbalance<sup>7</sup> will inevitably emerge and must be managed by the national government through intergovernmental fiscal grants and advances. If SNGs are given adequately fiscal autonomy, ex-post vertical fiscal imbalance is expected to be minimised before any fiscal transfer takes place<sup>8</sup>. However, it is also argued that if the national government focuses exclusively on filling the gap of vertical fiscal issues, this decision may reduce the incentive for the SNGs to increase their respective taxing powers and to manage public spending efficiently (Ahmad and Craig, 1997). One option for reducing the vertical fiscal imbalance without reform of tax assignment is to re-assign some spending responsibility for goods and services provision from SNGs to the national government. Nevertheless, experience suggests that mismatch between spending and taxing will also provide some balancing role for the national government in fiscal transfers (Bird and Smart, 2002).

There are a wide range of aims that the national government needs to achieve when designing the system of fiscal transfers. From a fiscal autonomy perspective, the principle issue is whether fiscal transfers are conditional or unconditional. That is, the extent of discretion that SNGs enjoy concerning the expenditure of these transfers. While the issue of when to, and how to, equalise transfers is important in its own context, it is generally a second order issue for fiscal autonomy<sup>9</sup>.

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<sup>7</sup> Vertical fiscal imbalance implies a mismatch between owned source revenue (excluding grants from other levels of governments) and own purpose spending (excluding grants to other levels of governments) for a particular level of government (Collins, 2001).

<sup>8</sup> This happens at least for the aggregate of SNGs. It is still possible, of course, for individual SNG to run deficits or surpluses, even when the vertical fiscal imbalance to be eliminated between the national government and the aggregate of the SNGs.

<sup>9</sup> The system of fiscal equalisation which is a complex issue is beyond the scope of this paper.

Fiscal autonomy of SNGs is clearly an important feature of fiscal decentralisation. Discussion on the degree of fiscal decentralisation of a particular country without dealing directly with local fiscal autonomy is only partial. However, fiscal autonomy is only one aspect of fiscal decentralisation, which also depends on the proportion of national fiscal activity undertaken by SNGs, or their “fiscal importance”.

## 2.2 Fiscal importance of SNGs

In theory, the economic performances of the government should become more productive, efficient and effective if services are provided by the lowest level of government possible. This is known as principle of subsidiarity (Martinez-Vazquez, 2001). While foreign policy, defence, immigration, international trade can be best formulated and implemented by the national government, SNGs are able to carry out some important tasks for provincial communities such as law, order and public safety, education, health policy, as well as very local issues such as street lighting system, local sewerage, garbage collection, local paper deliveries, etc. Services provided by the national government confirm the law of subsidiarity when demand is at a constant level across the various subnational localities. However, when demand varies from location to location, national provision to a common standard leads to inefficient under-provision, in some areas, and inefficient over-provision, in other areas. In short, services provided by the national government assume tastes and preferences to be homogeneous across locations and for citizens within locations.

However, SNGs can provide goods and services based on the size of jurisdiction, and in accordance with local tastes and preferences (Shah, 2004). If the size of jurisdiction is considered, the principle of benefit matching will be achieved because local citizens who receive benefits also bear costs. Also, cost for publicly provided goods and services can be recovered, at least at the margin, so that the pressures from the lack of financial resources for SNGs decrease. As a consequence, services are expected to be provided more efficiently. SNGs operate closely to local inhabitants so that they are the sole agents, who are in the best position to understand preferences, tastes and amount demanded. It is clear that levels of goods and services provided should not be exceeded the amount demanded by the community. This can avoid both under or overprovision of public goods and services. Moreover, a system of fees, users’ charges can be considered useful and effective for the purpose of cost recovered (McLure and Martinez-Vazquez, 2004).

On the basis of the law of subsidiarity, one would expect that it is efficient for SNGs to account for a significant proportion of fiscal activity across the nation. The larger the portion of the spending cake is for SNGs, the higher the degree of fiscal importance is granted to them. This needs to be recognised in any index of fiscal decentralisation.

## 2.3 Theoretical and empirical studies

The theoretical case for a relatively high degree of fiscal decentralisation outlined in 2.2 and 2.3 is quite clear. Efficiency has attracted a great attention from policymakers and economists. Supports for fiscal decentralisation will become much less persuasive if their discussions are separated from the ground of economic efficiency. This implies that

efficiency in the provision of public goods and services by SNGs will be translated into an one-off GDP increase by reducing and/ or minimising wastages and allocating scarce resources in efficient manner. If this is accompanied by greater fiscal competition between jurisdictions and resulting an increase in positive fiscal externalities, a higher degree of fiscal decentralisation may also be associated with higher rate of economic growth. However, it must be cautioned that this conclusion is not yet supported unequivocally by empirical studies. This appears, in part, to be due to use of inappropriate indices of fiscal decentralisation, which ignore either fiscal authority or fiscal importance of SNGs. This matter will be further discussed in section V.

#### IV. Vietnam and fiscal decentralisation

After national reunification in 1976, fiscal environment in Vietnam has changed significantly. This change can be confirmed in different legal documents governing fiscal arrangement issued in the period. It is generally agreed that Vietnam is pursuing a process of fiscal decentralisation – at least in terms of increasing the fiscal importance of SNGs<sup>10</sup>.

The outcomes of the State budget revenue and expenditure decentralisation in Vietnam for the period from 1997 (the first year of implementation of the First Budget Law) to 2004 are shown in Table 3. Revenues for SNGs have continuously increased, around 30% total government revenue for the period. In addition, there has also been an increase in the share of subnational expenditures in the total expenditures. The share has been almost 40% for the whole period. Even though the concept of fiscal decentralisation has multi-dimensions, from the aspects of expenditure and taxing assignments, Vietnam can be considered moderately decentralised (Martinez-Vazquez, 2004). However, without further consideration of the other dimensions, this comment may be misleading.

TABLE 3  
**REVENUE & EXPENDITURE DECENTRALISATION IN VIETNAM**

	1997	1998	1999	2000	2001	2002	2003	2004
Revenue (VND Billions)	65,352	70,612	78,489	90,749	103,773	121,716	141,930	149,320
Of which:								
Local budget revenue	19,264	20,280	19,571	22,269	25,463	30,545	38,683	44,743
Share in total budget revenue	29.5	28.7	24.9	24.5	24.5	25.1	27.3	30.0
% Growth rate (previous year = 100%)								
Total budget revenue	4.8	8	11.2	15.6	14.4	17.3	16.6	5.2
Local budget revenue	8.5	5.3	-3.5	13.8	14.3	20.0	26.6	15.7
Expenditure (VND Billions)	78,057	81,995	95,972	108,961	129,773	148,208	177,150	187,670
Of which:								
Local expenditure	28,039	31,808	39,040	45,082	56,043	64,573	66,254	67,184
Share in total expenditure	35.9	38.8	40.7	41.4	43.2	43.6	37.4	35.8

<sup>10</sup> Since Vietnam is a unitary country, the term “SNGs” or “local governments” will be used interchangeably.

% Growth rate (previous year = 100%)								
Total budget expenditure	10.7	5.0	17.0	13.5	19.1	14.2	19.5	5.9
Local budget expenditure	19.1	13.4	22.7	15.5	24.3	15.2	2.6	1.5
Fiscal transfers (VND Billions)	9,964	12,290	20,510	26,601	23,553	35,278	38,040	35,048
% Growth rate (pre. year = 100%)	35.4	23.3	66.9	29.7	-11.5	49.8	7.8	-7.9
Share in total local expenditure	35.5	38.6	52.5	59.0	42.0	54.6	57.4	52.2

Source: Martinez-Vazquez (2004, p. 16).

## 1. The assignment of expenditure responsibility

The current State budget law indicates responsibilities for expenditure between national and local governments. However, these regulations are not clear and overlapping in goods and services provision by different levels of governments is not uncommon. This violates the principle of clarity and is known as the co-sharing services responsibility. When possible, co-sharing responsibility should be avoided because the ambiguity will create unnecessary duplication in the provision of public goods and service to local communities, and, in turn, negatively affect the efficiency of the spending programs. The other problem with co-sharing spending is that this may, intentionally or unintentionally, confuse the assignment of responsibility across each level of governments, and therefore accountability and transparency may be in danger. Table 3 shows that total SNGs' expenditure for the period is around 40% total government spending. If the dimension of expenditure is used, Vietnam is moderately decentralised. It is however cautioned that the majority portion of SNGs' spending is a consequence of national government policy decisions. SNGs have limited discretion to decide the spending areas for their locality. In this case, SNGs are only spending units. As a result, conclusion of decentralised spending responsibility for SNGs can provide misleading information.

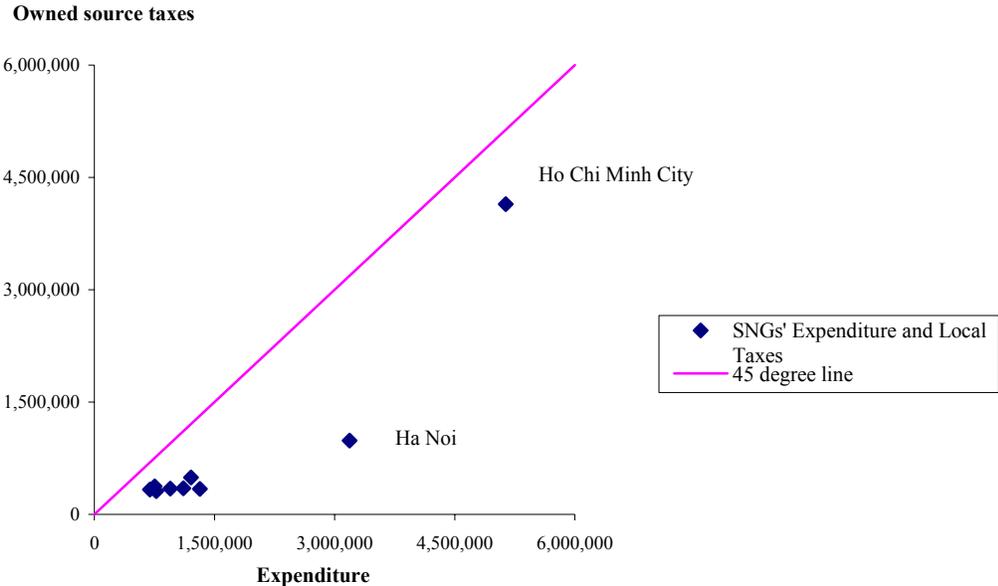
## 2. Revenue assignment (taxing powers)

Figures in Table 3 indicate that SNGs share of total government revenue is around 30%. This figure is only partial. For a more complete view on the current status of the taxing power assignment in Vietnam, the following factors should be taken into serious consideration: firstly, the national government sets all tax bases and rates; secondly, SNGs are allowed to autonomously set fees and charges for only revenues that comprise an insignificant share of their budget; and thirdly, tax collections are centralised with local tax authorities only collecting revenues arising within their administrative regions on the national government's behalf.

Consequently, purely local taxes are extremely limited in Vietnam. Figure 2 below shows the relationship between SNG's expenditures and its respective local taxes. This relationship reflects the degree of fiscal imbalances between the national and local governments. The sample of nine localities is selected among 64 provinces and cities in Vietnam based on the significant portion of local revenue to be transferred to the national budget. These cities and provinces are "typical" representatives for fast economic growth at regions across the nation, comprising the five big cities which were granted a provincial

status, as previously mentioned, and another four big provinces (Khanh Hoa, Dong Nai, Binh Duong and Baria – Vung Tau). No provinces experience a fiscal balance. All selected provinces experience some degree of fiscal imbalance. This conclusion can be applied for the whole Vietnam because the selected localities are the biggest provinces in the country.

**FIGURE 2**  
**FISCAL AUTONOMY OF SUBNATIONAL GOVERNMENTS**  
**IN VIETNAM - LOCAL TAXES**



In addition, shared national and subnational taxes also play very important portion in local revenues. In the case of Vietnam, SNGs have no discretion to change these bases and rates. As a result, SNGs have no power to adjust their revenue even at the margin. Also, it is noted that types of taxes to be shared and the proportion in which the taxes are shared are set by the national government. Even after the shared taxes take play, majority provinces in Vietnam are still in the fiscal imbalance condition as Figure 3 shows below. In this sample, only Ho Chi Minh City and Baria – Vung Tau are not in fiscal imbalance. Da Nang, Binh Duong and Dong Nai are at the margin whereas Ha Noi and Khanh Hoa, and all other provinces which are not shown in the Figure, are still in the condition of fiscal imbalance. This confirms the significant role of intergovernmental fiscal transfers in Vietnam.

**FIGURE 3**  
**FISCAL AUTONOMY OF SUBNATIONAL GOVERNMENTS**  
**IN VIETNAM - LOCAL AND SHARED TAXES**

Owned source and shared taxes

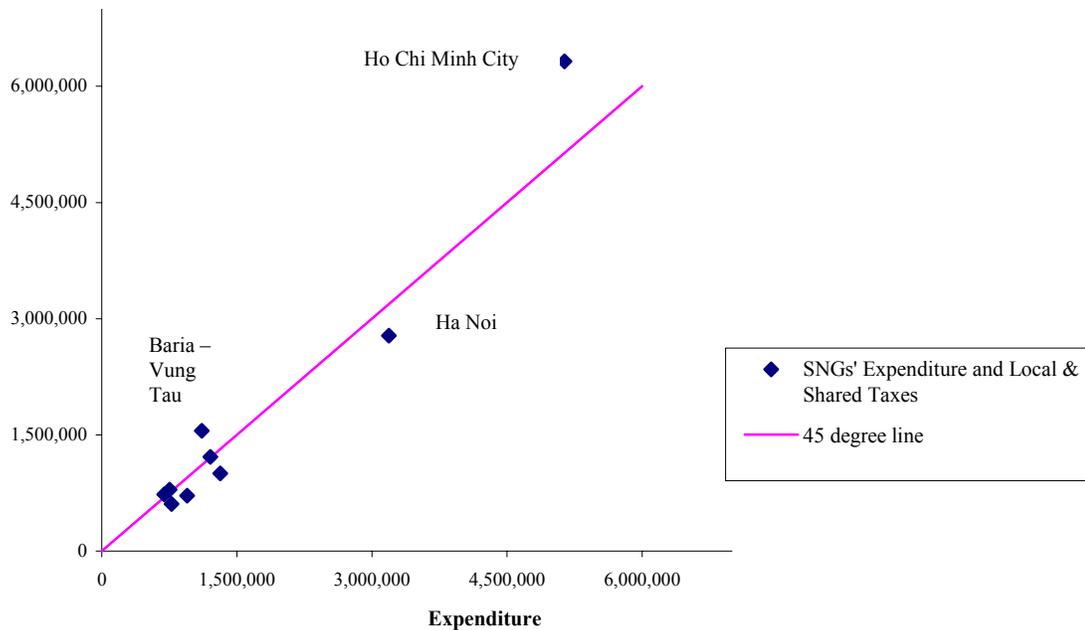


Table 4 shows the tax assignment for 2003 in Vietnam. Exclusively national government's taxes include export-import duties and excise tax. The taxes shared between the national and subnational governments comprise value added tax; corporate income tax; and personal income tax. Many minor taxes are fully assigned as the owned taxes for SNGs, such as tax on transfers of properties, licence tax, agricultural tax; land and housing tax; tax on land use rights; and etc. Table 4 reveals that almost two-thirds of total government tax revenue is generated by shared taxes. As national taxes account for one-third of the total revenue, it can be seen that fiscal arrangements in Vietnam are in fact highly centralised. SNGs are assigned with many different taxes, but they generate only 3% total tax revenue. Taken as a whole, this provides prime facie evidence of centralised fiscal arrangements in Vietnam.

Table 4

**APPROXIMATE TAX ASSIGNMENT IN VIETNAM IN 2003**

Item	Percent of total tax revenue
<u>A. National taxes</u>	
Export - Import Duties	24
Excise Tax	9
Subtotal	<u>33</u>
<u>B. Shared taxes</u>	
Value Added Tax	30
Corporate Income Tax	31

Personal Income Tax	3	
Subtotal		<u>64</u>
C. <u>Subnational taxes</u>		
Licence Tax, etc.	1.6	
Tax on transfers of properties	1.4	
Subtotal		<u>3</u>
Total		<u>100</u>

Source: IMF Country Report No. 03/382 & author's calculations.

### 3. Intergovernmental fiscal transfers

Like other developing countries, Vietnam suffers from the fiscal imbalance in both vertical and horizontal dimensions. The country has an implicit system of equalisation grants, although it is very partial in character. Fiscal equalisation has been applied in Vietnam with two main components: the expected revenue and the minimum expenditure need of local governments. Expected revenues for SNGs are determined by the subnational branch of tax administration, say, from Ho Chi Minh City Tax Department, on the basis of the actual revenue collections of the previous years, taking into account changes in tax policies in the year; and expected economic growth rate during the year. In addition, minimum expenditure needs are calculated on the basis of the expenditure norms determined by the national government (Martinez-Vazquez, 2004). The difference between expected revenue and minimum expenditure need for specific city or province will lay the foundation for the national government to decide the sharing rates which are applied to revenue from the shared taxes between national and local government. With one city or province, if its expected revenue (revenue from both owned source and shared taxes) is less than its minimum expenditure need, this city or province is allowed to keep all proceeds from shared taxes at local budget. This means that the local region is eligible to keep all tax revenue arising within its jurisdiction. On the other hand, with the well-endowed region where its expected revenue is greater than its minimum expenditure need, revenue from shared taxes must be transferred to the state budget at the rate to be centrally determined. These calculations will be kept unchanged for the stability period from 3 to 5 years. For example, in 2002, the allocation rates of shared tax revenue to SNGs vary with Ho Chi Minh City and Hanoi receiving 24% and 30% shared tax revenue, respectively; whereas other less well endowed provinces received all 100% of shared tax revenue, except for Baria – Vung Tau (48%), Binh Duong (52%) and Dong Nai (53%). The current regime in Vietnam, in a serious sense, is not a real system of fiscal equalisation because the gap among provinces is still large after equalisation.

TABLE 5

#### FISCAL AUTONOMY OF SELECTED PROVINCES AND CITIES IN VIET NAM IN 2002

No.	Province	Total SNG's Expenditure (Bil. VND)	Subnational governments (Billions VND)				Total SNG's Revenue (Bil. VND)
			Owncd taxes	Shared taxes	Owncd and Shared taxes	Transfers	
1	Ha Noi	3,188,420	986,734	1,796,224	2,782,958	1,516,082	4,299,040
2	Hai Phong	1,316,180	341,555	662,350	1,003,905	624,564	1,628,469
3	Da Nang	751,700	373,299	420,008	793,307	337,764	1,131,071

4	Khanh Hoa	773,700	310,038	297,393	607,431	427,780	1,035,211
5	Ho Chi Minh City	5,137,430	4,144,416	2,178,631	6,323,047	602,331	6,925,378
6	Dong Nai	1,207,000	493,872	720,531	1,214,403	318,941	1,533,344
7	Binh Duong	691,880	332,051	398,763	730,814	241,374	972,188
8	Ba Ria Vung Tau	1,111,430	347,127	1,205,785	1,552,912	295,891	1,848,803
9	Can Tho	947,530	345,232	369,807	715,039	412,229	1,127,268

Source: Martinez-Vazquez (2004, p. 29).

There are two basic types of intergovernmental grants in Vietnam, unconditional and conditional. For conditional transfers, there are two different types. The first is for the implementation of national programs such as Program on Hunger Eradication and Poverty Reduction; Program on Education and Training. The second type of conditional grants is to particular province(s) and is allocated at the national government's discretion. In addition, Vietnam does not have an explicit separate system of capital transfers. Funds for capital investment are tailored in the equalisation transfer and are basically very limited (Martinez-Vazquez, 2004).

#### 4. Subnational borrowings

In the case of Vietnam, mismatch between expenditure and revenue assignments is significant even after fiscal equalisation from the national government. As a result, subnational borrowings are, in some cases, important. Current practice in Vietnam shows that provincial governments are allowed to borrow from domestic sources by issuing bonds. However, these borrowings are closely supervised by the national government. The only exclusion from international borrowing applies to Ho Chi Minh City, Hanoi and Haiphong – the three largest cities in Vietnam. However, even in these cases, direct overseas borrowing is not permitted. The city's government looks for a source of fund, negotiates terms and conditions and then requests the national government to undertake the borrowings and on lending to the respective city.

### V. The development of the fiscal decentralisation index

#### 1. Background

To date, studies of the relationship between fiscal decentralisation and economic growth have only undertaken very crude measures of fiscal decentralisation. Oates (1972) used the national government share in total public revenue as the degree of fiscal decentralisation. Woller and Phillips (1998) measure fiscal decentralisation as one out of four scenarios as follows: (1) the ratio of local government revenues to total government revenues; (2) the ratio of local government revenues less grants-in-aid to total government revenues; (3) the ratio of local government expenditures to total government expenditures and (4) the ratio of local government expenditures to total government expenditures less defence and social security expenditures. Davoodi and Zou (1998) measured the level of fiscal decentralisation as the spending by SNGs as a fraction of total government spending.

It is widely admitted that the measurement of fiscal decentralisation on previous works is problematic because of “from lack of details on expenditure autonomy and own-source

revenue to deficiencies regarding reported data for the sub-national levels and information scarcity for analysing dispersion among sub-national regions” (Breuss and Eller, 2004, p.12). In fact, the above measures are inadequate because fiscal autonomy and fiscal importance of SNGs has not been properly taken into consideration. As a result, the theoretical literature is extended in this study by developing and applying a fiscal decentralisation index (“FDI”) to make systematic international comparisons of nations’ degree of fiscal decentralisation.

## 2. Establishment of the formula to calculate the fiscal decentralisation index

There are two main components included in the formula of FDI in this paper:

### \* Component 1: Fiscal autonomy for subnational governments

This component will represent the ratio between *the owned source revenue* (OSR) over its *expenditure* (E) for particular subnational government. This ratio can be seen as the level of vertical fiscal imbalance between the national government and SNGs. It is however noted that both definitions of “owned source revenue” and “expenditure” of SNGs can provide misleading indicator of its fiscal autonomy, and in turn, the degree of fiscal decentralisation of the country. Also, a simple ratio like this is partial, as it misses many factors that impact on fiscal decentralisation. Consequently, an *adjustment factor* (AF) is required to account for institutional constraints on fiscal events, such as the fiscal autonomy and fiscal importance over the four main areas of fiscal decentralisation and will be discussed further in the following sections (Section V.3).

As a consequence, the relative level of autonomy, which can be called “fiscal autonomy”, for SNGs can be defined as follows:

$$FDI' = \frac{\sum_{i=1}^n OSR_i}{\sum_{i=1}^n E_i} \times AF, \quad (1)$$

where  $OSR_i$  represents for the owned source revenue for subnational region  $i$ ;  $E_i$  represents for the expenditure made by subnational region  $i$ ;  $AF$  represents the adjustment factor for the country under review; and  $n$  is the number of subnational regions.

The above formula is expected to reflect the true picture of the degree of SNGs’ autonomy – the very important characteristic of appropriate definition of fiscal decentralisation. However, the formula does not yet indicate the degree of fiscal decentralisation because it only shows the degree of autonomy of SNGs, not the level of fiscal activity by SNGs relative to all public fiscal activity.

### \* Component 2: Fiscal importance of SNGs

The absolute level that represents the fiscal importance of SNGs can be defined as follows:

$$FDI'' = \frac{\sum_{i=1}^n E_i}{TE}, \quad (2)$$

where  $TE$  represents total public sector expenditures of the whole economy (including both expenditures from the national government and all SNGs).

This formula shows the fiscal importance of SNGs in the field of spending for the whole economy. For example, what would we conclude regarding the degree of autonomy of subnational region R when its owned source revenue and its expenditure are both 10 units, when its adjustment factor is unity whereas total national revenue and expenditure are both 1,000 units. If equation (1) is used, we would conclude that a  $FDI'$  is equal to unity, so that this region has achieved a highest possible level of fiscal decentralisation. However, this is not the case as the national government still retains all taxing and spending decisions.

#### The fiscal decentralisation index

To overcome the above problem, we need to use equations (1) and (2) simultaneously to give a reliable index. It is provisionally proposed that the index be the geometric mean of  $FDI'$  and  $FDI''$  :

$$FDI = \sqrt{\left( \frac{\sum_{i=1}^n OSR_i}{\sum_{i=1}^n E_i} \times AF \right) \times \left( \frac{\sum_{i=1}^n E_i}{TE} \right)} \quad (3)$$

(A)                      (B)

If we exclude the role of the adjustment factor AF in equation (3), as components (A) and (B) are to be both positive fractions, we can conclude that FDI will also be a positive fraction. Also, the higher the value of FDI, the more fiscally decentralised is the country.

### 3. Elements to be considered for the adjustment factor

Now we turn to the question of the value of the adjustment factor AF. The size of fiscal decentralisation index (FDI) will also depend on the size of the adjustment factor. Because of the value assigned for each element and the method of calculating the value of the AF, it is expected that the value of FDI will vary within the range from 0 to 1. The higher the value of the FDI, the higher the degree of fiscal decentralisation.

The elements noted in Table 6 below need to be accounted for when deriving the adjustment factor. In the first instance, the scale of 0 to 1 will be assigned to each important element with 0 represents as the lowest level (the worst) and 1 represents as the highest level (the best) in terms of decentralisation of the element being considered. The adjustment factor in equation (1) will be calculated as a simple average of the assessments for the four elements in Table 6. However, in the course of the subsequent research, other weightings and methods will be investigated.

The above formula for the FDI implicitly applies the same weight to every subnational region of the country. This may lead to some undesirable implications, however. In the course of future research, the dispersion of the size of SNGs will be considered. Where the country consists of many subnational regions of substantially different size in terms of population, land area, total revenue and expenditure, etc., it may be necessary to assign each region a different weight, rather than weight them all equally. Another way of proceeding

would be to modify the FDI so that it reflects this dispersion by including in it another term that is the function of the standard deviation of the shares.

**TABLE 6**  
**ELEMENTS OF THE ADJUSTMENT FACTOR**

Score	Level	Criteria
<i><b>Factor 1: Autonomy on expenditure decisions to various levels of governments</b></i>		
0	Very low	All spending areas are set by the national government and SNGs must follow the instructions.
0.25	Low	Unclear assignments of responsibilities with limited areas that SNGs can decide to spend on.
0.5	Moderate	Clear assignments of responsibilities with spending standards are set by the national government.
0.75	High	SNGs are basically able to decide their spending decisions with limited guides from the national government.
1	Very high	SNGs decide all their spending decisions without any intervention from the national government and this autonomy is assured by the Constitutions and/ or laws.
<i><b>Factor 2: The degree of autonomy of various levels of governments to set tax bases and tax rates</b></i>		
0	Very low	National government sets SNGs' tax bases and rates;
0.25	Low	Significant portion of SNGs' budget comes from share taxes and the sharing rate is predetermined. SNGs can set bases and/ or rates for fees, users' charges only.
0.5	Moderate	SNGs are allowed to set either tax bases or rates or "piggy-backing" is possible.
0.75	High	All bases and rates for SNGs taxes are set by SNGs within a band set by the national government.
1	Very high	SNGs set all bases and rates for their taxes which generate significant amount of revenue.
<i><b>Factor 3: Responsibilities of SNGs for borrowing and conditions for local governments to access to capital markets</b></i>		
0	Very low	No subnational borrowings are allowed.
0.25	Low	SNGs can arrange for domestic borrowings with administration and veto in the hands of the national government.
0.5	Moderate	SNGs can arrange borrowings from both domestic and overseas sources but all borrowings must satisfy strict requirements from the national government.
0.75	High	Borrowing from any sources is acceptable given some economic regulations are met.
1	Very high	SNGs can arrange borrowings as they wish and the capital market itself will decide whether or not the borrowing is given.
<i><b>Factor 4: Intergovernmental fiscal transfers across levels of governments</b></i>		
0	Very low	Ad hoc decision from the national government with rooms for political lobby and negotiation.
0.25	Low	Fiscal transfers are almost all conditional on their use and they are decided on a yearly basis.
0.5	Moderate	All types of fiscal transfers are clearly regulated with a stability period.
0.75	High	Formula has been used and a combination of conditional and unconditional transfers is available.
1	Very high	Clear and developed regimes for unconditional fiscal transfers have been set up and implemented. These regimes are assured by the Constitution and/ or laws and transfers are significantly unconditional.

## VI. Preliminary values for the fiscal decentralisation index

### 1. Values assigned for each factor of the adjustment factor for Vietnam

In accordance with suggested standard elements of the adjustment factor as discussed above, current practices in Vietnam in terms of the assignment of responsibility, taxing power assignment, SNGs borrowings and fiscal transfers can be summarised as follows.

**TABLE 7**  
**ADJUSTMENT FACTOR FOR VIETNAM**

Factor	Current practices in Vietnam	Score
1	<ul style="list-style-type: none"> <li>▪ After the introduction of Budget law, provincial and local governments assumed major new expenditure responsibilities.</li> <li>▪ However, most of the items on this list are perhaps more analogous to sectors that they are functions per se. Basically, expenditure responsibilities are vaguely defined.</li> </ul>	0.25

2	<ul style="list-style-type: none"> <li>▪ Clear assignments of revenues between the national government and local governments as regulated in the State budget law;</li> <li>▪ The national government set all tax bases (except Land tax from 2005) and rates for all taxes that generate significant revenue for the state budget as the whole. Main source of revenue for local governments comes from shared tax with the national government.</li> </ul>	0.25
3	<ul style="list-style-type: none"> <li>▪ Provincial governments can access domestic borrowings, except for there largest cities to borrow from overseas sources;</li> <li>▪ All borrowings must be approved and supervised by the cental government.</li> </ul>	0.25
4	<ul style="list-style-type: none"> <li>▪ Formula has been used in fiscal equalisation in Vietnam and there are two types of grants in Vietnam. Besides the unconditional transfers, there are two types of conditional grants in Vietnam: <ul style="list-style-type: none"> <li>* The first type of conditional transfers is for the implementation of national programs such as Program on Hunger Eradication and Poverty Reduction; Program on Education and Training; and so on;</li> <li>* The second type of grants is the conditional transfer to particular province(s).</li> </ul> </li> <li>▪ Vietnam does not have an explicit separate system of capital transfers. Funds for capital investment are tailored in the equalisation transfer and are basically very limited.</li> </ul>	0.25
<b>Simple Average</b>		<b>0.25</b>

## 2. Preliminary results of fiscal decentralisation index for selected countries

### 2.1 Sample of countries

The main purpose of this research is to establish the fiscal decentralisation index for both developing countries as well as developed economies to facilitate subsequent and hopefully definitive, investigations of the relationship between fiscal decentralisation and economic growth in the later part. It is therefore decided that countries from The Organisation for Economic Cooperation and Development (OECD) and The Association of South East Asian Nations (ASEAN) are to be selected. In order to measure the dispersion of political institutions, both federal and unitary counties are considered. Due to an unavailability of information and data, some countries are only selected. From high income OECD, for federal nations, the sample consists of Australia, Austria, Belgium, Canada, Germany, Switzerland and The United States of America. Representative unitary countries from OECD includes Czech Republic, Denmark, France, Hungary, Italy, Japan, Netherlands, Spain, Sweden and United Kingdom. Finally, for ASEAN, a mixture of federal and unitary countries is considered. Malaysia is the federal country and the selected unitary countries are Indonesia, Thailand, The Philippines and Vietnam.

### 2.2 Results

TABLE 8

#### FISCAL DECENTRALISATION INDEX OF SELECTED OECD & ASEAN COUNTRIES

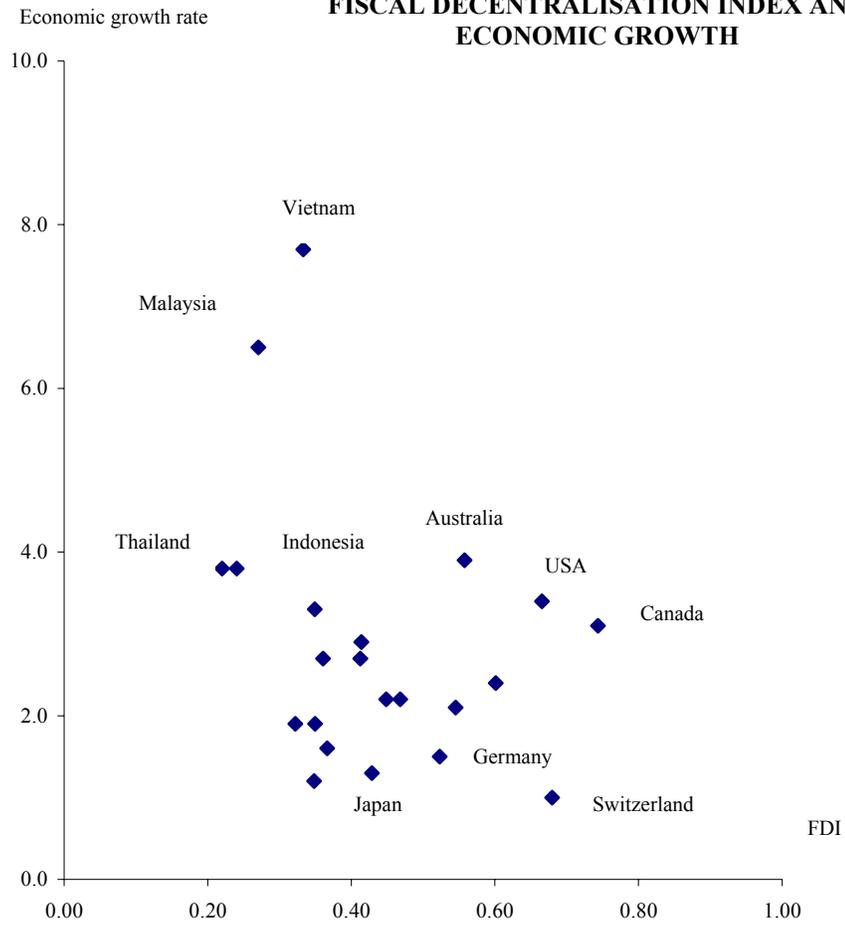
No. Country	Year	Units	Total owned source revenue	Total subnational expenditure	Total expenditure	Adjustment Factor	Fiscal autonomy	Fiscal importance	Fiscal Decentralisation Index
			OSR <sub>i</sub>	E <sub>i</sub>	TE	AF	FDI'	FDI''	FDI
1 Australia	2002	Mil AUD	123,776	124,550	323,603	0.81	<b>0.81</b>	<b>0.38</b>	<b>0.56</b>
2 Austria	2002	Mil Euro	41,020	39,501	127,435	0.63	<b>0.65</b>	<b>0.31</b>	<b>0.45</b>
3 Belgium	2001	Mil Euro	51,655	50,001	162,067	0.69	<b>0.71</b>	<b>0.31</b>	<b>0.47</b>
4 Canada	2002	Mil CAD	318,537	324,082	540,334	0.94	<b>0.92</b>	<b>0.60</b>	<b>0.74</b>
5 Germany	2002	Mil Euro	410,300	443,700	1,125,000	0.75	<b>0.69</b>	<b>0.39</b>	<b>0.52</b>

6	Switzerland	2001	M. Franc	105,575	105,216	185,714	0.81	<b>0.82</b>	<b>0.57</b>	<b>0.68</b>
7	United States	2001	Mil USD	2,022,530	2,040,100	3,997,940	0.88	<b>0.87</b>	<b>0.51</b>	<b>0.67</b>
8	Czech Republic	2002	M. Koruny	228,082	241,823	1,176,090	0.63	<b>0.59</b>	<b>0.21</b>	<b>0.35</b>
9	Denmark	2002	M. Kroner	459,170	462,221	953,389	0.75	<b>0.75</b>	<b>0.48</b>	<b>0.60</b>
10	France	2001	Mil Euro	148,147	146,049	832,789	0.69	<b>0.70</b>	<b>0.18</b>	<b>0.35</b>
11	Hungary	2002	M. Forint	2,072,600	2,196,700	9,978,300	0.50	<b>0.47</b>	<b>0.22</b>	<b>0.32</b>
12	Italy	2000	Mil Euro	164,618	162,934	613,024	0.50	<b>0.51</b>	<b>0.27</b>	<b>0.37</b>
13	Japan	2001	Bil JPY	100,004	97,432	306,192	0.56	<b>0.58</b>	<b>0.32</b>	<b>0.43</b>
14	Netherlands	2002	Mil Euro	71,196	71,940	259,676	0.63	<b>0.62</b>	<b>0.28</b>	<b>0.41</b>
15	Spain	2000	Mil Euro	87,482	89,716	288,994	0.56	<b>0.55</b>	<b>0.31</b>	<b>0.41</b>
16	Sweden	2001	M. Kroner	561,400	566,500	1,415,100	0.75	<b>0.74</b>	<b>0.40</b>	<b>0.55</b>
17	United Kingdom	2002	Mil GBP	118,238	116,610	510,706	0.56	<b>0.57</b>	<b>0.23</b>	<b>0.36</b>
18	Malaysia	1997	M. Ringgit	10,046	13,129	68,610	0.50	<b>0.38</b>	<b>0.19</b>	<b>0.27</b>
19	Indonesia	1999	Mil Rp	29,824,054	27,164,553	225,874,000	0.44	<b>0.48</b>	<b>0.12</b>	<b>0.24</b>
20	Thailand	2002	Mil BHT	161,800	137,800	1,464,400	0.44	<b>0.51</b>	<b>0.09</b>	<b>0.22</b>
21	The Philippines	2000	Mil Peso	138,325	127,925	638,665	0.56	<b>0.61</b>	<b>0.20</b>	<b>0.35</b>
22	Vietnam	2002	Bil VND	65,823	64,573	148,208	0.25	<b>0.25</b>	<b>0.44</b>	<b>0.33</b>

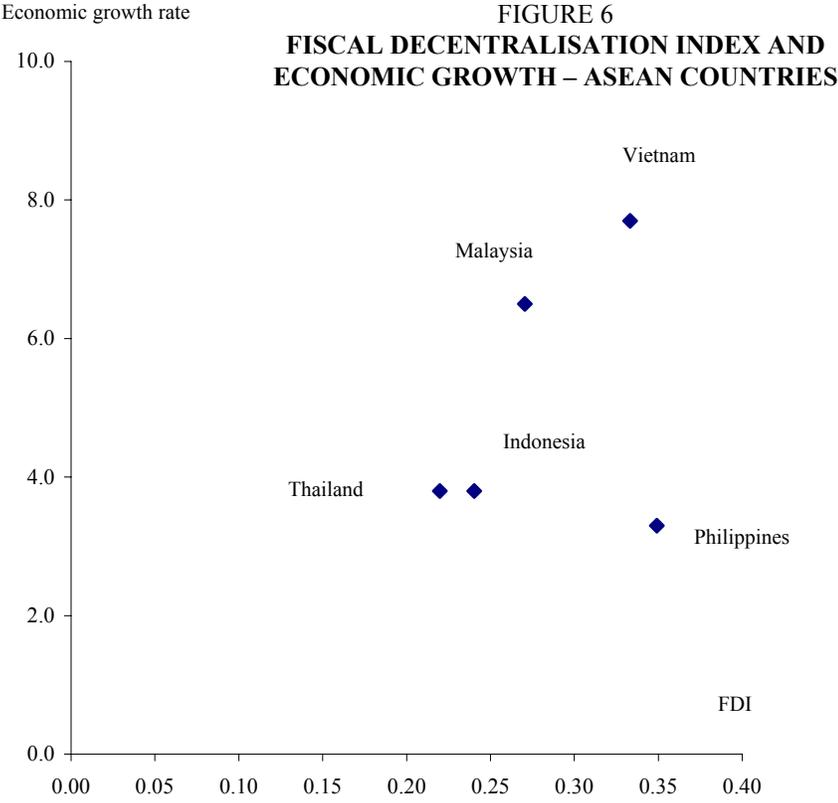
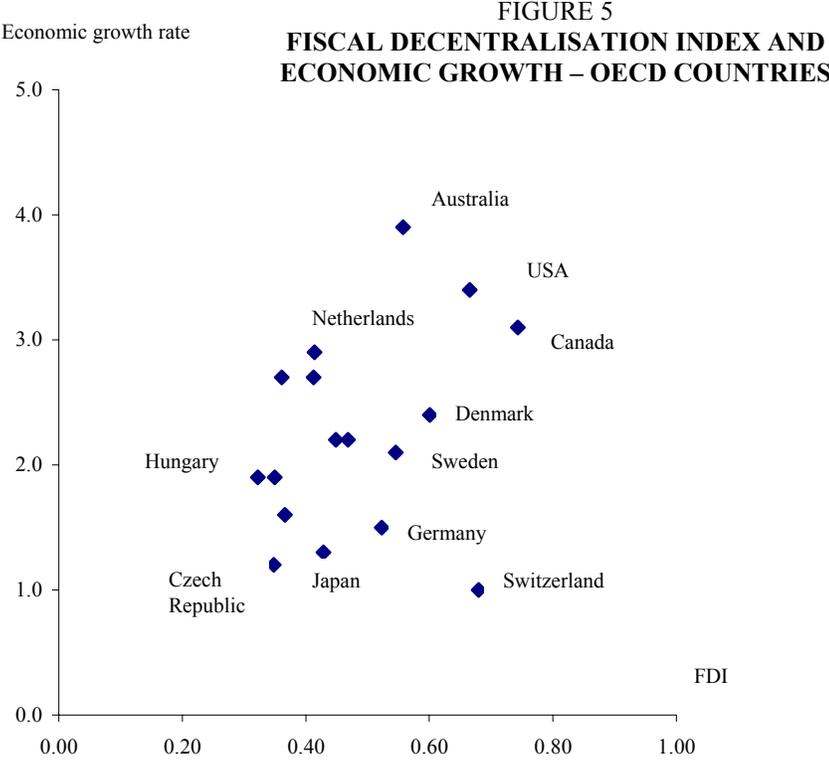
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There are, of course, many factors that contribute to economic growth and fiscal decentralisation (the fiscal arrangement between the national and subnational governments) will only be one of them. Nevertheless, it is still expected that there is a direct link between fiscal decentralisation and economic growth which will be further explored in the future. A description of this relationship is evident from Figure 4, which combines the FDIs and the average annual growth rates for selected countries from OECD and ASEAN for the period from 1990 to 2001 (from the World Development Indicators of The World Bank).

**FIGURE 4  
FISCAL DECENTRALISATION INDEX AND  
ECONOMIC GROWTH**



For a more accurate view, the groups of countries of OECD and ASEAN as represented for developed and developing countries, respectively, are considered in Figures 5 and 6.



At this stage, when two groups of countries are separately considered, from Figures 5 and 6, fiscal decentralisation is positively correlated with economic growth. That is: (i) for developed OECD economies, countries with more fiscal decentralised arrangement have generally experienced higher economic growth rates for the period (such as Australia, Canada and The US); and (ii) for developing ASEAN economies, the same conclusion is evident (such as Vietnam and Malaysia).

## **VII. Concluding remarks**

The FDI's developed in section IV reflect the expected various degrees of fiscal decentralisation between unitary and federal countries, and between developed and developing economies. It is clear that the degree of fiscal decentralisation in federal countries is generally higher than that of unitary countries since their SNGs' responsibilities and powers are often assured by their constitutions (this guarantee cannot basically be found in the constitutions of unitary countries). Also, with developed countries, their subnational governments are more advanced in terms of managerial capability and experience in comparison with developing countries. As a result, fiscal decentralisation is expected to occur at a larger extent in these developed countries.

Vietnam has a low FDI, even though the fiscal importance of SNGs is the highest of ASEAN countries. This is because SNGs in Vietnam have the lowest degree of fiscal autonomy of all ASEAN economies. However, further research, using the FDI's developed in this paper (which, unlike other indices, account for both fiscal autonomy and fiscal importance of SNGs), is required to confirm the positive link between fiscal decentralisation and growth. If confirmed, Vietnam should be encouraged to haste its fiscal decentralisation reform program, particularly by giving more autonomy to its SNGs.

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