Performance Budgeting in Korea: Overview and Lessons

Nowook Park
Center for Performance Evaluation and Management
Korea Institute of Public Finance
Contents

- Country Background
- Overview of Performance Management System in Korea
- Performance Management of Budgetary Programs
- Impact of Performance Budgeting
- Lessons
COUNTRY BACKGROUND

Geography, population, political system, & government structure
Map of South Korea
• Located on the Korean peninsula in North-East Asia
• 44.6% of the peninsula belongs to South Korea
  • Total land area of the peninsula is 223,170 km²
  • The size of S. Korea is about the size of Portugal or Hungary
• 70% of land are uplands and mountains
• Population of South Korea is about 50 million
  • Combined population of the Koreans is about 73 million
• Aging population
  • Ratio of people older than 65: 5.1%(1990) → 7.2%(2000)
    → 12.2%(2013) → 15.7%(2020) → 24.3%(2030) → 37.4%(2050)
* Aging society: 7-14%, Aged society: greater than 14%
• **Political system**
  • Presidential system with 5-year single term
  • Unicameral legislature
  • Direct vote for president, national assembly men/women, governor of local governments, local assembly men/women

• **Government Structure**
  • Three independent branches of government
    • Executive, Judiciary, Legislative branch
  • 45 central executive offices
    • Supreme audit office, prime minister’s office, 6 committees, 17 ministries, 20 agencies (small ministries & sub-ministries)
  • 8 special-cities and 9 provinces

---

**Political System & Government Structure**
OVERVIEW OF PERFORMANCE MANAGEMENT SYSTEM

System within the executive branch M&E by the NAO and the legislature
• Monitoring system has been in place since 1961
  • Corresponding to the economic development plan
  • Focused on input and process monitoring
• Monitoring focus has moved from process to output/outcome over time
• M&E has been reinforced by the public financial management reforms in mid 2000s
  • Explicit introduction of outcome-oriented M&E
  • Explicit Integration into budget process
• The Asian financial crisis in 1997/1998, aging population, and a political need provided a momentum for the reform.

History of M&E System in Korea
• Prime minister’s Office
  • Overall policy monitoring and in-depth examination of some policy issues
  • Trying to consolidate all the M&E activities in the government → “the Government Policy Evaluation Framework Act”

• Ministry of Strategy and Finance (MoSF)
  • Developed Monitoring, Review and Evaluation systems of budgetary programs with the PFM reforms in mid-2000s
  • Evaluates managerial performance of public entities including state enterprises and quasi-government entities

• Ministry of Security and Public Administration (MoSPA)
  • Reviews financial management of local governments

• Line ministries
  • Perform their own monitoring and evaluation

M & E in the executive branch
• M&E capacity in the executive branch is typically supplemented by the public research institutes and external experts
  • Although the relevant central ministry provides key inputs into evaluation process, most evaluation activities are conducted by the public research institutes or evaluation committees consisting of experts.
• Some line ministries have their own evaluation unit, but many of them rely on the public research institutes and experts

M&E capacity in the executive branch
### Korean Government M&E System

<table>
<thead>
<tr>
<th>Local Governments</th>
<th>Central Government</th>
<th>Public Entities</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Self-Assessment</strong></td>
<td>- Comprehensive Assessment of line ministries/agencies’ policies</td>
<td>- Performance Evaluation of Public Entities including state enterprises, quasi-government entities, and other public entities</td>
</tr>
<tr>
<td><strong>Assessment by Central government</strong></td>
<td>- PM Office: focused on policies</td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Ministry of Strategy and Finance: focused on budgetary programs</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Assessment of Selective Policies</td>
<td></td>
</tr>
<tr>
<td></td>
<td>① Key Policies</td>
<td></td>
</tr>
<tr>
<td></td>
<td>② Job Creation Policy</td>
<td></td>
</tr>
<tr>
<td></td>
<td>③ Low-income Family Policy</td>
<td></td>
</tr>
<tr>
<td></td>
<td>④ Green Growth Policy</td>
<td></td>
</tr>
<tr>
<td></td>
<td>⑤ Policy Management Capacity</td>
<td></td>
</tr>
<tr>
<td></td>
<td>⑥ Regulatory Reform</td>
<td></td>
</tr>
<tr>
<td></td>
<td>⑦ Public Relation Management</td>
<td></td>
</tr>
<tr>
<td></td>
<td>⑧ Citizens’ Satisfaction</td>
<td></td>
</tr>
</tbody>
</table>
• The National Audit Office
  • Quasi-independent office within the executive branch
  • Traditional audit
  • Performance audit
  • Examination of annual performance report from the central government
• The National Assembly Budget Office
  • Examination of annual performance plan/report from the central government
  • Its own evaluation of budgetary programs
  • Expresses its own opinion on the M&E systems of budgetary programs

M & E in the NAO & Legislature
PERFORMANCE MANAGEMENT OF BUDGETARY PROGRAMS

Background & Overview
- There had not been any major reform in PFM area since the Budget and Accounts Act in 1961, which is based on line-item budget classification.
  - Focused on resource mobilization to meet the given policy priority rather than on developing policy priority based on monitoring & evaluation
- After the Asian Financial Crisis in the late 1990s, the need for PFM reforms became evident.
  - Increasing government debt
  - Aging population
  - Increasing demand for social welfare

Need to overhaul PFM system
Aspiration for reforms within the central budget office

• Need for longer term perspectives in budget process
• Need for enhancing feedback mechanism
• Need for improving transparency and efficiency

Support from civil society

• In particular, strong support from academics and expert groups

Political need of the new government

• Need for shifting resource allocation to the new policy areas
• Need for more participatory budget process

Demand for reform
PFM reform programs in Korea
Sequence of PFM reforms
• Big bang approach with PFM reforms since 2003
  • Medium term fiscal plan (2003*, 2005**)
  • Top down budgeting (2003*, 2004**)
  • Performance budgeting (2000*, 2005**)
  • Digital budget and accounting system
    • Program budgeting (2006**)
    • Accrual accounting (2009*, 2010**)
    • IT system (2007**)

(Note) *: pilot project, **: comprehensive implementation

Sequence of PFM Reforms
• Act was enacted in December, 2006
  • To provide a legal basis for public financial management reforms
• Includes articles on PB
  • Annual performance plan and report become legal requirement for line ministries/agencies
  • Program review & in-depth evaluation are stipulated
• It gave stability & continuity which tend to be a problem to PB.

Enactment of “National Finance Act”
Big bang approach

• Introducing all major components of PFM reforms within a single presidential term (5 year)
• All initiatives are pursued in a parallel manner

Practical adjustment of reform programs

• Some delays in program budget classification and accrual accounting

Executive branch initiated reforms

• Almost no engagement of the legislature

Characteristics of Korean PFM reforms
Performance Budgeting (Pilot Project)
Developed Strategic Objectives, Performance Goals
Performance Indicators

Performance Goal Management System (PGMS)
Expanded PBB to all ministries and agencies
Annual performance plan and report are required

Budgetary Program Assessment (BPA)
1/3 of major budgetary programs are evaluated every year
Designed after the US PART (Program Assessment Rating Tool)

In-Depth Evaluation
Selected programs are subject to evaluation
About 10 cross-cutting programs are selected every year

Performance Information (PI) Board & BPA
Reviews all budgetary programs through PI Board
BPA reflects the results of PI Board

History of PB in Korea

2000 ~ 2002

2003 ~

2005 ~

2005 ~ 2012

2014
3 Layers of PB system

Monitoring
- Annual performance plan & report
- Performance indicators & targets

Periodic Review
- Assessing 1/3 of spending programs
- Checklist-based review

In-depth Evaluation
- Evaluating 10 cross-cutting programs
- Data-driven program evaluation
Framework of PB in Korea

PGMS

Annual Performance Plan (Oct. of the Year t-1)
- Annual Performance Report (May of the Year t+1)

BPA

Annual Review for 1/3 of Projects
- 5-Level Evaluation
- Mar. –May of the Year t+1

In-Depth Evaluation

Selection of about 10 Cases
- Recommendations
- Participation of Experts

FY (t+2) Budget
From Jul. to Sep.
• Every line ministries are required to submit annual performance plan & report to the National Assembly
• Annual performance plan & report include the hierarchical structure of policy goals, which is based on program budget classification
• Performance indicators and targets are developed each year by line ministries and examined by the Ministry of Strategy and Finance (MOSF)
• Annual performance report is examined by the National Audit Office
• Annual performance plan is a starting point for PB
Relation between Annual Performance Plan and Budget Structure
• 1/3 of sub-programs are reviewed each year by MOSF and Finance with support from the Korea Institute of Public Finance.
• Line ministries are required to submit their self-assessment based on the checklist developed by the MOSF.
• Then MOSF reviews the self-assessment results and finalize the review results.
  • This review process takes three steps to reach final conclusion
  • ①The first review by MOSF ➔ appeal opportunity for line ministries ➔ ②the second review by MOSF ➔ appeal opportunity for line ministries ➔ ③if there is still disagreement, there will be a final face-to-face meeting among MOSF, line ministries and experts.
• Program ratings are decided by the periodic review process.
• 10% budget cuts are recommended by MOSF to line ministries for “ineffective” programs.

Periodic Review
## Review checklist

<table>
<thead>
<tr>
<th>Category</th>
<th>Criteria</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Design and Planning</strong></td>
<td>- Program purpose&lt;br&gt;- Rationale for government spending&lt;br&gt;- Duplication with other programs&lt;br&gt;- Efficiency of program design&lt;br&gt;- Relevance of performance objectives and indicators&lt;br&gt;- Relevance of performance targets</td>
</tr>
<tr>
<td><strong>Management</strong></td>
<td>- Monitoring efforts&lt;br&gt;- Obstacles of program implementation&lt;br&gt;- Implementation as planned&lt;br&gt;- Efficiency improvement or budget saving</td>
</tr>
<tr>
<td><strong>Results and accountability</strong></td>
<td>- Independent program evaluation&lt;br&gt;- Results&lt;br&gt;- Utilization of evaluation results</td>
</tr>
</tbody>
</table>
## Program Review Results

(Number of Programs, %)

<table>
<thead>
<tr>
<th>Year</th>
<th>Total</th>
<th>Effective</th>
<th>Adequate</th>
<th>Ineffective</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008</td>
<td>384 (100)</td>
<td>55 (14.4)</td>
<td>226 (58.9)</td>
<td>103 (26.8)</td>
</tr>
<tr>
<td>2009</td>
<td>440 (100)</td>
<td>36 (8.2)</td>
<td>311 (70.7)</td>
<td>93 (21.2)</td>
</tr>
<tr>
<td>2010</td>
<td>552 (100)</td>
<td>26 (4.7)</td>
<td>393 (71.2)</td>
<td>133 (24.1)</td>
</tr>
<tr>
<td>2011</td>
<td>482 (100)</td>
<td>33 (6.8)</td>
<td>317 (65.8)</td>
<td>132 (27.4)</td>
</tr>
<tr>
<td>2012</td>
<td>474 (100)</td>
<td>32 (6.8)</td>
<td>330 (69.6)</td>
<td>112 (23.6)</td>
</tr>
<tr>
<td>2013</td>
<td>597 (100)</td>
<td>29 (4.9)</td>
<td>424 (71.0)</td>
<td>114 (24.1)</td>
</tr>
</tbody>
</table>
• About 10 cross-cutting programs are evaluated each year
  • Typical program evaluation approach is adopted.
  • Program consolidation is the primary goal.
  • Evaluation is outsourced to public research institute and academics.
• Examples of in-depth evaluation
  • Job assistance programs: 55 programs by 10 ministries
  • Local development programs: 27 programs by 5 ministries

**In-depth evaluation**
• Purpose of PB
  • Emphasis on making link between performance information & budget allocation
    ➔ Going beyond performance monitoring system
    ➔ Periodic review process is developed
• Outcome-oriented PB
• Executive branch-initiated reform
  • However, its nature evolves with involvement of the National Audit Office and the National Assembly.
IMPACT OF PB
• Information from monitoring system (performance plan and report) has not been systematically utilized so far.
  • For internal use, they are useful information
  • From the viewpoint of central budget authority, they provide limited information
• Information from review system are actively used in budget negotiation process.
  • Programs rated as ineffective are in danger of suffering budget cut
  • Its use is systematically built into the budget process
• Information from program evaluation is usually useful
  • Their use in budget process depends on the quality of evaluation and the will of central budget authority
  • Recently it gained visibility by formalizing the reporting process.
## Budget Cut for Ineffective Programs

<table>
<thead>
<tr>
<th>Year</th>
<th>No. of Ineffective Programs</th>
<th>Total Budget in FY (t)</th>
<th>Total Budget for FY (t+1)</th>
<th>Budget cut (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008</td>
<td>103</td>
<td>5.7</td>
<td>4.6</td>
<td>-19.3</td>
</tr>
<tr>
<td>2009</td>
<td>93</td>
<td>2.8</td>
<td>2.6</td>
<td>-6.8</td>
</tr>
<tr>
<td>2010</td>
<td>133</td>
<td>3.9</td>
<td>3.4</td>
<td>-12.5</td>
</tr>
<tr>
<td>2011</td>
<td>132</td>
<td>4.3</td>
<td>3.9</td>
<td>-10.0</td>
</tr>
<tr>
<td>2012</td>
<td>112</td>
<td>1.9</td>
<td>1.5</td>
<td>-18.4</td>
</tr>
</tbody>
</table>
329 recommendations are produced from the in-depth evaluation between 2008 and 2012.
- 166 are finished with follow-up actions
- 144 are in progress
- 19 are delayed

Program consolidation, program design and implementation improvement, improvement of performance management

Example: Program for the improvement of energy efficiency

ESCO (Energy Service Company) program
- Government provides subsidy and tax exemption to the company renovating facilities to improve energy efficiency.
- 20% of the expense was exempt from corporate income tax.
- The problem was government subsidy was counted as expense, which means double-counting.

One of the in-depth evaluation’s recommendation was the elimination of the double-counting practice, which was implemented by the Ministry of Strategy and Finance

Use of In-depth evaluation Information 34
• Monitoring & evaluation activities become essential elements of program design and management.
  • Many big programs set up M&E system. In particular, subsidy or grant programs are implicitly required to operate M&E system.
• Performance contracts are tried in some programs to improve program performance.
  • The initial evidence shows big improvement of performance.
  • However, contract management capacity is an issue to be addressed.

Cultural changes in line ministries
• Integration of performance information into budget documents
  • Consolidation of budget document and annual performance plan and report
• Introducing Performance Information Board
  • Quarterly monitoring process
  • Quarterly milestones will be specified in the integrated financial information management system (“dBrain”)
• Improve feedback mechanism
  • Not only budget cut but also program improvement will be pursued

Recent development
• In theory, performance information should be used as **one of important factors** for budget allocation

• In practice, consider setting specific targets for budget reshuffling, in order to secure fiscal space where PI can be more directly used
  - Reshuffling 5% of budget mostly based on PI may not cause serious unintended problems

**Use targets for PB**
• Consider focusing on selective areas/programs that are important and easily subject to performance budgeting at the initial stage of reforms
  • Since producing meaningful PI for every program takes time, it can be a good strategy to start with selective areas/programs to demonstrate the impact of performance budgeting.
• Consider moving beyond performance indicators and targets, particularly if outcome indicators are used
  • Outcome indicators need interpretation to be used in decision-making purpose due to external factors
  • Therefore, consider developing program review process to have more systematic performance information, unless communication between central budget authority and line ministries are easily facilitated
• Consider using output indicators in some areas
  • If link between output and outcome is very tight, output indicator can be a good proxy for outcome
  • If quality of services can be properly controlled, output-based budgeting can be useful
  • In some areas, above mentioned condition can be met
  • Then, consider using output measures for the selected areas, such as public health, education, social welfare and so on.

Selective Use of Output Information
• Capacity building is important
  • The central budgetary authority’s evaluation capacity
  • Line ministries’ evaluation and data management capacity
  • If outside resources, such as research institutes and universities, are available, cooperate with them

• Location of evaluation unit is important
  • If evaluation unit is separated from budget office, performance information is less likely to affect the budget allocation

• Develop proper incentive scheme for line ministries
  • Flexibility of management
  • Sanctions for poor performance

Other Lessons
Contact Information

Nowook Park, PhD.
Founding Director
Center for Performance Evaluation & Management
Korea Institute of Public Finance
Email: npark@kipf.re.kr