IMF SEMINAR ON
"INSTITUTIONS FOR FISCAL CREDIBILITY
FISCAL POLICY RULES AND FISCALS COUNCILS
EXPERIENCE AND PROSPECTS IN THE ASIA-PACIFIC REGION"
12 JUNE, 2014
TOKYO, JAPAN

SESSION 3
FISCAL COUNCILS:
ADVANCING CREDIBILITY THROUGH ACCOUNTABILITY AND TRANSPARENCY

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Outline

- Fiscal Governance
- Challenges in Public Financial Management
- Rationale for Fiscal Policy Committee (FPC)
- Mandate of FPC
- Achievements of FPC
- Challenges

FISCAL GOVERNANCE

Malaysia uses a judicious mix of laws, regulations, rules and guidelines to ensure sound public finances.

- **FEDERAL CONSTITUTION**
- **FINANCIAL PROCEDURE ACT 1957 (REVISED 1972)**
- **DEVELOPMENT FUNDS ACT 1966**
- **TREASURY INSTRUCTIONS / CIRCULARS**
- **SELF-IMPOSED RULES / GUIDELINES**

Legal Provisions.... *(not exhaustive)*

- **Article 97 Federal Constitution – Consolidated Fund (all monies and revenues raised by the Federation goes into the Consolidated Fund;**
- **Article 96 Federal Constitution – No taxation unless authorised by law;**
- **Article 98 Federal Constitution – Charged Expenditure (eg. expenses on pensions, debt service charges, payments to States are provided by law and charged to the Consolidated Fund);**
- **Article 111 Federal Constitution - States not authorized to borrow except from Federal Government;**
- **External Loan Act 1963: foreign borrowing by Federal Government capped at RM35 billion;**
- **Loan (Local) Act 1959 / Government Funding Act 1983 – caps domestic borrowing by Federal Government to 55% of GDP;**

Legal Provisions….*(not exhaustive)*

- **Treasury Bill (Local Act) 1946 – caps issuances of Treasury bills to RM10 billion;**
- **Exchange Control Act 1953 and subsidiary legislations – governs private sector borrowings, including NFPEs. Approval from Central Bank required if borrowing exceeds RM100 million.**

Guidelines….*(not exhaustive)*

- **Guidelines observed in the preparation of Development Plans include**:
  - ✓ Overall deficit within 3.0% of GDP by 2015;
  - ✓ Balanced budget by 2020;
  - ✓ Debt service charges within 15% of revenues;
  - ✓ Total Federal Government debt within 55% of GDP;
  - ✓ Federal Government external debt capped at 10% of GDP;
  - ✓ Maintain operating surplus ie. revenues to exceed operating expenditure.
- **Fiscal prudence observed in external borrowings and limited to the following reasons:**
  - ✓ For productive purposes ie to finance development expenditure only;
  - ✓ Maintain market presence;
  - ✓ Benchmark for corporate sector borrowing;
  - ✓ Promote Islamic finance.

Budget Controls

Parliamentary Control

- Annual Budget
- Public Accounts Committee (PAC)
- Federal Audit

Treasury Control

- Budget Examination / Allocation of funds / Monitoring / Circulars

Line Ministry / Agency Control

- Laws, Regulations and Treasury Instructions
- Internal Audit
- Vote Book and Other Internal Controls

Challenges in Public Financial Management

- Lack of fiscal flexibility;
- Narrow revenue base;
- Unsustainable Government Expenditure;
- High debt level;
- Lack of efficiency and quality in Government procurement;
- Poor governance and weak fiscal institutions.

"……….the Government is fully committed to strengthening public finances to ensure the nation's long-term fiscal sustainability. Towards this end, we will set up a ***Fiscal Policy Committee*** chaired by myself with selected cabinet members and heads of departments. This committee will be served by a ***Fiscal Policy Office*** in Treasury"

Hon. Prime Minister
Budget Consultation 2014
18 June 2013

Rationale for Fiscal Policy Committee

Part of a year-long Treasury Transformation Programme (2013) aimed at:

- **sharpening MOF's role by re-focussing on core business: financial and economic management, revenue, budget and investments;**
- **re-asserting leadership in formulating fiscal policy, strategies and discipline – responsible for overall fiscal management;**
- **Re-engineering key processes within MOF (eg. Procurement, Administration);**
- **Investing in talent management;**
- **Inculcating a culture of high performance and solution-oriented across MOF.**

Mandate of FPC

To play a leading role in strengthening public finances, ensuring fiscal sustainability and long-term macroeconomic stability through:

- endorsing guiding principles for the conduct of fiscal policy;
- Approving the medium-term fiscal strategy;
- Reviewing Government's fiscal performance *vis a' vis* the MTFF;
- Endorsing policies to meet fiscal targets and the management of risks;
- Ensuring alignment across Ministries and agencies on fiscal issues, discipline and compliance.

Features of FPC….*cont.*

- High-level, powerful, decision-making, executive body;
- Permanent members are :
  - ✓ Prime Minister – Chair
  - ✓ Deputy Prime Minister
  - ✓ Minister of Finance
  - ✓ Minister of Economic Planning Unit (EPU)
  - ✓ Chief Secretary to the Government
  - ✓ Secretary-General of Treasury
  - ✓ Director-General of EPU
  - ✓ Governor of Bank Negara Malaysia (Central Bank)
- Reps of various Ministries / agencies to be incorporated, if necessary;
- To meet at least twice a year - August, February;
- Supported by a Fiscal Policy Office (FPO) within MOF and works closely with Central Bank and Economic Planning Unit.

Features of FPC

- FPO to provide technical/analytical guidance in fiscal policy formulation; produce fiscal forecasts; monitor performance at macro level; and facilitate collaboration between MOF and other Government agencies;
- While it has operational independence, the FPC is not a stand alone entity, independent of partisan politics. Watchdog?;
- FPC has no legal backing, no sitting academics but draws its members from serving politicians and high ranking, eminently qualified civil servants;
- Hence, it is a hybrid of sorts - part executive, part partisan, still evolving;
- Nevertheless, the FPC has clout as it is helmed by the PM – the ultimate authority in decision making;
- FPC complements and reinforces rules, regulations and legislations in place to promote sound public finances.

Achievements of FPC….*cont.*

Although still in its infancy, the FPC, supported technically by the FPO, has made major decisions since 26 August 2013 (1st meeting):

- Fuel subsidy rationalisation – announced on 3 September 2013;
- Sugar subsidy was abolished (Budget 2014 tabled on 25 October 2013);
- Toll concession extended instead of paying compensation to toll operators;
- Implementation of GST at 6% effective 1 April 2015 with mitigating measures for targeted groups (Budget 2014);
- Real property gains tax (RPGT) was increased to curb speculation and address housing affordability issue (Budget 2014);
- Cost cutting measures instituted for operating expenditure (2014);

Achievements of FPC

- **Procurement rules tightened by reducing threshold for direct purchase and the use of schedule of rates in works-related procurement;**
- **Cash transfers to targeted groups increased while work is underway to introduce a comprehensive social safety net in 2015 (Budget 2014);**
- **Bank-in mechanism introduced for cash transfers to targeted groups;**
- ***Targeted fuel subsidy mechanism (on-going);***
- ***Medium-Term Fiscal Framework (on-going);***
- ***Fiscal Strategy Report (on-going);***
- ***Single window through EPU for the submission/approval of DE projects, including PPPs (on-going).***

Challenges

Moving forward:

- **Effective communication strategy – commit to a calendar of meetings, like Monetary Policy Committee, to send a message to the markets;**
- **FPO to undertake independent and rigorous technical analysis to support FPC;**
- **FPO's ability to work with EPU, and the Central Bank to forge common outcomes;**
- **FPC's role to be rationalised *vis a' vis* Economic Council, Cabinet and National Budget Office to enhance its credibility.**

THANK YOU