



Ministry of Planning & Budget



Fiscal Reform Efforts of Korea

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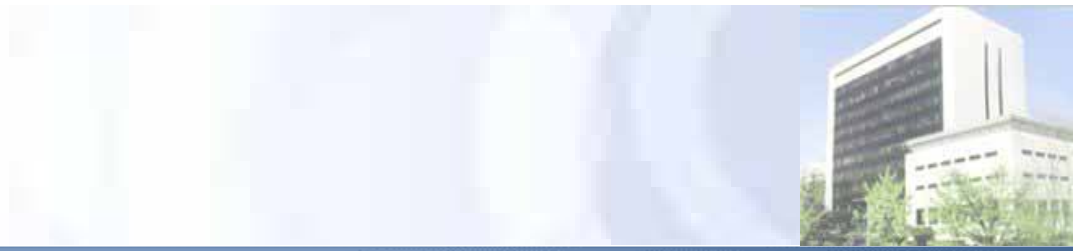
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Background



- **Based on fiscal soundness, public finance played an active role in overcoming the financial crisis**
 - In this process, national debt has more than doubled
 - However, fiscal situation remains comparatively better than other OECD countries

<Korea's National Debt>

	1997	2000	2001	2002	2003
National Debt (in trillion won)	60	111	122	134	166
% of GDP	12.3	19.2	19.6	19.5	23.0

<General Government Debt in OECD Countries>

	Korea	USA	Japan	OECD
General Government Debt ('03, % of GDP)	23.0	62.8	157.3	76.0

Changes in the Fiscal Management Environment



■ Socioeconomic changes

– Population ageing and low fertility rate

- % of the population over 65: 7.2 (2000) → 14.4(2019)
- Total fertility rate: 6.0(1961) → 2.1(1982) → 1.17(2002)

<Total fertility rate in OECD countries(2002)>

<i>Korea</i>	<i>Japan</i>	<i>USA</i>	<i>New Zealand</i>	<i>OECD</i>
1.17	1.32	2.01	1.90	1.6

– Rising demand for a better quality of life

- Focus on social welfare, education, culture, environment

– Possible slowdown in economic growth engines

- Input driven → productivity-driven economy

– Increased demand for participation and fiscal transparency



Changes in the Fiscal Management Environment



■ Public expenditure management will face future challenges

– Increase rate of tax revenues will drop

<Increase rate of national tax revenues(yearly average)>

1980~1990	1991~1997	1998~2003	2004~2008(Proj.)
17.0%	14.7%	8.6%	About 8%

– Spending requirements are continuously increasing

- Support for the aged / disabled / low-income bracket, childcare, medical services, unemployment countermeasures,
- Promoting regional economies, balanced national development, new growth driving factors

– Fiscal risk factors such as public pension scheme and unification-related costs



Identifying Weaknesses



Yearly Budgeting

- Lacks uniformity in fiscal investment
- Weak countercyclical function

Central Fiscal Authority-led

- Difficulty in overall policy assessment from reviewing individual programs (6,000+)
- Insufficient role of line ministries

Input-oriented

- Not enough attention on results
- Ex-ante control

Dispersed Fiscal Information

- Difficulty in gathering overall fiscal information
- Difficulty in supporting decision making process



Key Fiscal Reform Initiatives



■ **The new fiscal management system in Korea**

Yearly Budgeting

National Fiscal Management Plan

**Central Fiscal
Authority-led**

Top-down Budgeting

Input-oriented

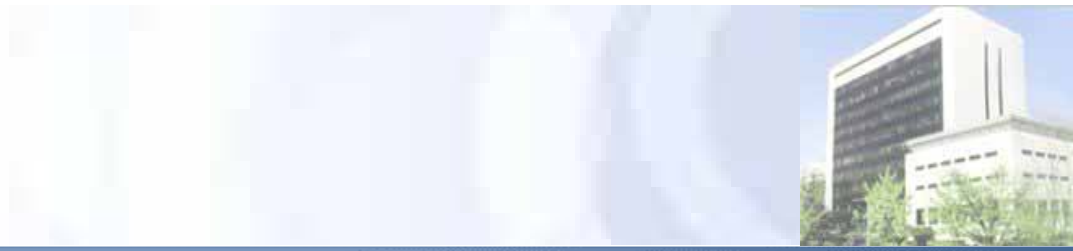
Performance Management System

**Dispersed
Fiscal Information**

**Digital Budget and
Accounting System**



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Reforming the Fiscal Management System



National Fiscal Management Plan



- **5-year plan to present national policy visions and directions**
 - Fiscal management from a medium-term perspective
 - National development visions into sectoral investment plans

- **Main contents**
 - Total expenditure ceiling
 - Sectoral and ministerial resource allocation plans
 - National policy directions
 - Medium-term fiscal management outlook

- **The NFMP will be revised every year and serve as a guideline for budget formulation**



National Fiscal Management Plan



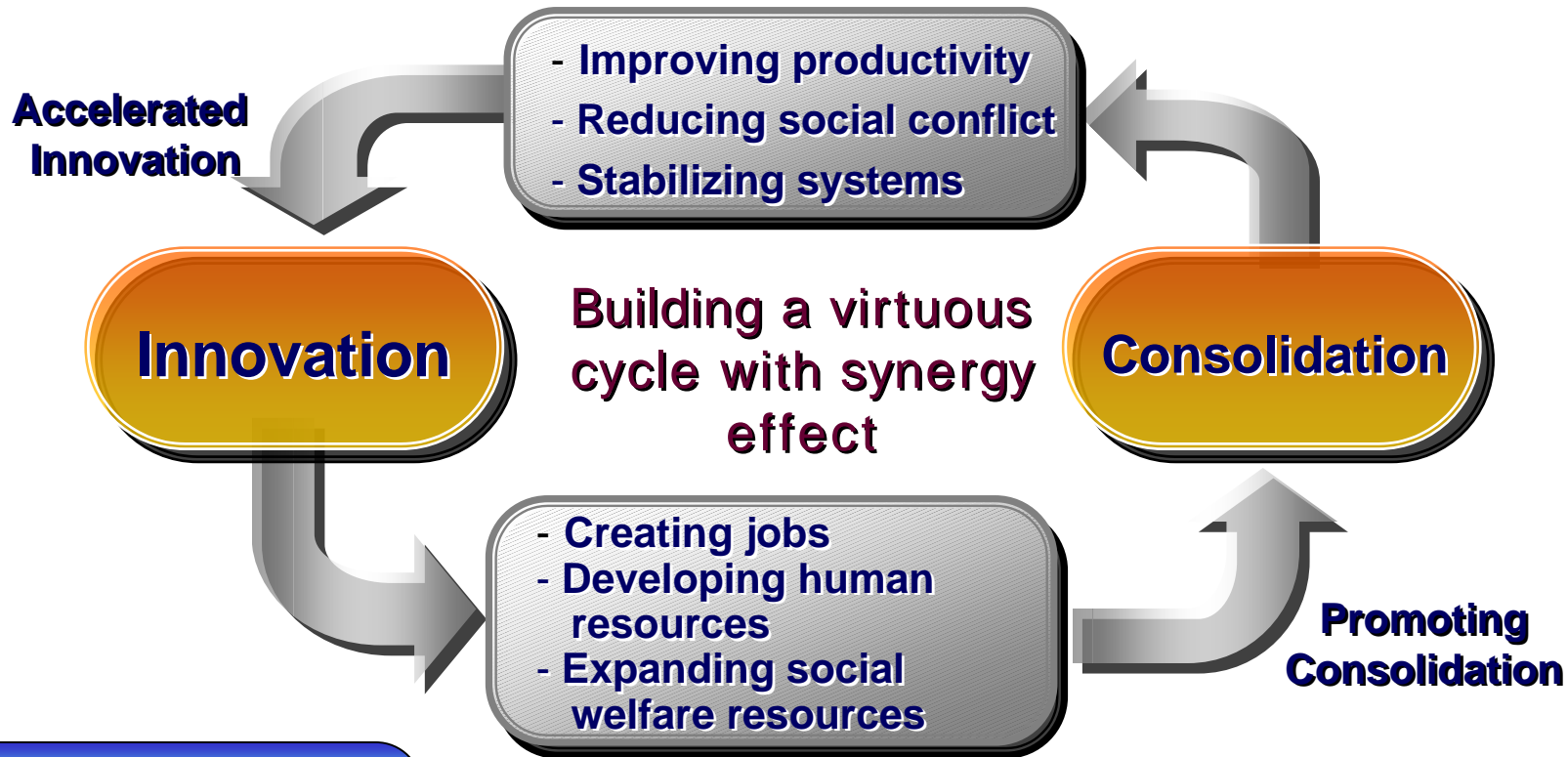
■ **Establishment process in 2004**

- Discussion between cabinet members (Jun. 2004)
- Finalization of the Plan at the Cabinet meeting (Sept. 2004)
- Submission to the National Assembly (Oct. 2004)

■ **Establishment plan in 2005**

- After the FY 2005 budget is passed at the National Assembly, the process of establishing the '05~'09 Plan will begin
- In April 2005, aggregate ceiling for FY 2006 will be set

NFMP '04 ~ '08 (National Vision)



Strategic Tasks

1. Technological innovation
2. Northeast Asian Economic Hub
3. Market reform
4. Balanced National Development
5. Stable management-labor relations
6. Political, administrative, social reform
7. Stable livelihood and expanded welfare



NFMP '04 ~ '08 (Main Contents)



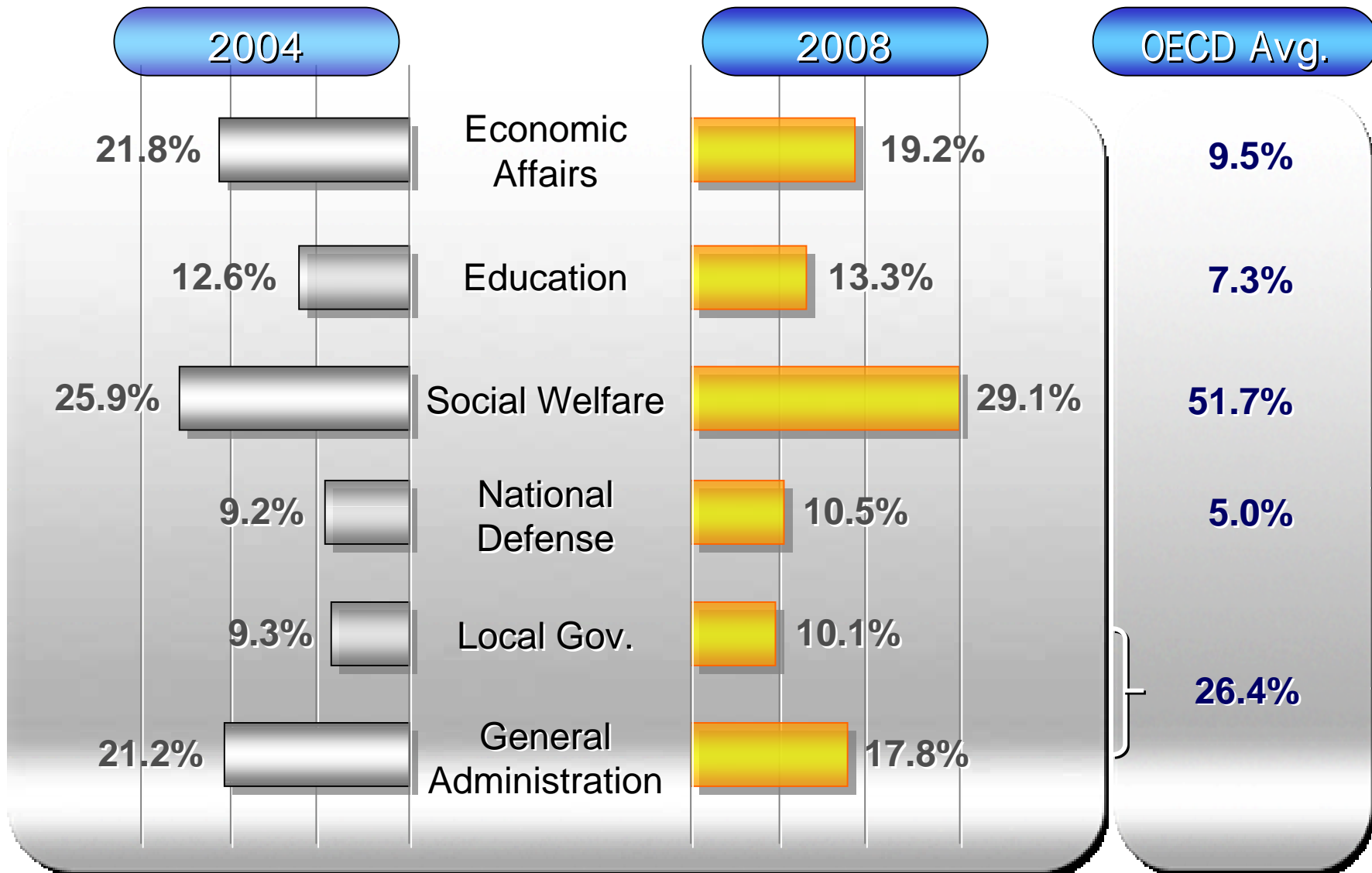
- **Total revenues are projected to increase at an average of 7.4% per year (national tax: 8.3%)**
 - Tax burden ration will remain at its current 20% level, national burden ratio will rise to record 25~26%

- **Budget deficit will drop beginning in 2005(1% of GDP), restoring a balanced level in 2008**
 - National debt will be managed to remain below its level in 2006(29.8% of GDP)

- **Total expenditures will increase at an average of 6.3% per year (general account: 7.4%)**
 - Spending will be focused on expanding economic growth potential, securing basic livelihood of the citizens, and national defense



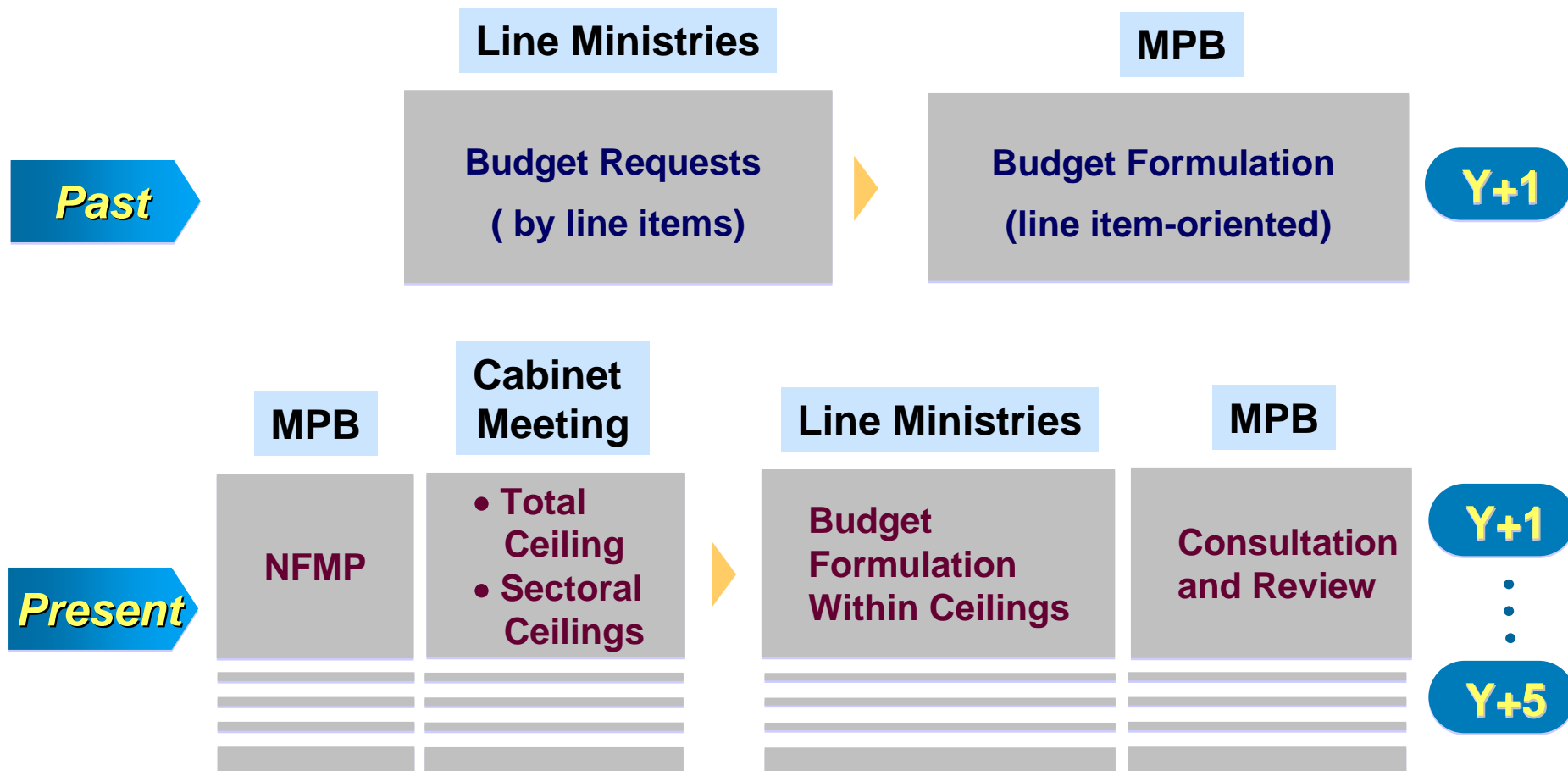
NFMP '04 ~ '08 (Resource Allocation)



Top-down Budgeting System



- A new strategic resource allocation method





Top-down Budgeting System (in 2004)



- **Top-down budgeting introduced to all 48 ministries**
- **Ministerial spending ceilings were set based on the National Fiscal Management Plan(tentative) '04~'08**
- **Line Ministries autonomously formulated their respective budgets and submitted budget requests**
 - **37 ministries: followed spending ceilings**
 - **11 ministries: broadly met ceilings or slightly surpassed them due to inevitable spending requirements**
- **MPB formulated the budget proposal through consultation with line ministries, in accordance with spending priorities of the NFMP**



Top-down Budgeting System (in 2004)



- **No more excessive budget requests**
 - Increase rate of budget requests in the general account dropped significantly: 30.8%('04) → 11.7%('05)
- **Autonomous restructuring of spending at line ministries**
 - Restructuring of multi-year programs and introduction of new programs have nearly doubled

<Comparison of FY 2004 and FY 2005 budget requests>

		'04 Budget	'05 Budget	Change
Restructuring multi-year programs	Programs	308	416	134
	Amount (trillion won)	-1.6	-2.7	-1.1
Introduction of new programs	Programs	351	459	108
	Amount (trillion won)	1.5	3.0	1.5



Top-down Budgeting System (in 2004)



- **However, there are areas for improvement**
 - **Consensus and understanding on the top-down system**
 - **Ex-ante consultations with line ministries when setting spending ceilings**
 - **Further expansion of autonomy at line ministries**
 - **Insufficient preparation and guidelines**

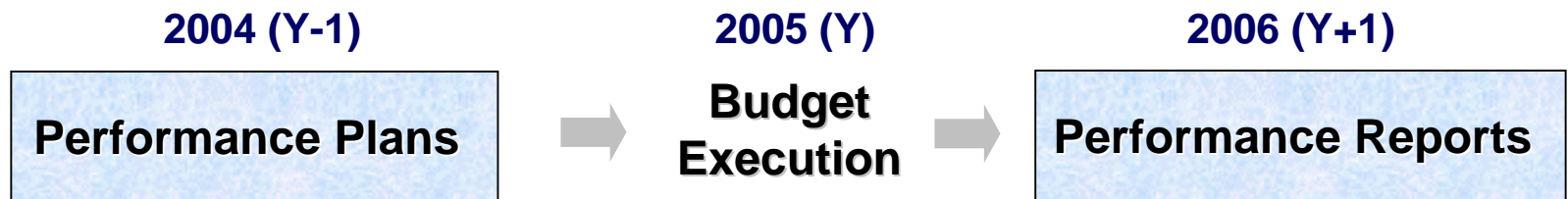
- **Future plans**
 - **Surveys and consultations with line ministries**
 - **Sectoral and ministerial spending ceilings set after sufficient discussions**
 - **Active restructuring of programs based on performance**
 - **Detailed budget formulation guidelines**



Performance Management System



- **Objective evaluation of performance to enhance accountability and transparency**
- **Line ministries set performance indicators and goals**
➔ **Yearly evaluation of performance**



- **Program effectiveness and implementation problems will be evaluated and the results will be reflected in budget formulation**



Performance Management System



- **This year, 22 ministries have submitted performance plans, with some being reflected in budgeting**
 - FY 2005 budget was adjusted comparing performance plans and fiscal spending plans
 - Excessively low performance indicators have been readjusted

- **Performance indicators have been developed during the past year and improvements are needed**
 - Training on developing performance indicators
 - Systematic management of statistics

- **Performance goals and indicators are not enough**
 - In-depth evaluations for key programs
 - Possibility of introducing program assessment systems



Performance Management System (example)



■ Ministry of Environment

- Goal: Blue sky, clean air
- Objective: air quality improvement
- Programs

	'04	'05	'06	'07	'08
• LNG vehicles (billion won)	63.5	57.7	117.8	130.9	90.0
• Measures to improve air quality in the Seoul Metropolitan Area(billion won) -		15.9	25.0	40.8	81.6
• Expanding automobile certification testing equipment(billion won)	2.6	9.4	6.8	7.2	7.4

– Key indicators

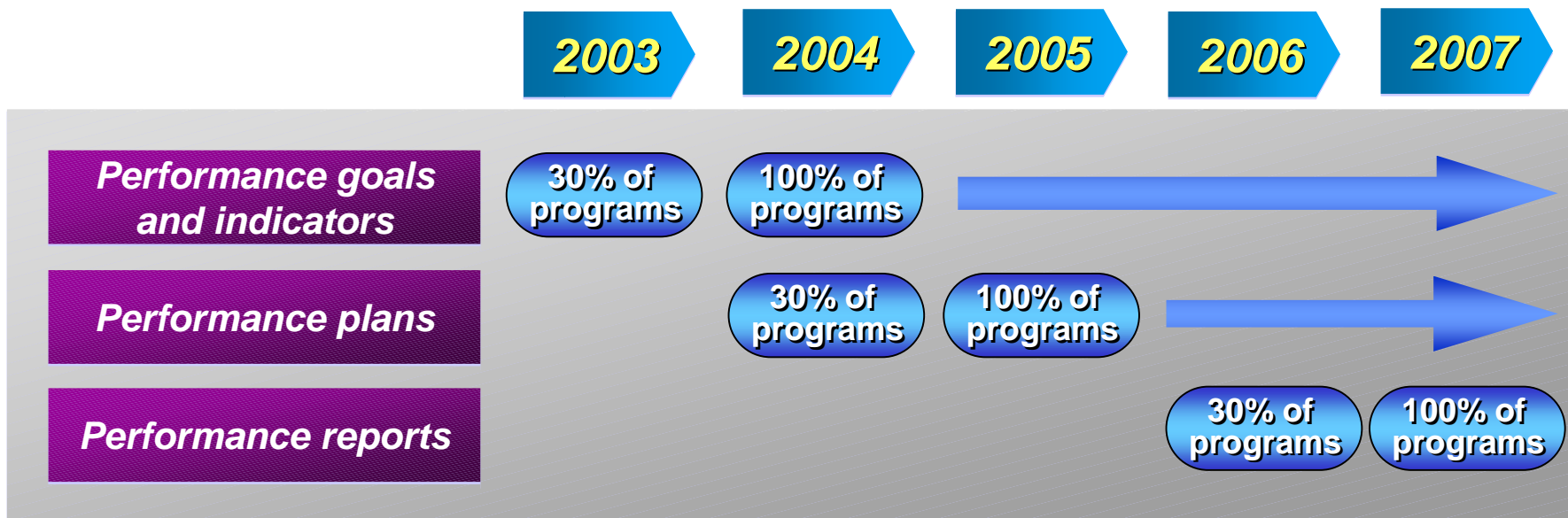
• NO ₂ emission(μg/m ³)	34	33	31	30	29
• PM ₁₀ emission (μg/m ³)	70	68	65	60	55



Performance Management System



Implementation schedule (22 ministries)



Note: for other ministries, the same schedule will apply with a delay of one year

→ Performance reports for all programs will be prepared in 2008



Performance Management System



- **In the future, evaluation of individual programs will be systematically implemented to strengthen the linkage between performance and budget formulation**
 - **Advanced countries are undertaking program assessments in addition to the management of performance goals and indicators (ex: PART)**
 - **12 in 2003, and 8 programs in 2004 have been selected as programs for individual assessment**
 - **A basic plan will be prepared by next year and will be implemented during the first half of next year**



Digital Budget and Accounting System



- **Establishment of the Budget and Accounting Reinvention Office (May 2004)**
 - **MPB, MOFE, MOGAHA, BAI**
- **Setting implementation tasks and directions(Jul. 2004)**
 - **Reform of the budget structure and system**
 - **Reform of the accounting system**
 - **Integrated fiscal information system**
- **Reform measures will be introduced according to yearly plans with the objective operating the system by 2007**
 - **A master plan for introducing the system will be completed this year**
 - **The system will be established by 2006**



Digital Budget and Accounting System (Implementation Tasks)



- **Redefining the scope of public finance**
 - Gradually expand the scope until 2005
 - Preparation of new fiscal indicators
- **Program-oriented and simplified budget structure**
 - Systematic linkage between policy, organization and program
 - Simplification of budget structure
- **Introduction of accrual accounting**
 - Early-warning system of fiscal risks
 - Supporting performance management
- **Integrated fiscal information system**
 - Real time analysis and projection capacity
 - Supporting policy formulation and decision making



National Fiscal Act



- **The current Budget and Accounts Act has maintained the basic framework since its enactment in 1961**
 - There are limits in effectively supporting the fiscal reform initiatives of the Korean government

- **The National Fiscal Act will serve as a legal framework for public expenditure management, supporting fiscal reform initiatives**
 - In October, 2004, the National Fiscal Bill was finalized at the cabinet meeting, and submitted to the National Assembly



National Fiscal Act (Contents and expected effects)



Advanced PEMS

Enhanced Efficiency

**Expanding
innovation,
autonomy and
performance**

NFMP

**Top-down budgeting
Performance
management
Strengthened counter-
cyclical function of
public finance**

Fiscal Soundness

**National debt
management and
sustainable fiscal
soundness**

**National debt
management plan
Ex-ante consultation for
laws accompanying
spending
Detailed conditions for
supplementary budget
Extra revenue for debt
repayment**

Fiscal Transparency

**Promoting
participation,
transparency and
outside input**

**Early budget account
settlement
Citizens' oversight for
illegal spending
Increased public
announcement of fiscal
information
Consultation bodies**

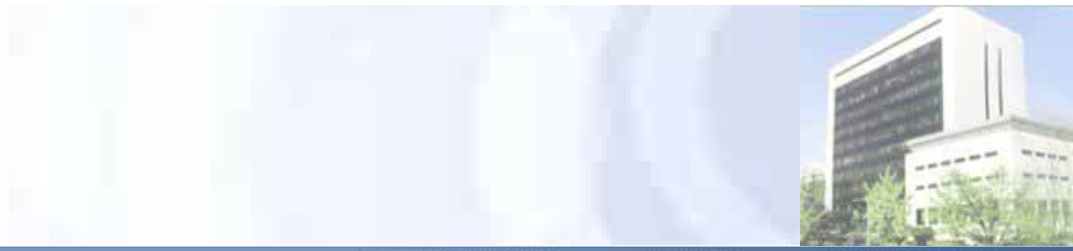


Summary (Innovating PEMS)





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Thank You