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COMMITTEE OF SENIOR BUDGET OFFICIALS**

**Budgeting in Chinese Taipei**

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# Foreword

Chinese Taipei is an *Invitee* in the OECD Committee of Senior Budget Officials (SBO) and takes an active part in its activities.

In 2023, it was agreed that the OECD would undertake a review of Chinese Taipei's budget process. This report presents the results of that review. It is divided into five sections. The first section provides an overview of Chinese Taipei's economic and fiscal performance and outlines key features of the "architecture" of public finances in Chinese Taipei. The second section profiles the Directorate-General of Budget, Accounting and Statistics (DGBAS). The third section discusses the budget formulation process. The fourth section discusses the budget approval process. The fifth and final section presents main findings and key recommendations for the Chinese Taipei authorities to consider.

OECD experts visited Chinese Taipei in March 2023 for extensive discussions with officials from the DGBAS, the Department of Finance, the Development Council and line Departments. The mission also met with officials from the Legislative Yuan, the Budgetary Research Center and the Audit Office. In addition, the mission had an opportunity to exchange with leading academics on these issues. A second mission visited Chinese Taipei in September 2023 for further fact-finding and discussion with DGBAS officials.

The OECD wishes to extend its gratitude to all the officials it met for the generous time they spent with the mission and the full and frank discussions. In particular, the OECD would like to thank Mr. Dennis Liu and Ms. Una Chang of the DGBAS for their invaluable assistance throughout the preparation of this review.

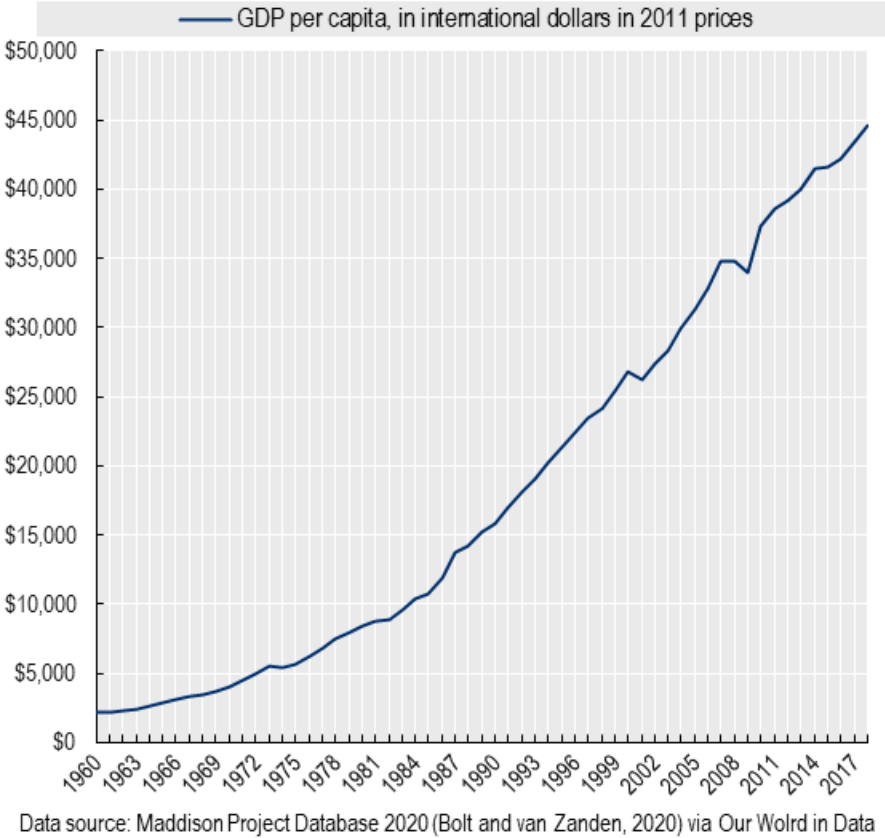
The views expressed in this report should not be attributed to any individual or organisation consulted in its preparation.

The term *Chinese Taipei* is used throughout this report in line with OECD protocols. The names of some governmental entities have been similarly modified.

# 1 Introduction

1. Chinese Taipei has experienced extraordinary economic growth since the 1960s (Figure 1), and today enjoys one of the highest per capita incomes in Asia. Sound macroeconomic policies have underpinned these achievements.

Figure 1. GDP per capita, 1960-2018



### Box 1. The Role of semiconductors

Chinese Taipei is the global leader in semiconductors, which drives its export-oriented economy. It produces over two-thirds of all advanced semiconductors and dominates the segment for the most advanced microchips essential to AI and other state-of-the-art applications. It is the home to the largest eco-system of research clusters for semiconductors in the world.

The importance of semiconductors to the economy and government finances of Chinese Taipei cannot be overstated.

### Prudent fiscal policy

2. An overriding emphasis on fiscal prudence – and small government – has characterised public finances in Chinese Taipei over time (Figure 2, Figure 3, Figure 4).

3. A balanced budget was maintained throughout the high-growth years. Only modest deficits were recorded following the financial crisis in 2008-9 and budgets were again largely balanced in the years prior to the COVID-19 crisis. Debt levels are low by international standards, fueled also by high GDP growth, and were declining steadily prior to the COVID-19 crisis. All government debt is domestic debt.

Figure 2 Total Debt, % of GDP, 2012-2022

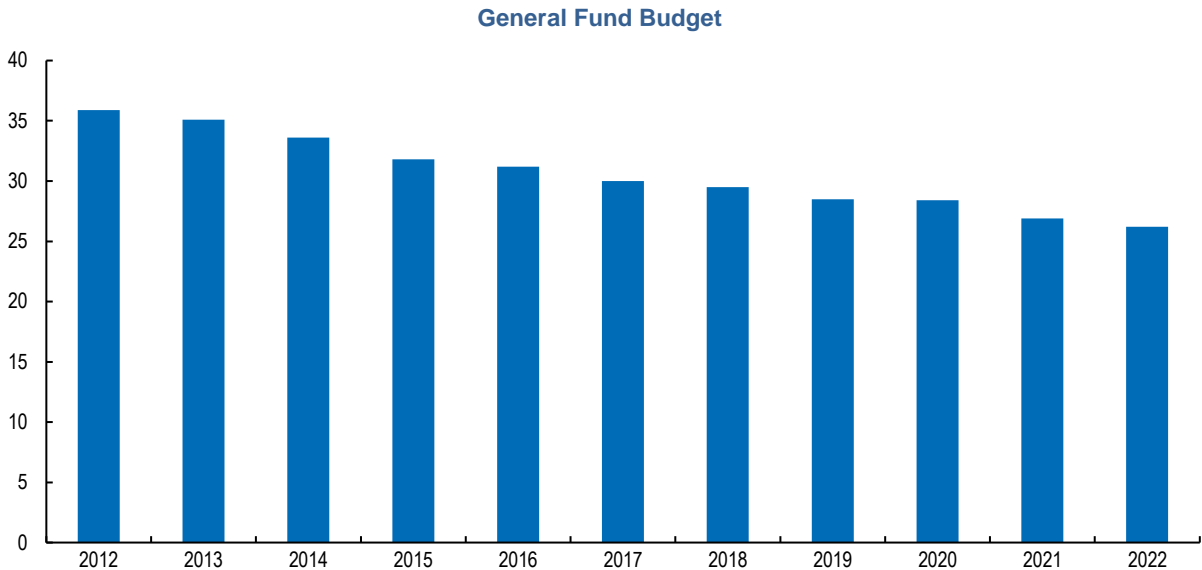


Figure 3. Budget balance, % of GDP, 2012-2023

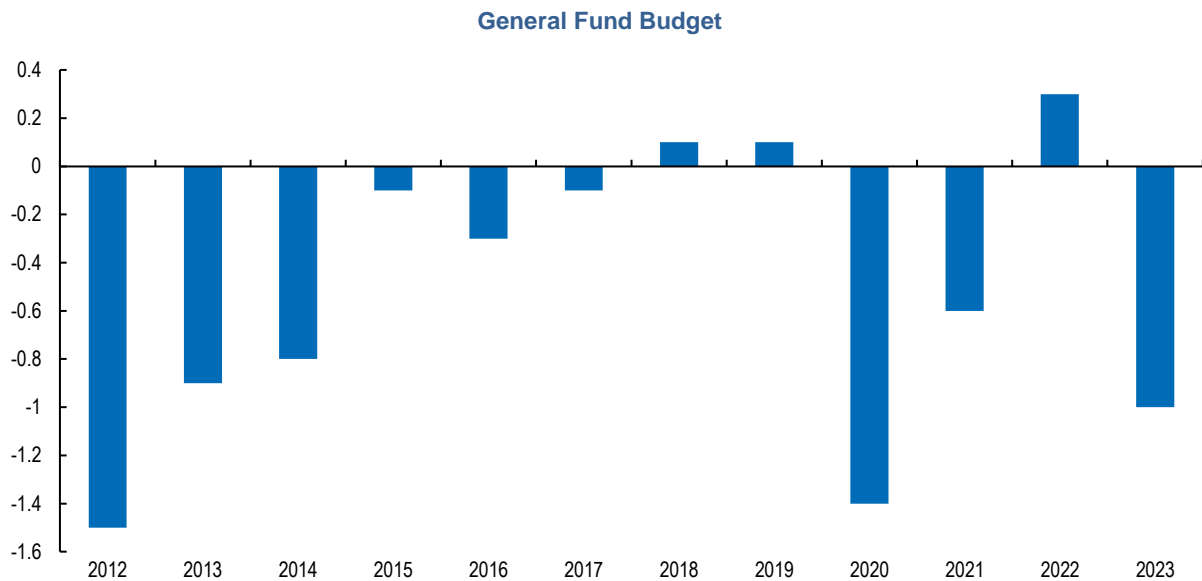
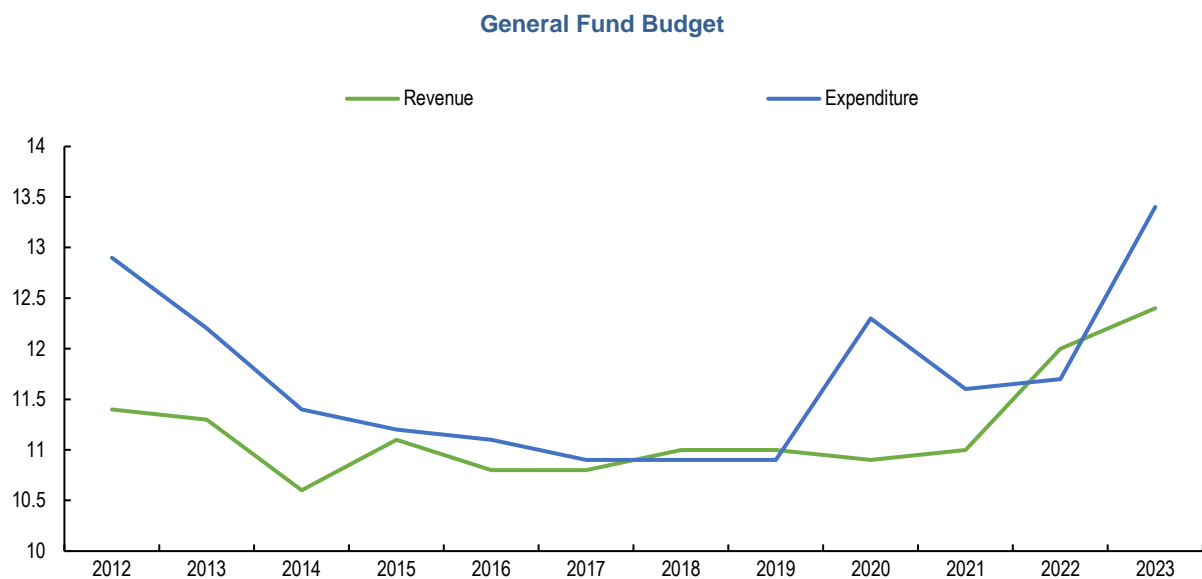


Figure 4. Revenue and expenditure, % of GDP, 2011-2023



4. Expenditures have grown largely in line with rising revenues over time, although strict expenditure discipline was maintained following the global financial crisis, as shown in Figure 4. The aggregate levels of revenue and expenditure are low in international comparison, especially for such an advanced economy. This needs to be interpreted with care, however, as social welfare spending is conducted largely through special funds with mandatory contributions separate from the general budget. This is discussed further in Box 3 and the next

section. It also needs to be borne in mind that this was a period of rapid economic growth with significant new nominal resources becoming available each year.

5. Chinese Taipei’s fiscal experience with COVID-19 was unique. The economy flourished during this period driven by demand for semiconductors (Box 1). This resulted in a surge in government revenue. Even with emergency support in full force, the budget only recorded modest deficits in 2020 and 2021 and experienced a surplus in 2022.

6. This surplus generated great public pressure for the money to be returned. At the same time, worldwide energy prices were surging following Russia’s war of aggression against Ukraine. As a response, innovative fiscal initiatives were taken which led to a significant fiscal deficit in 2023.

7. The measures were, however, constructed to be one-off or time-limited in duration and to support long-term fiscal challenges. Specifically, the government distributed a universal cash payment of TWD 6000 [USD 200] to each and every citizen and provided subsidies to the power utility to minimise rate hikes to households following the surge in global energy prices. The government also made a substantial capital injection to the public pension fund to support its long-term sustainability.

**Box 2. Summary of special fiscal initiatives, 2022-2025**

|  |                                   |
|--|-----------------------------------|
| Universal cash payment                     | TWD 142 billion (USD 4.4 billion) |
| Energy subsidies                           | TWD 300 billion (USD 9.4 billion) |
| Capital Injection to Labour Insurance Fund | TWD 225 billion (USD 7.1 billion) |

8. In addition to the above, the government also increased spending on specific public works projects on the basis they would support long-term economic growth.

**Box 3. General Fund and Special Fund**

The budget in Chinese Taipei is divided into two parts – the *General Fund* and the *Special Fund*. The Special Fund consist of a number of individual funds, each of which is an independent financial entity. The budget formulation procedures for the Special Fund is generally the same as for the General Fund and both are scrutinized and approved by the Legislative Yuan.

The key difference between the two is that the General Fund is financed mainly by general tax revenue whereas entities in the Special Fund are funded mainly by their own dedicated revenues sources, which can include revenue from the sale of goods and services and mandatory contributions to social welfare funds (See next section). Some entities in the Special Fund also receive appropriations from the General Fund.

## Special funds for social welfare spending

9. Chinese Taipei has a comprehensive social safety net and spending on social welfare accounts for one-fourth of total general budget outlays. However, most spending on social welfare takes place *outside* of the general budget and through special funds. These are funded by mandatory contributions from employers and employees, often supplemented by funding from the budget itself. This applies particularly in the case of health care and pensions.

10. A *National Health Insurance* (NHI) system funds universal medical coverage. Its principal source of financing is a mandatory payroll tax (currently 5,2%) that goes directly to the NHI. How the payroll tax is shared between employers and employees varies. In addition, the government makes contributions for low-income earners and ensures its overall viability.

11. A *Labour Pension Fund* (LPF) system administers individual retirement accounts for all workers. Employers must contribute a percentage (6% in 2023) of an employee's salary to their respective individual retirement account. Employees can make additional voluntary contributions to their account. The government guarantees a minimum rate of return on the accounts. Various other corporate and profession-specific pensions funds are in operation as well in Chinese Taipei in addition to the government-affiliated ones.

12. In addition, the *Labour Insurance Fund* (social security tier-1 pensions) has been undergoing comprehensive reform in recent years. This pension fund is severely underfunded and represent the greatest long-term fiscal challenge for Chinese Taipei. The government has been raising contribution rates as well as making very significant capital injections to the fund as outlined above.

13. The expenditures undertaken by these social welfare funds are mainly financed by social security contributions equivalent to about 6% of GDP. This compares to general budgetary expenditures of around 12% of GDP in recent years – see Figure 4 above.

14. The use of these special funds is largely a reflection of public attitudes towards government. The contributions are perceived as premiums rather than taxes, and thus face less opposition than taxes. This attitude is also reinforced by the fact that most medical services in Chinese Taipei are provided by the private sector.

## Fiscal responsibility legislation

15. Two laws have been enacted in Chinese Taipei to further promote fiscal responsibility – the Public Debt Act of 1996 and the Fiscal Discipline Act of 2019. It is noteworthy that this legislation had its origins in the Legislative Yuan, and not with the government. This demonstrates the widespread commitment to fiscal responsibility in Chinese Taipei.

- *The Public Debt Act* mandates that the debt of the government may not exceed 40.6% of GDP (three-year rolling average). Chinese Taipei's debt sits well below these limits. New borrowing may not exceed 15% of total expenditures each year. In addition, it requires the government to allocate “at least 5% to 6%” of tax revenue for repayment of principal on debt.<sup>1</sup>
- *The Fiscal Discipline Act* builds on the Public Debt Act and contains general provisions to promote fiscal discipline and spending restraint. Most pronounced is a requirement to identify the sources of funding for any new government expenditure. .

16. However, in many ways the latter only served to codify current practice. For example, the 2015 Long-term Care Services Act was accompanied by a series of new earmarked taxes to fund it.

17. These two laws come on top of the long existing organic *Budget Act*, which stipulates that current revenue and expenditure be balanced except in extraordinary circumstances.

### Box 4. Local governments

Chinese Taipei has twenty-two local governments. They receive grants from the government to deliver many services – including education in schools. Local government have traditionally also had property taxes as a principal source of own revenue. In line with a policy of greater autonomy, local governments now have the power to enact taxes. There is, however, great public resistance to such moves. Instead, local governments focus on securing larger grants. This is the principal tension in inter-governmental finances in Chinese Taipei. The total amount of debt held by local government is equivalent to about 4% of GDP. Similar fiscal responsibility laws also apply to local governments.

<sup>1</sup>Originally agreed as 40% of **GNP**, later modified to **GDP** at the equivalent level of 40,6%. The 5%-6% range reflects a compromise between competing proposals in the Legislative Yuan.

## Conclusion

18. The economic and fiscal situation of Chinese Taipei is enviable in most respects. It has a dynamic economy underpinned by the dominance of the global semiconductor sector, low levels of public debt and a commitment to expenditure discipline, backed by fiscal responsibility laws. Chinese Taipei's experience during COVID-19 and the resultant extraordinary revenue were disbursed in a fashion compatible with its commitment to fiscal discipline.

19. Looking forward, the greatest fiscal challenge facing Chinese Taipei relates to its rapidly ageing society and unfavourable demographics (very low birth rates). Most directly, this will impact old-age pensions and care for the elderly. As noted above, the government has been extensively reforming the pension system. A substantial amount of the extraordinary revenue during the COVID-19 pandemic was devoted to the legacy pension fund.

20. Finally, it is worth noting that, at the end of 2023, Chinese Taipei had foreign reserves of USD 571 billion - the fourth largest foreign reserves in the world. These are managed by the central bank and kept strictly from financing the budget. The amount of the foreign reserves is in excess of balance of payments requirements and represents a great reserve fund for Chinese Taipei.

## 2 Directorate-General of Budget, Accounting and Statistics

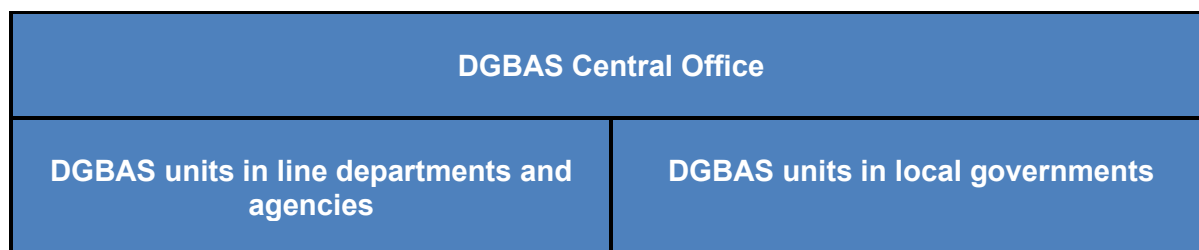
21. The Directorate-General of Budget, Accounting and Statistics (DGBAS) is a unique body with extraordinary scope and power. It has a staff of over 12,800 located at its central office in Taipei and in every budget entity at all levels of government. It lies at the centre of government, co-located with the office of the Head of Government, and its staff accompany the Head of Government to meetings. It has special independent power to issue “instructions” to government entities. It is responsible for the formulation and implementation of the budget, and is the government’s principal control agency. It sets accounting standards and produces the government’s financial reports. It is the official economic forecaster. It acts as the statistics office and census bureau.

22. The modern DGBAS traces its origins to the early 1900s when corruption was widespread in Chinese Taipei and the quality of decision making in government was low. The DGBAS was founded to foster good governance in Chinese Taipei, to professionalise decision making and eradicate corruption. This is the historical underpinning for the fundamental role of DGBAS in almost all aspects of government decision making and operations.

### Organisation and functions

23. In discussing DGBAS, it is useful to think of it structurally in terms of consisting of three elements – a DGBAS central office, DGBAS units in every line department and agency, and DGBAS units in every entity in local governments (Figure 5).

Figure 5. Organisation of DGBAS



24. Of the 12,400 DGBAS staff, fewer than 400 work in the Central Office. The remaining staff members are divided roughly equally among the units located in line departments and agencies and the units in local governments.

25. The vast majority of DGBAS staff – estimated at over 70% – are involved in budget implementation, including internal control. This also largely explains why most DGBAS staff are located in line departments and agencies and in local government. The comprehensive compliance procedures and internal control measures take place where the transactions occur.

## DGBAS Central Office

26. The DGBAS central office consist of eight departments, two of which are dedicated to budgeting – the General Fund Budget Department and the Special Fund Budget Department (Figure 6).

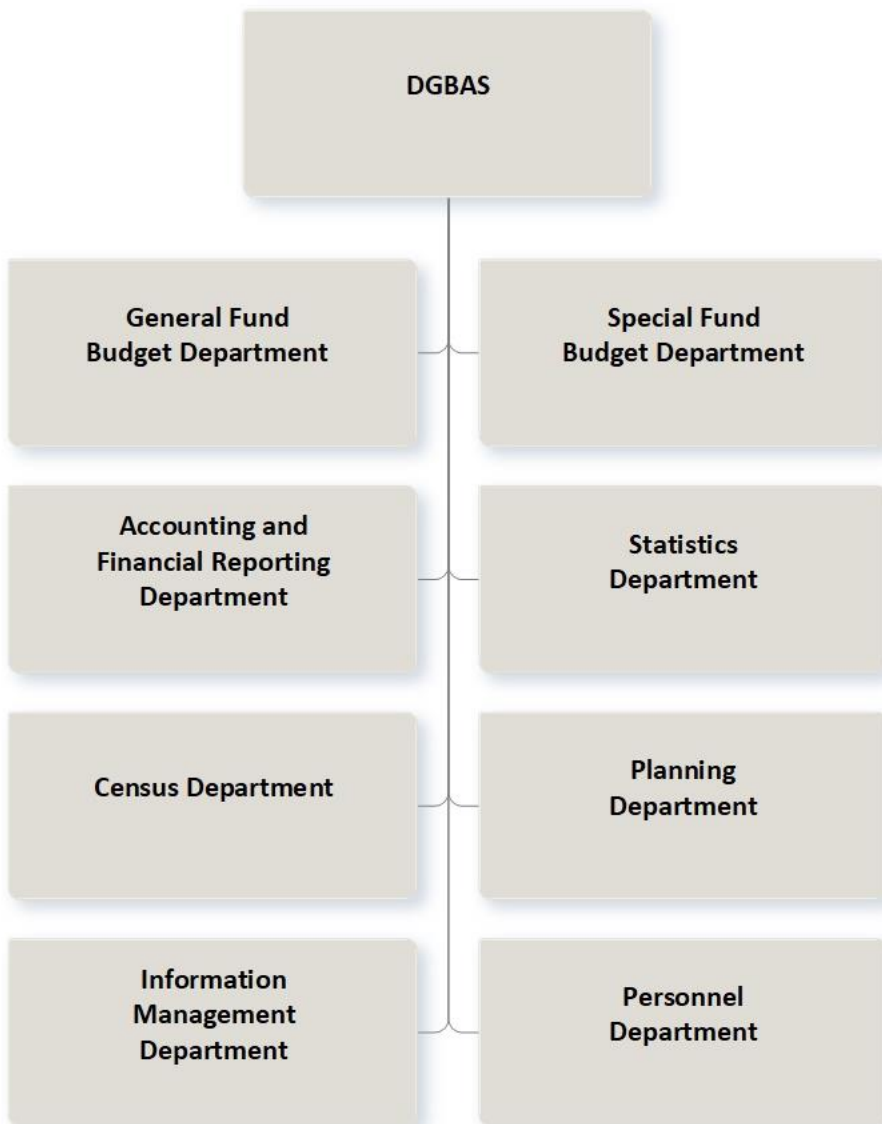
27. The General Fund Budget Department has a typical structure with a number of sections mirroring and interacting with their respective departments and agencies (Figure 7). A budget compilation section focuses on the aggregates and integrating the work of the various sections. It also has a section that focused on the finances of local government. The Department has 77 staff.

28. The Special Fund Budget Department (Figure 7) scrutinises the various Funds (such as the Health Insurance Funds and various pension funds), government enterprises, government sponsored foundations and similar. These bodies are generally not dependent on the annual budget funding for their operations. The Special Budget Fund Department focuses on the government's "ownership" interest in these bodies and fiscal risk implications. They review business plans, governance arrangements and major strategic decisions. These must be approved as part of the overall budget process. Each of the bodies will have a DGBAS unit in place. The Department has 40 staff.

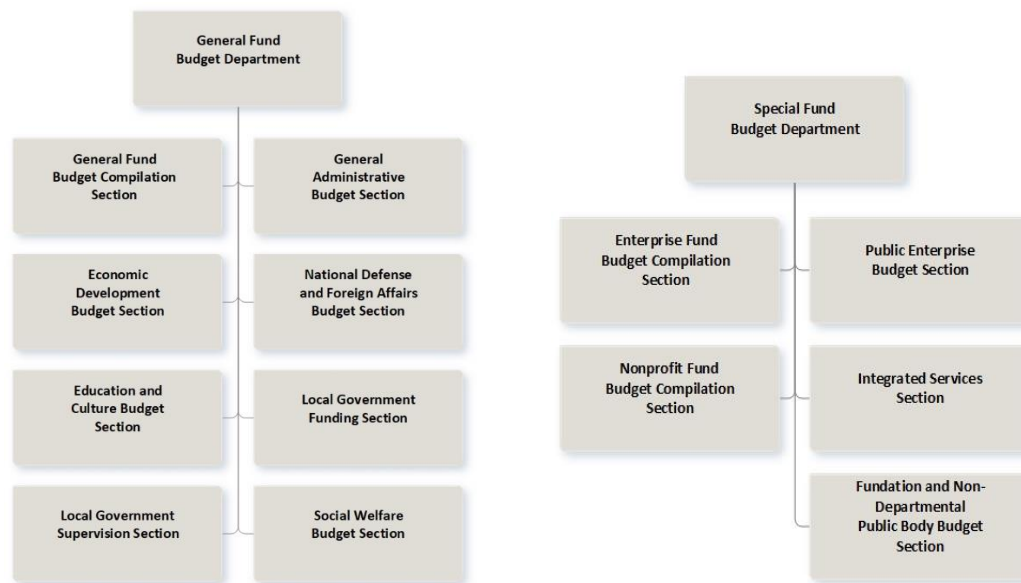
29. The Statistics Department is responsible for formulating the economic assumptions underlying the budget.

30. The Accounting and Financial Reporting Department is responsible for producing the government's financial statements. It also sets accounting standards for the government.

Figure 6. DGBAS organigram



**Figure 7. General Fund Budget Department and Special Fund Budget Department - organigram**



### DGBAS units in line departments and agencies

31. Each line department and agency is required to have a DGBAS unit. There are currently 67 Level-1 units and 1,120 Level-2 Units in place. Typically, a department would have one Level-1 unit and a number of Level-2 units located in its affiliated agencies. Various organs, independent councils and commissions would have their own Level-1 unit as well. The number and size of each unit is set by the DGBAS central office. There are a few instances where entities are considered too small for establishing a dedicated unit. In such cases, a single DGBAS unit serves more than one entity.

32. The staff of these units are nominally the staff of the entity where the unit is located while they serve there. They however remain part of the overall DGBAS personnel management system. While they are paid by the entity where they are located, they are very much seen as “DGBAS staff.” The DGBAS central office appoints the head and other senior staff of the Level-1 units. The Level-1 units in turn appoint the staff of the Level-2 units. The heads of the DGBAS units have a term of office of four years.

33. The overwhelming focus of the DGBAS units is on internal control. They have the sole authority to validate or reject transactions. In budgeting, they must also take into account the views of their respective Departments and agencies. How this works in practices varies greatly from one entity to another. These units are the official interlocutors with the DGBAS central office in the budget process. Their role is discussed further in the next chapter.

### DGBAS units in local governments

34. Despite the autonomy that local governments have come to enjoy in their finances, each local government is required to have DGBAS units.

35. Each of the twenty-two local governments will have a Level-1 unit. In turn, there are 4,807 Level-2 units in local governments. At the local level, there are many instances where multiple entities share a single DGBAS unit. Individual schools are an outstanding example of such arrangements.

36. All staff of DGBAS units in local government are fully integrated into DGBAS' personnel management systems. The head of each Level-1 Unit is appointed by DGBAS. Consultations are held with the respective mayors/heads of local government on these appointments. This can be sensitive, especially in cases where the mayors/heads of local government come from a different political party. The head of each Level-1 unit appoints other staff.

37. In their work, the DGBAS units are jointly responsible to the DGBAS central office and to the local government where they are located. In practice, they do not involve themselves extensively in budgeting/policy-making. Rather, the DGBAS units in local governments will focus on budget implementation, including internal control of transactions. The DGBAS units have the final say in these matters at local government level as well.

### Box 5. Department of Finance

In addition to DGBAS, there is a Department of Finance in Chinese Taipei. It is responsible for tax policy, tax administration and customs.

A key area of interaction between the Department of Finance and DGBAS concerns the revenue forecast which is the responsibility of the former and the economic assumptions the responsibility of the latter.

The Department of Finance also disburses all money (and receives all moneys) through the government's Treasury Single Account. Payments are only made following validation by DGBAS

## Conclusion

38. The story of DGBAS has been an overwhelming success in terms of its original mandate to professionalise decision making and eradicate corruption. Chinese Taipei is now an advanced economy and the circumstances that led to the current DGBAS could not be more different. It may be timely to revisit the organisation and functions of DGBAS and embrace a greater focus on the quality of expenditure.

## 3 Budget formulation

39. Chinese Taipei has an extremely centralised approach to budgeting, dominated by the DGBAS. It is very much focused on the maintenance of aggregate fiscal discipline.

40. The setting of spending ceilings at the start of April each year is the key milestone in the budget formulation process. An intensive period of activity, starting in January, leads up to this. Baselines are updated. Preliminary economic assumptions and revenue forecasts are prepared. New high-level policy priorities are put forward and departments lobby for new spending. After setting spending ceilings, departments prepare their budget submissions, often in excess of the ceilings. Continued high-level discussions and lobbying takes place. Following updated economic assumptions and revenue forecasts in August, the budget proposal is finalised and submitted to the Legislative Yuan.

**Table 1. Budget formulation calendar**

| Fiscal Year = Calendar Year |  |
|-----------------------------|--|
| <b>January-March</b>        | Baselines updated<br>Preliminary economic assumptions and revenue forecasts<br>High-level discussions on policy priorities |
| <b>Early April</b>          | Spending ceilings set  |
| <b>May-July</b>             | Departments prepare budget proposals<br>Review of budget proposals<br>High-level discussions on policy priorities          |
| <b>August</b>               | Updated economic assumptions and revenue forecasts<br>Final preparations of budget proposals                               |
| <b>End August</b>           | Budget proposal submitted to Legislative Yuan  |

### Updating baselines

41. The first step in the budget cycle is reviewing the baseline of existing expenditure for the upcoming year. This takes place in the first quarter. The objective of DGBAS during this period is to ensure that all baselines are up to date. The DGBAS units in line departments will request updates from the various policy areas across their departments.

42. The role of the DGBAS units can vary greatly from one department to another department. In some cases, they are viewed as a partner. Information flows easily. In other cases, the DGBAS units are treated more as arm's length bodies. In such cases, the various policy areas across the department largely operate in isolation, and only provide the DGBAS units with the necessary information to transmit to the DGBAS central office. Importantly, the DGBAS central office conducts all of its communication with departments through the DGBAS unit.

43. The policy areas will often request increases that are well above what can be considered legitimate updates to their baseline. They will nonetheless work to convince the

DGBAS units of their spending pressures as this will be key to the setting of their spending ceilings. The DGBAS units will engage in discussion with the respective policy areas to moderate these. The line between baseline updates and new policies can be fine at times. At the end of the day, however, the DGBAS units will transmit the figures the policy areas have put forward. The DGBAS central office, informed by the DGBAS units, will judge what are legitimate updates to the baseline.

44. In the case of infrastructure spending and science and technology spending, the baseline updates will be forwarded also to the Development Council and the Science and Technology Council, respectively, for review. The role of these bodies in the budget process is unique (Box 6).

### Box 6. Development Council

The Development Council played a pivotal role in the early development of Chinese Taipei. It formulated detailed four-year Development Plans that strongly informed budget decisions. As Chinese Taipei has modernised, the Development Council has evolved and the Plan is more of a commentary on structural issues.

The Development Council does however continue to maintain a comprehensive Infrastructure Development Plan. This includes a long-term pipeline of new investment. As such, the Council takes a leading role in reviewing all infrastructure-related spending in the budget to ensure its consistency with the Plan. A small amount of “Social Development Projects” are also subject to review by the Development Council.

The Science and Technology Council has a similar role in reviewing spending in that area and ensuring its consistency with the Science and Technology Development Plan.

## Economic assumptions and revenue forecast

45. At the same time, preliminary economic assumptions are being prepared by the Statistics Department of DGBAS and an initial revenue forecast by the Department of Finance. The forecast will indicate resource availability ahead of decisions on Spending Ceilings. These will be ready by the end of March.

46. It is noteworthy that it is DGBAS itself that prepares the economic assumptions for the budget. This includes the forecasts for GDP growth, the composition of GDP growth, the current account and inflation.

47. The Department of Finance’s revenue forecast will naturally be informed by the economic assumptions prepared by DGBAS, but the Department of Finance employs a conservative approach to revenue forecasting. Actual revenue regularly exceeds forecast revenue – and at times by very significant amounts.

48. There is not an independent body to assess the economic assumptions prepared by DGBAS. It does however invite academics and external researchers to share their views on economic trends and the economic assumptions for the budget. According to the *Fiscal Discipline Act*, DGBAS must provide an “explanation” if there’s a difference of more than “twenty percent” between the forecasts and assumptions formulated by DGBAS and the views of the invited academics and researchers. The conservative approach to revenue forecasting serves as a buffer for any deviations that may arise.

## Expenditure ceilings

49. The DGBAS central office will analyse all the baseline updates it has received, including the reviews from the Development Council and the Science and Technology Council, and prepare a report to the Head of Government. It will only incorporate into this report its judgment of legitimate baseline updates, not the original proposals by Departments. DGBAS updates, on a standardised basis, certain categories of expenses such as salaries.

50. The Department of Finance will also present its revenue forecast to the Head of Government. There will be discussions with the Statistics Department of DGBAS and the Budget Departments of DGBAS in arriving at the revenue forecast.

51. The report by DGBAS does not recommend specific expenditure ceilings. It is however the basis for high-level discussions between the Head of Government, Head of DGBAS and Heads of Departments, and the basis upon which the spending ceilings are arrived at.

52. An intense amount of lobbying for new policies and new spending occurs in the months leading up to the decision on spending ceilings and it becomes more intense in the immediate period before. With high economic growth, resources would typically exceed baselines for the upcoming year, creating room for new spending.

53. These are resolved through a series of bilateral meetings between the Head of DGBAS and the Heads of Departments. In some case, bilateral meetings occur between the Head of Government and Heads of Departments.

54. In early April, the DGBAS issues the spending ceilings for each department. A department would only be aware of its own spending ceiling, not those of other departments. The ceilings that departments receive will reflect their updated baselines and any political decisions to increase (or decrease) funding for a particular area. In formal terms, the spending ceilings are set for the following year and the next three years. In practice, the focus is on the following year only (Box 7).

### Box 7. Four types of expenditure ceilings

The Expenditure Ceilings are divided into four categories:

- Operating expenditure
- Mandatory expenditure
- Infrastructure expenditure
- Science and technology expenditure

The latter two ceilings are simply to ring-fence the spending that is under the purview of the Development Council and Science and Technology Council as detailed earlier. In recent years, they have together account for about 10-15% of the budget. The ceiling for mandatory expenditure covers 60-70% of total expenditure. This concept has a wide definition in Chinese Taipei. The operating expenditure – accounting for 20-30% of total expenditure in recent years – is a residual category and, in some ways, receives the greatest attention in the budget process.

Salaries of government employees are considered in the mandatory category. This reflects the tenured nature of government employment in Chinese Taipei. A comprehensive system of manpower quotas (staff ceilings) is in place as a control to reinforce the spending ceilings.

## Budget submissions

55. Departments will then prepare their budget submissions.
56. In some cases, this will be a continuation of the work already undertaken as part of the process of updating the baselines. In other cases, this will represent the first active involvement of departments in the budget process. In such cases, their baselines will only have been updated for the categories of expenditures centrally determined by DGBAS, such as salaries.
57. How departments approach the spending ceilings also varies. This also reflects the diversity of how the DGBAS units operate in departments. As discussed earlier, this in turn reflects the varied relationship they have with their “host” departments. In some cases, the DGBAS units support the leadership of the department by providing a strategic overview of the different policy areas for budgeting purposes with insights on strengths and weaknesses. In other cases, they are treated at arm’s length.
58. In the former case, the various policy areas would present their submissions to the DGBAS unit – often a recasting or enhancement of the originally submitted updates to their baselines. What was rejected as an update to a baseline may well be funded within a larger spending ceiling. A Review Committee, headed by the Deputy Head of the Department, will make the recommendations to the Head of the Department on final choices to submit. The Review Committee would include representatives of all the policy areas of the department with a leading role played by the head of the DGBAS unit in informing choices.
59. In other cases, the spending ceilings will be deconstructed to the various policy areas. In effect, even the smallest spending entity within the department will receive its own ceiling. Each of them will prepare their submissions – for the first time in the process as they did not participate in the baseline updating exercise.
60. In both cases, the final submissions may be higher than the spending ceiling. In fact, over half of departments submit proposals that exceed their spending ceilings. The former are however more strategic in nature having undergone a thorough internal review whereas the other proposes are less developed. The DGBAS units will transmit the final proposals of the department, irrespective of whether they exceed the spending ceilings or not.
61. There is very limited reallocation, even in departments with an elaborate review structure. This is a reflection of the history of resource availability due to higher economic growth each year. At the stage of providing budget submissions there may still be a view that additional resources will become available in the final stage when new economic assumptions and revenue forecasts are presented. Departments position for this, often informed by the discussion of priorities earlier. Intensive lobbying continues.
62. To incentivize compliance with the spending ceiling for operating expenditure, DGBAS has put in place a reward system. A department will receive a “bonus” of 0.5% for remaining within the ceiling. This rises to 1% for being within the ceilings for two years, and 1.5% for three. The reward is in the form of a “lump sum” that may be applied throughout the department. Only a few departments benefit from this incentive system.
63. As with the case with baseline updates, infrastructure submissions and science and technology submissions will be forwarded also to the Development Council and the Science and Technology Council for review.
64. Budget proposals must be in accordance with instructions and guidelines set by DGBAS. The instructions include information requirements needed to support the proposal. In the case of infrastructure spending and science and technology spending, the proposals must

also comply with special information requirements set by them, including cost-benefit analysis for major projects.

### Box 8. Performance information

Although the role of the Development Council in the budget process has fundamentally changed since the Council was established, and is now limited to infrastructure spending, each department is required to submit an annual planning document to the Council. These documents provide details of each department's policy objectives – often at very high-level – and contain an abundance of performance data. Although the DGBAS participates in the review of these documents by the Development Council, there appears to be ample scope to improve the linkages between them and the budget.

Separately, DGBAS has in place a system of “performance assessments.” These assessments contain performance measures that are centred around efficiency and spending control, and compliance with these measures is linked with employees' financial benefits. In reality, they serve as further controls on spending.

It is a work in progress to enhance the use of performance information in the budget process.

## Finalising the budget proposal

65. In July, all spending proposals will have reached DGBAS, including the reviews from the Development Council and Science and Technology Council. The DGBAS central office will have been in constant communication with the DGBAS units in department during the period where the proposals were being finalised. DGBAS will assess the proposals received, including the ones in excess of the spending ceilings.

66. The updated economic assumptions and final revenue forecast will also be available at this time. In view of the updated revenue forecast, there may be scope for additional spending than was envisaged at the time of setting the spending ceilings.

67. An intensive series of meeting between the Head of Government, Head of DGBAS and the Head of Department of Finance on the one hand and heads of line departments on the other hand takes place for final consideration of the budget proposal.

68. The budget documentation is then finalised by DGBAS and submitted to the Legislative Yuan just prior to the end of August.

### Box 9. Accounting standards

Chinese Taipei budgets on a cash-basis and prepares budget execution reports on a cash-basis. At the same time, it has adopted accrual basis for accounting and financial reporting. Comparison tables are prepared to reconcile the two. The adoption of full accruals has been a gradual process that started in 2016. A single IT system is in place across all levels of governments which facilitates the timely and paperless preparation of financial statement.

The accounting standards used for financial reporting are set internally by the Accounting and Financial Reporting Department of DGBAS. There is no independent accounting standards mechanism in place, although DGBAS stated aim is to align with international standards.

### Box 10. Budget transparency

There is a very high level of budget transparency as well as a high level of public engagement on fiscal issues in Chinese Taipei, as witnessed by the strong sentiment for fiscal discipline and small government.

The budget and any special budgets are available in full, including on-line in machine-readable format. Very detailed information is available on the finances of each entity. The government publishes monthly budget execution reports (cash basis) as well as mid-year and annual financial statements (accrual basis), including on-line in machine-readable format. Information on future commitments, such as unfunded pension liabilities, and contingent liabilities, is regularly disclosed as an inherent part of the financial statements.

Detailed information on government debt is regularly made available by the Department of Finance. The Department also maintains a network of public displays in various venues showing the total amount of government debt – “debt clocks.”

## Conclusions

69. The overwhelming focus of the budget formulation process in Chinese Taipei is to maintain aggregate fiscal discipline and control expenditures. It has a proven track record in achieving this mission.

70. There is less of a focus on the institutional framework that supports the quality of public expenditure.

71. Budgeting in Chinese Taipei has only an annual focus, notwithstanding the existence of a nominal multi-year framework. Updating baselines is a singular event rather than an on-going process. These two issues are mutually reinforcing.

72. The use of performance information to inform budget decision making is lacking despite the collection of a wealth of such information by the Development Council. There is little attention paid to re-allocation and spending review of baseline expenditures. Attention is focused on incremental increases.

73. Addressing these issues may imply a change in the way DGBAS operates with a greater focus on quality of public expenditures.

74. The lack of institutional independence for formulating economic assumptions and setting accounting standards is noteworthy.

75. Budget transparency is exemplary although information on public finances may appear rather dispersed to a casual user.

## 4 Budget approval

76. The Legislative Yuan's takes as its mission to promote and reinforce expenditure discipline in Chinese Taipei. As discussed in the Introduction, it was the Legislative Yuan – at its own initiative – that enacted the *Fiscal Discipline Act*. This is very much a reflection of popular sentiment. Members of the Legislative Yuan regularly implore the government to exercise fiscal discipline and they “interrogate” senior officials for their use of funds throughout the year.

77. The actual powers of the Legislative Yuan to amend the budget are however very limited. It can only reduce expenditure; it may not increase expenditure. This has been interpreted to prevent the Legislative Yuan from any reallocation of funds, (it may not reduce one appropriation to fund an increase in another even if the net effect is zero).

78. As a principle, the Legislative Yuan exercises this power and proposes reductions in expenditure from what is contained in the original proposal. The Legislative Yuan has however increasingly taken to the practice of “freezing” appropriations, *i.e.* preventing the use of an appropriation, until specific requirements have been met in the course of implementing the budget.

79.

### Box 11. The Legislative Yuan

The Legislative Yuan is a unicameral body with 113 members. The members serve four-year terms and are eligible for re-election. Members are elected through a mixed system. Seventy-three members are elected by simple majority vote in single-member constituencies and 34 members by proportional representation vote. Six seats are reserved for the Aboriginal community.

For members elected by proportional representation, voters select political parties and members are then chosen based on party candidate lists. At least half of the seats won by each party must be filled by female candidates. Six seats elected by proportional representation are reserved for Aboriginal candidates.

Parties need at least 5% of votes to secure a seat in the Legislative Yuan.

**Budget approval cycle**

80. The budget must be presented to the Legislative Yuan four months prior to the start of the fiscal year, *i.e.* before the end of August each year. The Legislative Yuan must approve the budget one month prior to the start of the fiscal year. The Legislative Yuan therefore has three months to deliberate the budget.

81. Following the introduction of the budget, it has three readings in plenary session and is scrutinised by the Finance Committee and seven sectoral committees. The Legislative Yuan is supported by the Budgetary Research Center in its deliberations. The Audit Office also contributes important input to the discussion.

82. The presentation of the budget proposal is a high-profile event extensively covered by the media. The government will highlight its policies and priorities. All political parties engage in the subsequent discussion which often becomes quite boisterous. This occasion is a prime opportunity for the parties and individual members to present themselves to the public. General calls exhorting fiscal discipline often animate this discussion. The government responds as appropriate.

83. This constitutes the first reading of the budget. It is then referred to the Finance Committee.

**Table 2. Budget approval calendar**

| Fiscal Year = Calendar Year |   |
|-----------------------------|---|
| <b>End August</b>           | Budget proposal submitted to Legislative Yuan   |
| <b>September</b>            | First Reading in plenary<br>Budget proposal referred to the Finance Committee and sectoral committees   |
| <b>October</b>              | Finance Committee and sectoral committees scrutinize budget proposals   |
| <b>Early November</b>       | Each Standing Committee submits report to the Finance Committee<br>Finance Committee prepares its report<br>Negotiations among political leaders / Party caucuses |
| <b>End November</b>         | Second and Third Reading<br>Budget approved by Legislative Yuan   |

84. The Finance Committee plays a key role in scrutinising the budget proposal. It focuses on the overall fiscal position, the budgetary aggregates and its economic impact. The Finance Committee also has direct oversight responsibility for DGBAS, the Department of Finance and the Central Bank.

85. For specific appropriations, the Finance Committee relies on the seven sectoral committees to scrutinise their respective areas of competence. For example, the budget for the Department of Education would be examined by the Education and Culture Committee. The Finance Committee manages this process and sets specific timelines for each of the sectoral committees to report back. Committee meetings are open to the public and are broadcast live.

86. The level of analysis and the time it takes to consider the budget proposal ranges across each of the seven committees. They may invite senior officials to present on their proposal and to answer questions. The committees will be assisted by the Budgetary Research

Center in its work as well as informed by the conclusions of the Audit Office. Outside groups and external experts are rarely invited to participate in meetings where the budget proposal is being considered.

87. The focus of the committees is on discussing which appropriations to “freeze.” A common practice in for the Legislative Yuan to “freeze” an appropriation. This entails that the appropriations cannot be disbursed, or can only be partially disbursed, without the department reporting back to Legislative Yuan after fulfilling specific requirements set by the committee. It is also not uncommon for committees to undertake field visits departments.

88. Some committees complete their scrutiny in a meeting lasting only a few hours, others may take several days. It is, however, always a short period of scrutiny.

89. The committees then submit a report to the Finance Committee. The reports will include a list of appropriations to be frozen. If there are divergent views in the committees, they will all be presented in the report. The Finance Committee will integrate all of the sectoral committee reports together with its overview. This will be ready ahead of the Second Reading of the budget in plenary. It is noteworthy that very few specific recommendations for reducing expenditure are generally contained in this integrated report.

90. The discussion on where to reduce expenditure takes place in negotiations among political leaders or party caucuses following the report of the Finance Committee. They will agree (or a majority will) where to reduce expenditure and by how much. The reductions are generally across-the-board in nature and apply to categories of expenditures rather than to specific programmes. DGBAS staff as is often at hand to provide costings and technical advice. These negotiations conclude prior to the second reading in plenary. The negotiations will also finalize any outstanding items resulting from the Report of the Finance Committee.

91. At the Second Reading, the proposed budget document itself is formally read article-by-article. The review reports of the Committees are also presented. The conclusions of the negotiations among political leaders are also formally introduced. A general discussion follows and a motion to revise the budget proposal is made. Once the proposed budget bill has completed the Second Reading, it proceeds immediately to the Third Reading and is formally approved.

92. There are standing procedures in place if the Legislative Yuan were not to approve the budget prior to the start of the fiscal year. With the exception of new capital spending and new program expenditure, the government may continue to operate based on the same level of spending previously authorized (previous year).

### Box 12. Special Budgets

In extraordinary circumstances, a Special Budget may be proposed. Some provisions of the fiscal responsibility laws do not apply to a special budget.

The extraordinary circumstances are defined as follows:

- Major Emergency
- Major Economic Event
- Major Calamities
- Major political events that takes place irregularly or once every few years.

Extensive use of Special Budgets was made in the context of the COVID-19 pandemic. Previously they had been used principally enacted at times of natural disaster. There has been criticism that special budgets have been used in instances where expenditure could have been made through the regular budget.

Special budgets receive expedited treatment in the Legislative Yuan.

## Budgetary Research Center

93. The Budgetary Research Center provides analytical support to the Legislative Yuan in its deliberations of the budget. It has a staff of 50 analysts and is organized into divisions to mirror the committee structure of the Legislative Yuan. The staff of the Center attend meetings of the committees and in effect act as the Committees professional staff on budget-related issues.

94. It prepares over 300 research reports each year. These range from a 2-volume flagship report analysing the government's budget proposal each year as well as numerous reports on individual institutions and specific topics. The reports provide a comprehensive narrative and a wealth of financial analysis. It is its principal reference for members of the Legislative Yuan in budget scrutiny. Its reports are publicly available and attract media attention. It all supports the culture of fiscal responsibility in Chinese Taipei.

95. The Center also provides "consulting opinions" at the request of members of the Legislative Yuan.

## Audit Office

96. Independent audit is performed by the Audit Office.

97. The financial statements of the government are prepared by the DGBAS. This must be completed within four months of the conclusion of the fiscal year. The Audit Office must then complete its audit of the government's financial statements within three months and submit its audit report to the Legislative Yuan.

98. As has been discussed throughout this report, there is a very strong focus on internal control in Chinese Taipei to ensure that spending complies with the budget. In practice, inappropriate budget execution is extremely rare in Chinese Taipei.

99. The Audit Office currently places a strong emphasis on further developing its work on performance auditing.

100. The relationship with the Legislative Yuan is very strong. The Budgetary Research Centre and the committees of the Legislative Yuan make strong use of its work in scrutinizing the budget and holding the government to account.

101. A particularly noteworthy aspect of how the Audit Office operates is the priority placed on communication and engagement with stakeholders. This extends to citizens and civil society groups directly through means such as focus groups, advisory committees and surveys.

### Box 13. Limited Flexibility in Budget Implementation

The budget in Chinese Taipei is appropriated at an exceptionally detailed level.

- Re-allocation during the year is limited to changes only between object of expenditure within the same account. Transfers may not exceed 20% of the original budget for both the sending and receiving objects. No transfers can be used for personnel expenses.
- No transfers may be made for items deleted or reduced by the Legislative Yuan.
- Aside from fulfilling commitments already entered into, there is no possibility to carry-forward unused funds to the next year.

Due to the strong system in place for internal control, the budget is generally implemented exactly as the Legislative Yuan approved it. No carry-forwards and only minimal underspends.

## Conclusions

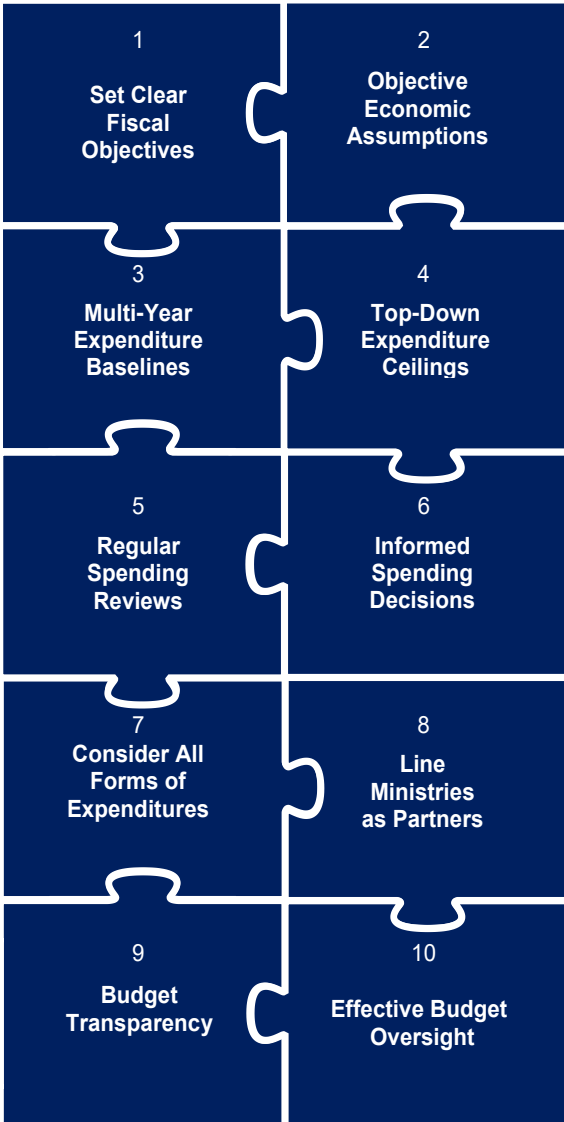
102. The budget approval process in Chinese Taipei highlights the commitment to fiscal responsibility in Chinese Taipei. The Legislative Yuan promotes a general culture of fiscal discipline and demonstrates this by reducing total spending in the budget proposal each year.

103. The actual scrutiny of the budget proposal by the committees of the Legislative Yuan, however, appears to be minimal and rely to a large degree on the conclusions of the Budget Information Center and the Audit Office.

# 5 Main Findings and Key Recommendations

104. This chapter draws together the main findings and key recommendations arising from the previous discussion. It is organized in line with the OECD Spending Better Framework.

Figure 8. OECD Spending Better Framework



## Fiscal Objectives

105. Chinese Taipei has clear fiscal objectives and enjoys widespread commitment for those objectives. Fiscal responsibility and expenditure discipline is enshrined in legislation and political commitment is well symbolized by the Legislative Yuan reducing spending when it considers the government's budget proposal.

106. This has been achieved by a strong focus on aggregate expenditure discipline. This fiscal culture developed in a period of high economic growth when new fiscal space became available with rising revenues. Looking forward, it is important for Chinese Taipei to develop a greater focus on the quality of public spending and the reallocation of expenditures to fund new spending pressures and new priorities.

107. Many of the findings and recommendations below can be seen directly in this light.

## Economic Assumptions and Revenue Forecasts

108. Unbiased economic assumptions are crucial to avoiding revenue shortfalls and unplanned spending pressures. Deviations in this area are a government's greatest recurrent fiscal risk.

109. In Chinese Taipei, the economic assumptions are prepared *internally* in DGBAS and the revenue forecasts *internally* in the Department of Finance. The conservative approach to revenue forecasting employed by the Department of Finance implies a buffer against deviations.

110. Chinese Taipei may wish to consider establishing an external body to *review* the economic assumptions and revenue forecasts.

111. In some OECD countries, responsibility for their *production* has been transferred to an independent body.

## Multi-Year Expenditure Baselines

112. Baselines are the foundation of the budgeting process. They illuminate the multi-year implications of spending decisions, and act as an early warning of emerging expenditure trends. They facilitate decisions to re-allocate resources, especially in case of structural reforms that require a time horizon beyond the upcoming budget.

113. In Chinese Taipei, the budget formulation process is focused almost entirely on the following year's budget. The period of updating baselines in the budget formulation process could more accurately be described as simply constructing a baseline. The previous year's baseline would not have been maintained.

114. Chinese Taipei may wish to revitalize the multi-year expenditure baselines in place by ensuring that it is continually updated throughout the year. There should be a reconciliation of the baseline and actual expenditure to encourage discipline in its preparation and foster transparency. This would also enhance the efficiency of the annual budget process.

## Top-Down Expenditure Ceilings

115. Expenditure ceilings operationalize the government’s high-level fiscal objectives in concrete terms and reflect allocations and reallocations to fund new policy initiatives. Implicit in the concept of expenditure ceilings is that Heads of Departments should have flexibility to reallocate resources within their overall expenditure ceilings.

116. Chinese Taipei has in place a robust system of expenditure ceilings. They are focused on the control of aggregate expenditures. The ceilings are less effective in promoting reallocation of spending within the total expenditure ceilings.

117. This is likely due to several factors. First, it is a historical legacy with the budget process focusing on new incremental spending. It will take time to unwind this. Second, Departments may lack capacity to effectively promote reallocation within their departments – this is discussed further later in the section. Third, there are practical obstacles to reallocation. Some 60-70% of spending is classified as mandatory and is therefore considered off-limits. What is mandatory with a one-year time horizon, however, may be less mandatory with a longer time horizon. The multi-year nature of the expenditure ceilings should be revitalized in tandem with the multi-year expenditure baselines.

118. Chinese Taipei may wish to consider comprehensive action to further enhance the expenditure ceilings and promote reallocation by Departments as described. Relaxing rules for in-year transfer of appropriations should also be considered in this respect.

## Regular Spending Reviews

119. Spending reviews are a powerful tool to identify opportunities for reallocation in order to align spending with government priorities, and to control total expenditures. They focus in particular on the accumulated baseline of expenditures. The scope of individual spending reviews may be broad or narrow. Performance and results information, budget impact analysis, and public policy evaluations are key inputs to spending reviews. Spending reviews are generally conducted jointly by budget offices and line Departments and are inherent part of the budget process.

120. There is currently not a system in place in Chinese Taipei for conducting regular spending reviews.

121. Chinese Taipei may wish to consider implementing a system of spending review. It may be especially fruitful in an environment where there has been less systematic scrutiny on the baseline of expenditures and significant amounts are classified as “mandatory.”

## Informed Spending Decisions

122. Performance information helps inform spending decisions and improve expenditure performance. It is a key support for spending review and reallocation of resources. Key performance indicators and targets should be included in budget documents together with monitoring mechanisms and regular reporting.

123. The budget and the budget process are also a powerful instrument for affecting change, including in areas such as climate change and gender equality. Budget impact analysis is one of the tools that can help inform how budget decisions impact both positively and negatively on specific high-level policy goals.

124. The situation in Chinese Taipei with regard to performance information is complicated. A wealth of performance data is collected by the Development Council. This is a legacy of the period when the Plan informed budget decisions. This is no longer the case except in the case of infrastructure spending and certain “Social Development Projects.” There would appear to be ample scope to rationalize the institutional responsibility and ensure performance information is for, and used for, budget decision making.

125. Green budgeting and gender budgeting are in their infancy in Chinese Taipei. In the case of gender budgeting, it is the responsibility of the Department of Gender Equality rather than DGBAS. Gender budgeting as a tool would appear to especially relevant for Chinese Taipei to promote women’s participation in the labour market and other initiatives stemming from the demographic challenges in Chinese Taipei.

126. Chinese Taipei may wish to consider reforms in this area to yield returns from the considerable investment it already makes in collecting performance information and also to realize the potential benefits from green and gender budgeting.

## Consider All Forms of Expenditures

127. Public spending comes in many forms. This includes appropriations authorized in the annual budget, expenditure authorised in standing legislation (“entitlements”) and expenditures authorized in tax legislation (“tax expenditures”). In addition, governments carry out significant activity through loans, guarantees and other contingent liabilities that will – or may – have future budgetary implications.

128. Chinese Taipei limits the use of tax expenditures and favours the use of direct spending as a policy instrument. The few tax expenditures in place are listed in the annual budget documentation with their estimated fiscal impact. There is a similar conservative approach to the use of loans and guarantees. Only one significant guarantee is in place. Very detailed information on this guarantee is presented in the budget documentation.

## Line Departments as Partners

129. Line departments play a crucial role in the budget process. Top-down expenditure ceilings are built on the concept of giving line departments more room to reallocate among their various programs while remaining within the same overall ceiling. They will have ownership over their actions. They are also crucial to maintaining multi-year expenditure baselines and managing robust performance information and spending reviews. In short, all aspects of modern budgeting require line departments as partners. In order to do so, they need to have the capacity to do so.

130. In Chinese Taipei, there is no such capacity in line departments, in the sense that line departments have ownership over the function. Rather, the DGBAS units in line departments fulfil this role. As has been described previously in this report, the role of these varies tremendously. They are very much focused on budget implementation (internal control) rather than providing strategic advice to departments. Reallocation is uncommon.

131. Chinese Taipei may wish to consider detaching the budget formulation function in line departments from the DGBAS units in line departments. (The DGBAS units would continue their focus on budget implementation, internal control.) This would give line departments ownership over the budget formulation function, they would no longer be treated at “arm’s

length.” This would support – and may in fact be a pre-requisite for – a culture of reallocation in line departments. This could be implemented in a number of ways.

## Budget Transparency

132. All revenues and expenditures, assets and liabilities should be reported in a comprehensive, timely, routine and reliable manner. Financial reports should be produced in accordance with generally accepted accounting practice. The government should endeavour to make this information available in a user-friendly manner and should promote awareness of fiscal issues among the public and key stakeholders.

133. There is a very high standard of budget transparency in Chinese Taipei although information on public finances may appear rather dispersed to a casual user. There is nonetheless an exemplary level of fiscal literacy by the public and key stakeholders.

134. The government endeavours to produce its (accrual) financial statements in line with international accounting standards. The actual standards in use in Chinese Taipei are however set internally by DGBAS and may deviate from international standards.

135. Chinese Taipei may wish to consider establishing an independent accounting standards board, or independent accounting standards advisory board, rather setting the standards internally.

## Effective Budget Oversight

136. The legislature should provide for an inclusive, participative and realistic debate on budgetary choices by offering key opportunities for the parliament and its committees to engage with the budget process at all key stages of the budget cycle. It should have the necessary analytical capacity to engage in the budget process in a meaningful manner.

137. Although it may not increase any appropriation, the Legislative Yuan has a strong influence on budgeting in Chinese Taipei. It promotes expenditure discipline. It was its initiative that the two most recent fiscal responsibility laws were enacted. It demonstrates this clear will by reducing total spending in the budget proposal each year.

138. The Legislative Yuan has three full months to scrutinize the budget in detail. The actual scrutiny by the committees of the Legislative Yuan is however minimal. No outside groups or experts are invited to appear before the committees. They seem to rely to a large degree on the conclusions of the Budgetary Information Center, its strong analytical arm, and the Audit Office.

139. The Legislative Yuan may wish to consider extending the time committees devote to scrutinising the budget of the various Departments. This could also be an important opportunity to extend public engagement in the budget process by inviting citizens groups to appear before the committees. An enhanced role for sectoral committees would also be an impetus for the further development of robust performance budget information as they would likely be a principal user of such information.