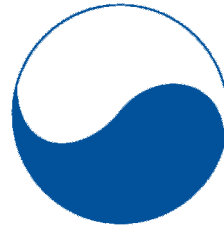

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CONTENTS

Part I: Overview and Macroeconomic Issues

Overview of the Korean Economy <i>Jeon Jong-kyu</i>	1
---	---

Part II: Financial Institutions and Markets

Korea and the IMF–World Bank Financial Sector Assessment Program <i>Meral Karasulu</i>	7
--	---

The Banking Sector <i>Thomas Byrne</i>	15
--	----

The Corporate Bond Market in Korea <i>Kim Sungmin</i>	20
---	----

Part III: Structural Reform

Public Sector Reform <i>Lee Kang-ho</i>	33
---	----

Business Perspective on Corporate Reform <i>Oh Moon-suk</i>	41
---	----

Accounting Reform <i>Lee Suk-jun</i>	48
--	----

Part IV: External Issues

U.S.-Korea Economic Relations View from Washington <i>Nan N. Fife</i>	55
View from Seoul <i>Lee Hyun-ju</i>	61

Korea-China Relations <i>Lee Chang-kyu</i>	69
--	----

Part V: North Korea's Economic Development and External Relations

Economic Reform in North Korea <i>Bernhard Seliger</i>	77
--	----

Japan-North Korea Relations <i>Mimura Mitsuhiro</i>	87
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STRUCTURAL REFORM

REFORMS AND NEW GOVERNANCE OF PUBLIC BODIES IN KOREA

by Lee Kang-ho

Background

Since 1962, the Korean government has implemented and executed a series of five-year development plans that have led Korea to spectacular economic growth. The Korean government played a major role in the Korean economy during the past three decades,¹ and the government decided to centralize its authority through the five-year development plans. Each ministry created a number of public bodies that were based on special acts that granted authority; these bodies were controlled by the discretion of each ministry. After the financial crisis in 1997, the President initiated a new focus on reforms and efficiency in the public bodies.

When the Korean government realized that the government-led growth strategy had resulted in widespread inefficiencies and bureaucracy in the public sector, the Kim Dae-jung administration between 1998 and 2002 launched intensive reform programs that covered the four major areas of Korea's economy—the corporate sector, the finance sector, labor, and the public sector. In terms of public sector reforms, the objective was “a small and efficient but better-serving government.”² Three dimensions conformed with the goal:

- **Restructuring (small government).** The government restructured the central government and local governments, downsized and contracted out portions of the public sector, and undertook deregulation reform.

- **Innovative operational system (efficient government).** The government created 23 executive agencies that operated in a businesslike manner; it adopted an open personnel system and performance-based remuneration; and it instituted a budgetary incentive system.
- **Improving service delivery to the public (better-serving government).** The government directed e-government reforms such as government for citizens (G4C) and government to business (G2B), cut down on verification paperwork, and adopted the Internet Procedure Enhancement for Civil Applications and Customer Charters, which made government document processing more transparent and convenient.

Korea has tried to build a new governance system of public bodies since the establishment of reforms in the public sector. The President submitted to the National Assembly the Basic Governance Act of Public Bodies in October of 2002, which was passed by the National Assembly on 18 December 2003. The Act marks the beginning of transferring the governance system of public bodies from a priori regulation and management to performance appraisal management.

Reform of Public Bodies

Framework

The President appointed official government organizations to lead the reforms and endowed them with

1. Lee, Kang-ho, “A Study of the Korean Economic Crisis: Causes and Recovery Policies,” *Quarterly Journal of Ashwattha* (India) 13, no. 1 (January–March 2003): 12–3.

2. “How Korea Reformed the Public Sector” (Seoul: Ministry of Planning and Budget, 2003), 3–20, www.mpb.go.kr/attach/morgue/bbs1/2002public_sector.pdf.

the legal authority to implement efficiently the governmental reform in the public sector. Examples of government organizations implementing public sector reforms are the Planning and Budget Commission (PBC) with the Government Reform Office, and the Commission on Government Reform (CGR) in 1998. The PBC was transferred to the Ministry of Planning and Budget (MPB) in 1999, and the CGR was transferred to the Presidential Commission on Government Innovation (PCGI) in 2000.

The strategy of public sector reforms was to implement top-down reforms such as privatization, deregulation, downsizing, and outsourcing through the PBC and the CGR from 1998 to 2000, and to implement bottom-up reform through the MPB and the PCGI after 2001. These organizations were in charge of governmental reforms and reforms of the public bodies.

The public sector is divided into two parts, the government and the public bodies, as shown in *Table 1*. The government is defined as ministries and agencies based on public laws; civil servants are engaged in these ministries and agencies. Agencies were created since 2000 as part of the downsizing of government; 23 agencies were created. In 2003, certain public bodies were classified as organizations with public tasks based on private laws. Certain other public bodies (the subject of this paper) are based on public laws; these include state-owned enterprises (SOEs), research institutes, major public bodies, and other public bodies.

Management Reforms in the Public Bodies

Reforming the public bodies was categorized as one of the major areas of public sector reform and one of

the four necessary reform areas defined by President Kim Dae-jung in his effort to overcome the financial crisis in 1998. Reform of the public bodies can be divided into two steps.³ The first step was initiated by the MPB and was carried out between 1998 and 2000; it focused on downsizing employees and structures, privatization, and selling non-necessary assets. The second step approached reforms from the bottom up, and since 2001 it has encouraged the public bodies to create reform plans voluntarily. This step entailed an MPB- and PCGI-led appraisal system for evaluating the performance of self-innovation projects every year.

The first step of the reforms caused the dismissal of approximately 60,000 employees, or about 25 percent of the total number of employees of the public bodies, and contracted out 209 organizations from 1998 to 2000. The Government Reform Office of the PBC played a major role in the first step. The office sought new areas to reform, implemented measures to achieve the objectives, and led each public body to implement the reform plans through parent ministries of the public bodies. Although the first step of the reform achieved some of its objectives, there were several problems such as mismatching plans and bogus reforms. Thus, the government changed the pattern of the reforms from a top-down approach to a bottom-up approach, and at the end of 2000 a special appraisal team made up of private professionals began to evaluate the performance of the self-innovation plans.

At the second step of the reform, the public bodies that were evaluated were selected on the basis of the size of the government grant or subsidy that the body received. Every year the MPB issued guidelines for innovation of the system of public bodies. For 2003,

Table 1: Classification of Government Organizations in Korea

Public law					Private law	
Ministry	Agency	SOE	Research institute	Major public body	Organization with public task	Organization without public task
Government		Public body			Private sector	

Source: Summary of a survey by the Ministry of Planning and Budget, 2003.

3. "White Paper on Public Sector Reform in Korea" (Seoul: MPB, 2002), 168–75.

the most important guidelines were the rationalization of structures and personnel management, appropriate uses of budget, efficiency of management, customer-oriented service, and a performance-based system. Every year every public body must present its plan of self-innovation, based on a guideline that normally includes 10–15 projects for innovation. The total number of projects evaluated was 1,943 in 2000; 1,906 in 2001; 2,881 in 2002; and 2,311 in 2003. The special appraisal team coordinated by the MPB evaluates the plan.

The MPB announces the appraisal results to the public and assesses the results as incentives and differentials in formulating and allocating the budget. This leads the public bodies to accelerate the implementation of system innovation.

The Basic Governance Act of Public Bodies that was enacted in December 2003 mandates that appraisals will be integrated into new governance systems for public bodies.

Privatization of SOEs

SOEs since 1962 have been Korea's primary means of delivering required social infrastructure such as electricity, steel, roads, and telecommunication networks, which were necessary given Korea's early stage of the economic development. The SOEs played a major role in achieving the government's objectives during the growth era.

The increasing number of the SOEs created a number of problems—e.g., profligate management resulting from a lack of sense of ownership, inefficiency, operational problems of weak managerial autonomy as a result of excessive outside intervention and rigid regulations, and a distortion of national resource allocation. The financial crisis in 1997 was an important factor that led the Korean government to move toward privatization of the SOEs. Goals of privatization included:

- Raise national competitiveness by reducing the role of the public sector in the economy;

- Introduce the autonomy and creativity present in the private sector to the public sector, with the goal of upgrading the quality of services and allocating resources efficiently;
- Obtain funds by privatizing the SOEs in response to fiscal deficits caused by the financial crisis; and
- Encourage the active participation of foreign investors in privatization.⁴

To the Korean government, reform of the privatization policy was an important part of public sector reform instituted to overcome the financial crisis in 1997. The government launched its privatization program with an understanding that transferring ownership to the private sector would be a fundamental solution to the inefficiency of the SOEs. The government established the Privatization Steering Committee (PSC) under the PBC (later the MPB), which was active from 1998 to 2002, to achieve the goals of privatization. The PSC's mandate was general coordination of the privatization program, monitoring progress, and the authority of the final decision making regarding privatization policies. The head of the committee was the minister of the PBC, and the committee consisted of 10 relevant vice ministers and 2 civilians.

The Korean government also announced three principles of its privatization

- The SOEs that were engaged primarily in commercial business would be privatized immediately; the SOEs that by their nature were unsuitable for immediate privatization would follow a strategy of phasing in privatization in stages as they restructured themselves;
- The government decided to maximize the move toward privatization by pursuing multiple means of privatization and by flexibly adjusting the timing; and
- Shares of SOEs would be offered to both the general public and SOE employees in order to maxi-

4. "How Korea Reformed the Public Sector," 57–68.

mize participation by both groups in the process of making SOEs belong to the citizens.

As the result of privatization from 1998 to 2002, the government completed the privatization of eight parent SOEs—POSCO, Korea Telecom Corporation, Korea Tobacco and Ginseng Corporation, Korea Heavy Industry Company, Korea Chemical Company, KTB, Government Textbook Company, and DOPCO. Therefore, the number of parent SOEs was reduced from 26 in 1998 to 19 in 2002.⁵ The number of subsidiary SOEs was also reduced—from 82 to 16. Therefore, the total number of SOEs decreased from 108 in 1998 to 35 in 2002. The number of employees decreased from 212,000 in 1998 to 81,000; in other words, 131,000 employees were dismissed. The revenue generated by privatization during that time was 24.3 trillion *won* (23 percent of the 2002 general account in the budget). This accelerated the process of overcoming the financial crisis in 1997, which was reflected in the upgrade of Korea's sovereign credit rating by Moody's from C++ to A.⁶

Deregulation of Government

As the Korean government was working to achieve economic development during the past three decades, it instituted a number of regulations affecting the public sector and the private sector and created a number of regulatory bodies that oversaw certification, registration, or policy guidance needed to implement regulations. Although the President has reformed the government toward better administration, bureaucratic burdens on the public sector still exist because many governmental missions (such as road safety) were consigned to public bodies.

Regulations are required to protect employees at work, consumers, and the environment, but it is important

to maintain the right balance to avoid imposing unnecessary burdens on businesses. After the financial crisis in 1997, the Korean government undertook substantial deregulation to improve the competitiveness and creativity of businesses and the private sector in general. The framework act of public regulation was enacted in 1998, and the Presidential Regulatory Reform Committee began meeting at the same time to accelerate systemic regulatory reforms.

The Regulatory Reform Committee has played two main roles: reduction of current regulations and review of new regulations. The Regulatory Reform Committee that reviewed the central government surveyed all the regulations in 1998—a total of 11,125—and crafted a plan for reducing the number by half. The plan was approved at a Cabinet meeting that was led by the President. In 1998, the Regulatory Reform Committee reviewed all regulations regarding international standards and effectiveness, and it eliminated 5,430 regulations (48.8 percent) and amended 2,411 regulations (21.7 percent).⁷ It was an epochal period of deregulation. Resistance from ministers and interest groups was significant, but President Kim Dae-jung prevailed with the strength of his convictions to carry out deregulation. In 1999, the Regulatory Reform Committee reviewed the remaining regulations and abolished 503 regulations and liberalized 570.

The Regulatory Reform Committee also reviewed new regulations according to the Framework Act of Regulation. When ministers want to create any act or decree, they must assess the regulatory impact of the changes, listen to interest groups, and then receive a review of the proposed regulations from the Regulatory Reform Committee. The Regulatory Reform Committee reviewed 3,621 such new regulations that were included in 1,050 new acts from 1998 to 2001. This brought about liberalizations in 902 regulations,

5. Because one parent SOE was created and eight SOEs were privatized during that time, the total number of SOEs is 19.

6. "White Paper on Public Sector Reform in Korea," 82–140.

7. The author was in charge of deregulation in the Office of the President when he served as an Assistant Secretary to the President for Policy and Planning from 1998 to 2001. When this office reported the first draft of deregulation plan to the President—which was less than half of the target goal—the President ordered each minister to augment the deregulation plan. The Senior Secretary to the President met the minister and senior officials in each ministry to accelerate the deregulation plan in order to meet the target goal: reduce regulations by half. Finally, a reformulated deregulation plan that reduced the total number of regulations by 48.8 percent was reported to the President and was approved in a Cabinet meeting in 1998.

the passage of 2,381 regulations in their original form, and recommendations for the withdrawal of 338 regulations.

Finally, the Framework Act of Regulation mandated that the government keep a record of regulations related to restrictions on rights or duties of citizens and also post these regulations in the form of public notices on the Internet. As a result, a total of 10,717 regulations was recorded in 1998, but by 2002 this number had been cut to 7,309. Deregulation formed the basis of the government's later moves toward downsizing, contracting out, or eliminating public bodies.

A New Governance System for Public Bodies

Basic Governance Framework

The Korean government has enacted two important pieces of legislation related to governance and management of public bodies. These are a 2003 law—Basic Governance Act of Public Bodies—that covered about 90 public bodies, and a 1998 law—Institution, Operation, and Support Act for Research Institutes—that covered 42 research institutes. These two acts have contributed to building a new governance system for public bodies (*Table 2*).

In Korea, public bodies are created by a special act, and parent ministries are responsible for their governance and management. However, the Office of the President and the MPB⁸ are also involved in the governance, budgeting, and recruiting processes of public bodies. Because the Korean government has played a centralized role in the development of the economy, the Office of the President and the MPB in the past were influential without having transparent legal authority for governance and management of public bodies. This led to parent ministries' influencing governance and management of public bodies via prior guidelines or orders under the guidance of the Presidential office and the MPB. In the past there was no need to create a transparent legal governance system.

After the financial crisis in 1997, however, the Korean government undertook reforms in the direction of transparent authority and responsibility for public bodies and for building a performance evaluation system. The two important acts—Basic Governance Act of Public Bodies and Institution, Operation, and Support Act for Research Institutes—include performance evaluation systems.

The MPB implemented reforms for public bodies between 1998 and 2000, and then it evaluated the self-innovation performances of approximately 200 public bodies that were selected from among all public

Table 2: Status of Public Bodies in Korea, 2003

Public bodies	No. of public bodies	Budget (trillion won)	Government grant/subsidy (trillion won)	No. of employees (000)	Examples
SOEs	19	56.7	3.5	51	Korea Electronic Power Corporation, KOTRA, Korea Highway Corporation
Research institutes	47	2.0	0.7	9	KDI, KIEP, KIST, Korea Reunification Institute
Other public bodies	136	78.1	11.2	86	Korea Development Bank, KOICA, National Health Insurance Corporation
Total	202	136.8	15.4	146	—

Source: Ministry of Planning and Budget, 2003.

8. The MPB originated in 1962 as the Economic Planning Board; it became part of the Ministry of Finance and Economy in 1995. In 1998 it was reconstituted as the PBC and in 1999 merged with the Office of National Budget to become the MPB.

bodies because of the size of their government grants or budget subsidies⁹ while they were consolidating legal systems. When the legal performance evaluation system has settled down, the self-innovation performance evaluation will be replaced by performance evaluation led by the Basic Governance Act of Public Bodies. The new governance system for public bodies is summarized in *Table 3*.

State-Owned Enterprises

SOEs are classified into two categories: SOEs in which the government invests more than half of the capital stock, and SOEs in which the government invests less than half of the capital stock. The first group is governed by the Framework Act of SOEs and comprises 13 SOEs, including the Korea Electric Power Corporation, Korea Agricultural and Rural Infrastructure Corporation, and Korea Minting and Security Printing Corporation. The size of the budget for these SOEs was 43 trillion *won* (about \$35 billion, 43 percent of the general account budget of Korea's central government), and the number of employees in 2002 was 44,449. The second group consists of 18 SOEs governed by each parent ministry.

The chief executives and inspectors of the 13 SOEs in which the government invests more than half the capital are appointed by the President through the parent minister and the Minister of Planning and Budget. Candidates for chief executives and inspectors are to be publicly invited to serve in these positions prior to their Presidential recommendations. Each executive board determines budgets, but the parent ministers and the Minister of Planning and Budget consult on the budgets before any budget decision is made.

The Minister of Planning and Budget conducts performance evaluations every year and reports the results to the National Assembly in June. The Minister then presents guidelines for budget formulation. The Minister of Planning and Budget forms a Committee of Performance Evaluation comprising 30–40 professionals who work in the private sector (e.g., universities). Performance evaluation results are used as criteria for performance-based remuneration and dismissal of chief executives. Therefore, the influence of the Minister of Planning and Budget is prominent. The government operational committee consists of 11 members: the Minister of Planning and Budget

Table 3: Korea's Governance System for Public Bodies

Public bodies	Act	Executive board	Governance committee	Resource and process	Recruitment of head of group	Performance evaluation
SOEs	Framework Act of SOEs; separate acts	Fewer than 15 members (3-year terms)	Depends on each act	Decided by executive board	President	Minister of Planning and Budget
Research institutes	Institution, Operation, and Support Act for Research Institutes	Fewer than 15 members (3-year terms)	5 research councils	Decided by the 5 research councils	Decided by the 5 research councils	Decided by the 5 research councils
90 major public bodies	Framework Act of Public Bodies; separate acts	Depends on each act	19 members (10 gov't, 9 private sector)	Decided by executive board under permission of parent minister	Process differs according to specific public body	Parent ministry
Other public bodies	Separate acts	Depends on each act	Depends on each act	Decided by executive board under permission of parent minister	Process differs according to specific public body	Process differs according to specific public body

9. According to a survey by the MPB at the end of 2002, the number of public bodies totals about 550.

(chair), 5 vice ministers of related ministries, and 5 private professionals. The committee resolves issues of performance evaluation and dismissal recommendations of board members. This committee is a center for the governance of SOEs.

Research Institutes

Beginning in 1960s, every ministry had several research institutes attached to it; the purpose was to acquire academic support and expertise for formulating government policies. Examples of specialized institutes include the Korea Development Institute, Korea Institute for International Economic Policy, and the Korea Institute for National Reunification. At the beginning, many distinguished professionals applied to the government-supported research institutes, but recently the institutes have lost their some of their competitiveness vis-à-vis private institutes. Parent ministries controlled the institutes in a bureaucratic manner and did not provide performance incentives.

The government therefore implemented reforms of the governance systems of government research institutes and also enacted the Institution, Operation, and Support Act for Research Institutes in 1998. Government research institutes are classified into five categories: the Korea Council of Economic and Social Research Institutes (14 institutes), the National Research Council for Humanities and Social Sciences (9), the Korea Research Council of Fundamental Science and Technology (4), the Korea Research Council for Industrial Science and Technology (7), and the Korea Research Council of Public Science and Technology (8).

Each research council is composed of 12 members: 5 governmental vice ministers and 7 members from the private sector. They are responsible for determining the budget, appointing presidents of institutes, and evaluating research performance. For overall governance of all councils and institutes, the prime minister is responsible. There are loose relationships between each institute and each former parent ministry.

Major Public Bodies¹⁰

The National Assembly on 18 December 2003 passed a very important reform act entitled Basic Governance Act of Public Bodies, which included general mechanisms for governing the public bodies. The pattern of governing public bodies is to be changed from guidance by parent ministries prior to policy decisions to performance appraisal after self-management. The principle will be “eyes on, hands off.”

The act covers major public bodies except for SOEs and research institutes; this includes approximately 88 public bodies in 2004. The law states which public bodies will be governed by the Basic Governance Act of Public Bodies, which will enter into force on 1 April 2004.

The first category is the public bodies that receive support of more than 5 billion *won* (about \$4 million) from the central government budget. This category includes, for example, the National Computerization Agency, the National Parks Authority, and the Korea Labor Welfare Corporation. The second category is the public bodies that receive more than 5 billion *won* in terms of the sum of their public budget and the revenues generated on the basis of authority of government officials or law, where the latter account for more than 50 percent of the total. The third category comprises the public bodies in which the government invests as a dominant owner. This covers about 90 public bodies that are administered by 18 parent ministers who are responsible for management.

The parent ministries are supposed to carry out a performance evaluation of their public bodies every year. Each public body must report its annual performance to the parent minister within three months after the beginning of the new fiscal year, and each parent minister evaluates the performance of its public bodies by June. Each parent minister reports the result of the performance evaluation to each standing committee of the National Assembly and the Minister of Planning and Budget. The Minister of Planning and Bud-

10. Major public bodies are public bodies that are covered by the Basic Governance Act of Public Bodies.

get is supposed to digest all the performance evaluations from all the parent ministers and submit them to the Management Committee of Public Bodies for approval. After the Management Committee of Public Bodies approves the reports of performance evaluation, the Minister of Planning and Budget has until August to report to the National Assembly. The government is preparing the evaluation procedures in 2004, and each parent ministry will begin performance appraisals in 2005.

The Management Committee of Public Bodies, chaired by the Minister of Planning and Budget, will play a major role in deciding policies related to the public bodies—general guidelines for performance appraisal, guidelines for budget management, and review of functions. The Management Committee of Public Bodies consists of 19 members: the chair, 9 vice ministers from major parent ministries, and 9 private professionals.

Other Public Bodies

There is no general governance system for remaining public bodies except for the SOEs, research institutes, and major public bodies. Each parent ministry governs the remaining public bodies according to the respective base acts. However, even if the parent ministers have no obligation to follow the Basic Governance Act of Public Bodies, parent ministers will follow the act for the remaining public bodies.

Conclusion

Korea undertook reforms and built a new public governance system of public bodies after the financial crisis of 1997. The results of reforming and building a new public governance system has resulted in some successes. The reform of public bodies was a catalyst for reforms of the corporate sector, the finance sector, and the labor sector; these reforms helped Korea to overcome the effects of the 1997 economic crisis.

In addition, enactment of the Basic Governance Act of Public Bodies was the turning point in building a new kind of public governance system of public bodies—governance moved from a priori regulation and guidance to a performance appraisal system. Further-

more, it achieves a balance between parent ministries and the MPB through the Management Committee of Public Bodies. It also builds a new performance appraisal system for public bodies, and it will indirectly affect other public bodies.

The Korean government has built a new system for the governance of public bodies, and now must establish it as the means to achieve better governance of public bodies.

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