

**Minister's Summary by Minister Ota**



**19th Meeting (July 28, 2008)**

- (1) "FY 2009 Budget Overview"
- (2) Guidelines for FY 2009 Budget Requests
- (3) Reform of special accounts of the government budget

Hiroko Ota here. Today, the Council on Economic and Fiscal Policy (CEFP) held its 19th meeting of the year and conducted discussions on "FY 2009 Budget Overview," Guidelines for FY 2009 Budget Requests, and reform of special accounts of the government budget.

The new version of "Budget Overview" reflects only two remarkable differences compared to the previous one. During the previous meeting, some members pointed out the need to incorporate forward-looking messages as well as expenditure reduction efforts. In response, this version of "Budget Overview" refers to Economic Growth Strategy and other forward-looking agendas on page 2 which presents "Future Economic and Fiscal Policies." The last paragraph on the last page points out that the Government should sufficiently reflect the Pension Reform Law (which passed the Diet in 2004) when increasing the portion funded from its budget to basic pension plans to 50%.

Regarding "Budget Overview," the following comments were voiced:

Expert Member: The Pension Reform Law refers to the need to secure revenue sources for supporting the increase in the portion funded from the Government's spending to basic pension schemes, and indeed, it is really important to secure the revenue sources. We are yet to discuss what kind of revenue sources should be secured for the increase in the portion funded from the Government. This, in turn, will be a good opportunity for us to discuss issues concerning the consumption tax. We need to thoroughly discuss the issues, regardless of when the Government will increase the consumption tax.

Meanwhile, Network System for Basic Resident's Register is already put in place on a nationwide basis. This is the time to accelerate discussions on the introduction of a social security card.

No other comments were made, and I closed the discussion on "Budget Overview."

Regarding the Guidelines for FY2009 Budget Requests, Member Nukaga, Minister of Finance, made a presentation based on his papers. In response, the following comment was voiced:

In the fiscal year 2009 budget formation, what is important is how to strike a good balance between “financial consolidation” and “responses to priority issues.” Regarding financial consolidation, fiscal year 2009 marks the third year of the five-year program incorporated in “Basic Policies 2006,” and in line with a reform framework, we should continue our spending reduction efforts. In addition, to respond to priority issues, each ministry should make an inventory of its policies for the purpose of securing revenue sources worth 2% of an entire budget for its discretionary expenses, and the Government as a whole should establish a framework for addressing priority issues worth 300 billion yen, so the Government can sufficiently respond to important issues, including a national shortage of physicians. I would like to translate the framework into reality for formulating guidelines for the FY 2009 budget requests.

In response, the following comments were voiced:

Expert Member: What is the most important in the FY 2009 budget formation is to establish the framework for addressing priority issues. Important issues on the agenda are what should be incorporated in this framework and what kind of policies and expense items should be introduced in the framework. Dynamically changing the budget allocation practice by using the framework for addressing priority issues is an important point. Prime Minister should take the initiative in determining what should be incorporated and introduced in the framework. At the same time, determining what should be incorporated in the framework will convey clear messages to the general public. To clearly show the messages to people, the Government needs to present them in an easy-to-understand manner during the budget formation process. Accordingly, parties concerned are asked to present what kind of requests have been made by each ministry in terms of amounts and standards at meeting of the CEFT to be held in September and October. Then, the CEFP should discuss the requests.

Expert Member: The budget formation should convey forward-looking messages that share the standpoint of ordinary people. While the Prime Minister’s framework which is not constrained by ministerial frameworks (i.e. the framework for addressing priority issues) should be carefully deliberated in details, the CEFP should also sufficiently discuss the framework. As impressive messages addressed from the Prime Minister to people, the Government should clarify details of the framework.

Expert Member: The framework for addressing priority issues offers a good opportunity to demonstrate what kind of issues are considered important in the Fukuda Administration. It is essential for the Government to make better use of the opportunity. While requests each ministry will make to be incorporated in the framework are important, what is more important is to demonstrate the Prime Minister’s initiative to address these issues and to make the country more forward-looking.

In particular, countermeasures against the declining birth rate which should be taken across different ministries and global issues on the agenda such as environmental problems should be pushed forward as the administration's priority issues by the Prime Minister's initiative.

Mr. Nakano, Vice Minister of Economy, Trade and Industry: I appreciate Member Nukaga's presentation on the budget formation for the next fiscal year because it stresses the importance of "the budget efficiency improvement" by properly presenting policy issues essential for dealing with priority issues. METI will also make sharp budget requests for the next fiscal year.

Member Nukaga made the following comments in response to the above comments:

The Fukuda Administration has so far spent much of its time and energy in dealing with negative legacies from the 20th century. In preparation for the budget formation for the next fiscal year, we will establish a framework offering budgets which can be spent freely to make a fresh start and to deal with new political issues. As the expert members have commented, it is important to demonstrate the Prime Minister's initiative to formulate a better budget.

Then I said that a very important issue on the agenda is what should be incorporated in this framework, and accordingly, the CFP should also discuss what should be incorporated.

Regarding special accounts of the government budget, expert members made a presentation on the reform of special accounts based on their papers, and Member Nukaga also explained how special accounts have been reformed so far based on his papers. Member Nukaga also voiced the following comments in response to the expert members' papers.

I would like to do my best to make an inventory of policies and to implement the reform of special accounts.

The expert members have pointed out the need to review the existing mandatory system for many special accounts to make a deposit to the fiscal investment and loan program, and they have recommended that authorities should establish policies on the management and holding of assets of special accounts in order to optimize their assets management, instead of depending on the easygoing deposit management. Of course, depending on the easygoing management of deposits is no good, but the deposit system offers some benefits. For example, the system is offering low-risk depository services with relatively small clerical burden and covers many different agencies. Accordingly, one has to discuss what kind of policies special accounts are responsible for and who will take risks in terms of safety. One cannot abolish the deposit system simply concluding that it is no good. Anyway I would like to make reform efforts, giving careful attentions to various issues including the management of reserve funds.

Merger and abolition of special accounts of the government budget have been pushed forward at present in line with the administrative reform promotion law, and I will also reexamine details of special accounts carefully in preparation for a thorough review of the need of special accounts themselves scheduled to be carried out in fiscal 2011.

In addition, the expert members have recommended the implementation of the transparent budget management, pointing out the need to explicitly demonstrate expenditure reduction efforts in business accounting funds for special accounts (11.2 trillion yen for fiscal 2008) by setting a specific reduction target. Five trillion yen out of the 11.2 trillion yen balance was the amount transferred from general accounts; accordingly, budget ceilings shall be set on this portion. For the rest of the amount (six trillion yen), which includes the amount for reinsurance programs for earthquakes, should be treated differently, and one should not handle all of special accounts in a uniform manner. However, ensuring the transparency is an important challenge, and accordingly, we will make efforts to address each issue separately for pushing forward the reform.

Then the following comments were voiced:

Expert Member: We need to ensure the transparency of every process concerning special accounts, asking ourselves whether their policy purposes are reasonable and what kind of basis of calculation has been adopted for special accounts. Generally, people consider special accounts of the government budget as a castle full of demons which totally lacks transparency. At least, they have been seen in that way by people. Accordingly, the Government has to make reform efforts that are easy to understand for people. In efforts to reduce wasteful spending, the Government should discuss revenue sources earmarked for specific purposes as well as special accounts. In addition, not only special accounts but also the entire nationwide stock management should be reviewed based on the national government's financial statements. For example, property for public use which accounts for a considerable part of national assets, is currently evaluated at cost, and loans are recorded based on their book values. Instead, these accounts and total assets of the Government have to be explicitly clarified based on private-sector accounting rules. In other words, we have to review not only special accounts but also the national government's total assets as well. In this way, the review of special accounts will mark a milestone in the review of the governmental total assets.

Expert Member: 1.8 trillion yen has been transferred from the foreign exchange fund special account to general accounts. At a glance, it sounds nice. However, in reality, the operation of the foreign exchange fund special account depends on foreign bonds which are being invested at an interest rate of approximately 4.5%. The interest is being paid in US dollars. At the same time, on the other side of the investment, foreign exchange fund bills are being issued. The interest rate of the foreign exchange fund bills is 0.5%, and the difference, 4.0%, is investment profits denominated in US

dollars, thus generating investment profits worth 3.5 trillion to 4.0 trillion yen. Then the investment profits generated are spent to issue another foreign exchange fund bills. In order to balance a balance sheet, foreign exchange fund bills equivalent to the investment profits generated are being issued. Why the investment profits generated are spent to issue additional foreign exchange fund bills? The bills are issued to post the investment profits in the balance sheet, and the profits are then to be transferred to general accounts. The transfer of the investment profits to general accounts may contribute to a reduction in debt issues, or may be contributing to a reduction in long-term debt issues. However, additional short-term debt issues called foreign exchange fund bills are being issued instead within the foreign exchange fund special account. In other words, the whole process just issue additional short-term debt issues instead of long-term ones. This type of national debt management is really wise and prudent enough? Authorities should carefully reexamine the practice in the long run.

In addition, in the labor insurance special account, obviously wasteful spending, such as the construction of resort facilities called “Spausa” and other facilities including “The Vocational Museum Exhibit,” is all too noticeable. Why such construction projects have been approved? Anyway, special accounts, including the transfer from general accounts to labor insurance schemes, should be thoroughly reformed, with consideration given to specific cases.

Expert Member: The reform of special accounts should review functions and systems of special accounts themselves, instead of just saving money little by little. Though Member Nukaga has pointed out some advantages of the deposit system in the fiscal investment and loan fund in terms of safety, such advantages vary with features of each special account. For example, in employment insurance schemes, reserve funds shall be spent at once to pay unemployment benefits in case of a sudden sharp rise in the jobless rate resulting from some economic fluctuations. In that sense, employment insurance schemes need some liquidity. In contrast, the employees’ accident account is being operated just in a manner similar to pension plans, with its annual spending almost unchanged. Accordingly, I believe that it is acceptable enough to manage the employees’ accident account together with employees’ pension plans. There is some room for integrating fund managing programs for each special account, by abolishing the bureaucratic sectionalism across special accounts, I believe.

Mr. Nakano, Vice Minister of Economy, Trade and Industry: The wage level of those working for independent administrative agencies and for public interest corporations which receive money from special accounts is criticized as too high compared to the one paid for national government workers. We should discuss this issue, too.

Member Nukaga made the following comment regarding the foreign exchange fund special account: We have to understand that the foreign exchange fund special account is originally designed to

respond to a possible exchange revaluation loss following the appreciation of yen. At present we have some reserve funds in this special account, however, we have to keep in mind that the balance of the reserve fund will vary depending on foreign exchange rates.

I summed up the discussions as follows:

People are paying much attention to special accounts, too. Accordingly, the efficiency improvement in expenditures and ensured transparency are important, and of course, we should achieve a “zero futility government” and should make an inventory of policies. Yet I would like to further discuss the functions and systems of special accounts here at the CAFP. In addition, as the expert members have recommended, I will ask Expert Committee on “Research Committee on Government Assets and Debts Reform” to discuss reform directions and present the direction by this autumn so that they can be reflected in the FY 2009 budget formation.

At the end of the meeting, the Prime Minister made the following statements:

We must screen out every wasteful spending practice in special accounts in a manner similar to the one we adopt in our reform efforts concerning general accounts. We should confidently push forward the review of government expenditures, including issues the expert members have presented here today, and I would like to ask the expert members’ continuous support and cooperation.

(End)