

Public Sector Budget: An Overview

Zuhariah Husin

ABSTRACT

The public sector budget, tabled in Parliament every year, plays an important role in resource allocation towards achieving some public values. The importance of the budget is further stressed by the legal requirements for the preparation of budget. The main components in the budget are revenues and expenditure and presently every two years public sector entities have to go through the budget process, which starts in January and ends in December. A number of budget issues such as program evaluation, problem of shortfall, two-year budget and budget deficits seem to attract continuous debates and discussion amongst the concerned parties.

Introduction

Several parties with bated breath have always awaited the Federal government budget presented in Parliament every year. The business community fervently pray for more tax incentives and no increment whatsoever in any kind of taxes, the civil servants anticipate at least a month's bonus to be announced and other concerned parties just hope for the best in the budget. There appears to be different kinds of expectations from the general public before the Finance Minister announces the budget. Furthermore, the public sector budget also touches the lives of all Malaysians with its programs and activities. As such it is the objective of this paper to give an overview of the public sector budget by looking at the legal requirements for budget, the components of budget, the budget process and ends with issues in budget.

Legal Requirements

Budget has always been the most important financial tool in the public sector. It is used as an instrument to allocate public resources towards achieving some public values. This is further stressed by a number of legal requirements for the preparation of budget. These requirements are provided in the Federal Constitution, Financial Procedure Act 1957, Treasury Instructions and Treasury Circulars.

i. Federal Constitution - Article 99 and 101

Article 99(1) of the Federal Constitution requires a statement of the estimated receipts and expenditures of the Federation in respect of every financial year to be laid in Parliament before the commencement of that year. Article 101 touches on a supplementary estimate to be laid before the House of Representatives in the event of amount appropriated by the Supply Act is insufficient or for expenditure in which no amount has been appropriated.

ii. Financial Procedure Act 1957 - Section 15

Section 15 states that the estimates of expenditure prepared are required to show clearly the divisions and sub-divisions of expenditure proposed, the amount expected to be received or spent for the year and the purpose of such expenditure.

iii. Treasury Instructions no. 29 – 51

Treasury Instruction no. 29, for instance, states that the preparation of estimated revenue and expenditure for the Federal and States is the responsibility of the Secretary General to the Treasury and State Financial Officer respectively.

Components of Budget

The main components of the public sector budget comprise of revenues and expenditure. According to Haslinda Yusoff et al. (2003), revenues of the Federal Government consist of tax revenue, non-tax revenue, non-revenue receipts and revenue from Federal Territories.

Tax revenues are revenues from duties and tax imposed by law and can be categorised as direct tax revenue and indirect tax revenue. Direct tax revenue includes income tax, stamp duty, petroleum tax, property gains tax and film hire duties. Indirect tax revenues include sales tax, receipts from import and export duties, service tax and levy on goods and vehicles leaving peninsular Malaysia.

Non-tax revenues are revenues to the government not in terms of taxes. These include receipts from registration payments, licenses and permits, receipt from sales of goods, rent, interest and returns on investment locally and abroad, penalties etc.

Non-Revenue Receipts are all repayments from expenditure; inter-departmental credits, repayments and contributions from other government departments, statutory bodies or government companies and receipts from Federal Territories. Refunds of expenditure include refunds of salary on resignation and refunds of training expenses. Receipts under this category include all repayments of expenditure such as refunds of salary on resignation and refunds of training expenses, inter-departmental credits, repayment of excessive payments or errors in earlier years, repayments and contributions from other government departments, statutory bodies or government companies. It also includes receipts from Federal Territories.

Revenue from Federal Territories consists of tax and non-tax revenues collected on behalf of the government. These include receipts from licenses and permit; quit rent,

sales of assets, rentals, service fees and entertainment duties.

Meanwhile public sector expenditure can be divided into Operating Expenditure and Development Expenditure as depicted in Figure 1.

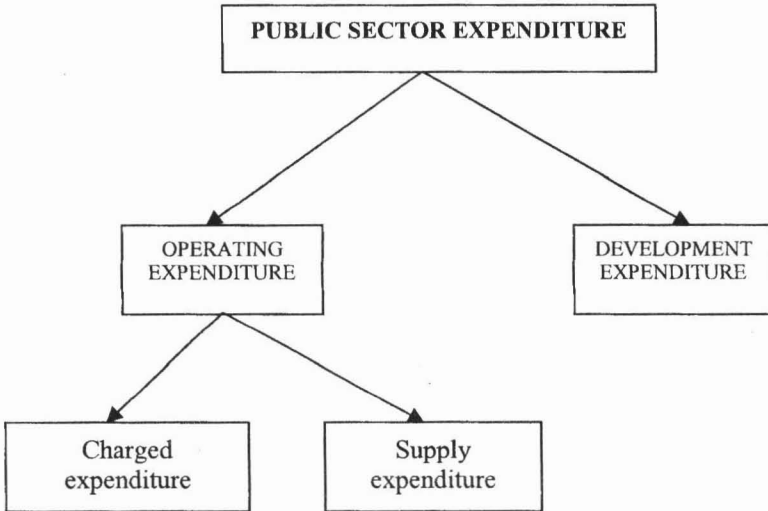


Figure 1: Public Sector Expenditure

Operating Expenditure

The public sector expenditure is divided into operating expenditure and development expenditure. The operating expenditure is further split into charged expenditure and supply expenditure. Charged expenditure as per Article 98 (1) of the Federal Constitution includes all pensions, compensations for loss of office and gratuities for which the Federation is liable; all debt charges, and all moneys required to satisfy any judgment, decision or award against the Federation by any court or tribunal. As for supply expenditure, it represents all charges to the budgeted allocation such as payment for emoluments, goods and services, contribution to Development Fund and Housing Loan Fund and allocation to State

Government, Statutory Bodies and Government-owned Companies by way of grants, loans and investment. Supply expenditure must be approved by Parliament before its incurrence, which is in contrast to charged expenditure that requires no Parliamentary approval.

Development Expenditure

Development expenditure is the expenditure for development purposes and non-recurrence in nature. It usually involves a large amount of money. Consequently, borrowing on long-term basis either from internal or external financial institutions usually finances the expenditure.

Budget Process

Traditionally, budget is prepared and approved on an annual basis. However, starting from year 2002, with the effect of Treasury Circular No. 2/2001, the budget preparation process will be carried out once every two years instead of annually. The budget process at the Federal level is shown in Figure 2.

Budget process at Federal Level

In summary, the budget process starts in January with Treasury issuing call circulars to all ministries and agencies requesting for the submission of budget proposal for the following year. In March, Budget Review Officers of the Budget Management Division at Treasury would hold discussions with all government agencies relating to the budget proposal. In April the budget examination process is carried out. This session which includes preliminary budget hearing and actual budget hearing also involves central agencies such as the Public Service Department and Economic Planning Unit. In July the budget for all Federal government entities will be compiled. The Finance Minister and the cabinet will approve the budget, after which it will be printed and

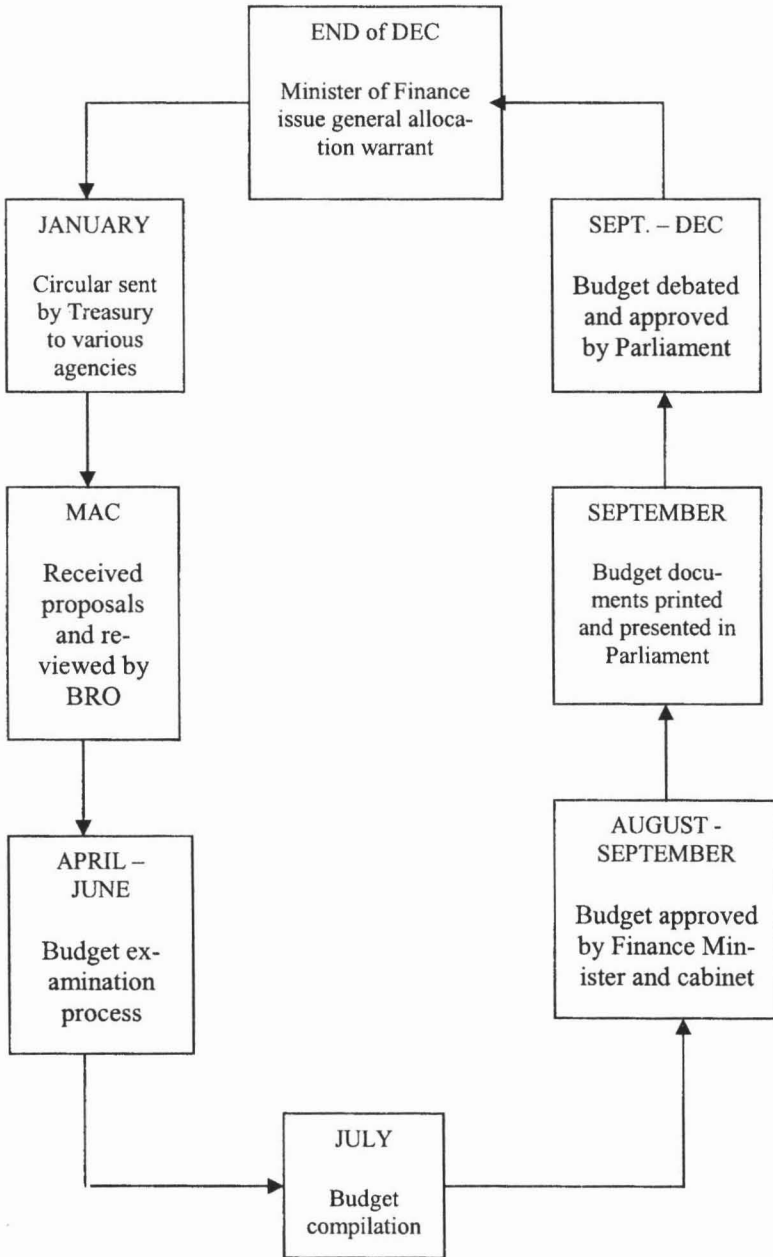


Figure 2: Budget Process at Federal Level

tabled in Parliament. From September to December the budget will be debated and eventually approved by Parliament. It will then be forwarded to the Yang di-Pertuan Agong for royal consent and gazette. The Minister of Finance will then issue general allocation warrant to the Accountant General's office as an authority for the Accountant General to utilize the Consolidated Fund required for expenditure.

Issues in Budget

The debate and discussion on budget seems never ending especially among those who are greatly affected by it. To satisfy every party in the budget is a difficult task, therefore, the government just has to take into account priorities that best serve the public interest. Hence, this gives rise to a number of issues in budget.

Program Evaluation

One of the elements under the Modified Budgeting Technique is program evaluation, which refers to an in-depth examination of programs undertaken by public sector organisations. Every public entity that has been allocated the resources to carry out the specific identified programs in a particular year is required to carry out program evaluation exercise at the end of the year. The evaluation is of great importance since it provides feedback on the efficiency of program planning by government managers. The decision flowing from these evaluations would provide the basis for annual adjustment to expenditure target set by the Treasury. However, public sector entities appear to be complacent in carrying out the program evaluation. This could be due to the lackadaisical attitude of some government managers since the evaluation does not require an external evaluator. Furthermore, the Treasury imposes no penalty for failing to perform program evaluation.

Problem of Shortfall

Under the Traditional Budgeting System technique, previously used in Malaysia, the government managers are led to believe that an important objective is to spend exactly the amount budgeted, and that if this amount is not spent, the following year's appropriation will be cut. This led to wasteful end-year surges evident in the past (Handyman, Jones and Pendlebury 2003). In addition, this practice offers little incentive for them to economize. As such the budget requested tend to be inflated by government managers. It seems that the practice mentioned earlier still exists under the currently in use Modified Budgeting System. This resulted in a shortfall, which indicates inefficient planning of programs and activities. As a consequent, allocation of public resources is not utilised fully. This bodes ill for government managers since the amount could be allocated to other public entities, which is in dire need of the resources.

Two-year Budget

As mentioned earlier, with the effect of Treasury Circular No. 2/2001, the budget preparation and examination process will be carried out once every two years. However, the change is purely administrative and does not involve any amendments to the existing legislatures. Among the rationales for the two-year budget is to help increase the quality and efficiency of budget allocations. With government spending determined two years ahead, the new process facilitates the assessment on the fiscal position of the government and, hence, improves cash flow planning and management. Accordingly, resources such as manpower, time and money both at the Treasury, ministries and government agencies for budget examination purposes will be reduced but I beg to differ. The question here is - is that so? According to one government officer who has been in service for many years, the two-year budget is not as rosy as it was made out to be. Manpower, time and money are still needed from time to time for revisions to the budget.

Budget Deficits

The emergence and persistence of large public sector budget deficits in many countries in the last two decades has generated widespread concern that policymakers may be keen on resorting to “excessive” deficit financing (Corsetti and Roubini 2001). Malaysia is also not spared this phenomenon of budget deficits. This is a reason for worries among concerned parties. For the past few years, the federal government budget has shown more expenditure compared to revenues. The long-term budget target of the government is to achieve surplus budget. However, in the medium term the government is going for prudence financial management with a pro-development strategy to gradually reduce the deficit for a balanced budget. In the meantime, according to one Treasury official, even though some quarters of the public are a bit skeptical on the budget deficits, the government due to the current economic climate needs to continue with the strategy of budget deficit where only development projects will be financed by borrowing.

Conclusion

There is a legal requirement for the budget to be prepared and presented in Parliament annually. The budget process which involves all public sector entities is carried out once every two years among others is to help increase the quality and efficiency of budget allocation. Despite several issues raised in relation to the public sector budget, in my personal view it continues to be the most important financial tool especially in allocating financial resources for the benefit of the public.

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ZUHARIAH HUSIN, Faculty of Accountancy, Universiti Teknologi MARA Pahang.
zuhariah@pahang.uitm.edu.my