

THE MAGNITUDE OF PUBLIC ACCOUNTS COMMITTEE'S (PAC'S) WORK IN REVIEWING AND REPORTING ON STATE GOVERNMENT'S FINANCIAL STATEMENTS

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Abstract

This paper examines the function of the Public Accounts Committee (PAC) of all the eleven states in Peninsula Malaysia. The concept of PAC oversight exists as an essential effect to the legislature's process, where oversight function compliments rather than hampers the effective performance of financial accountability with which the executive is entrusted. A preliminary study was carried out on one 2005 PAC Report of a state and it was found that the Report was made based on the 2002 audited financial statements. Further analysis on the 2005 PAC Report of the other ten states reveals that the PAC Reports of all these states were outdated because they review non-current audited financial statements. Some states even reviewed and made reports on a few years' financial statements concurrently. Thus, the significance of the PAC Report is at stake as the comments and recommendations made might not be relevant.

Introduction

In addition to performing legislative function (which is law making) Public Accounts Committee (PAC) has oversight tasks, and thus, acts as oversight mechanism in the states. PAC generally oversees the integrity, economy,

efficiency and effectiveness of government financial management by examining state government's financial statements, other related documents and considering AGO Reports. This permanent committee (or sometimes called standing committee of the legislature) holds close meetings or hearings to examine the government's implementation of the laws by means of reviewing the financial statements and the Auditor General (AGO) Reports; call up witnesses; and finally produce the PAC Reports (Mulgan, 2002; Bovens, 2005).

In this paper, we aim to comprehend the work of Malaysian states PAC and the extent that committee work as a whole, reflect the pattern of PAC activity feature of the rest of the states. It is our intention to shed light on this reservation through comparative cross state analysis of PAC Reports. Results presented in this paper were from analysis made on PAC Reports tabled at State Legislative Assembly (SLA) in the year 2005. Research could therefore, draw only initial conclusions regarding the work of PAC in reviewing and reporting on state financial statements. Our main summary concept, institutionalization of PAC, is a means to understand the extent or magnitude to which the PAC and the activity of PAC became established in the state legislature.

The findings from the study suggest that although AGO provides assurance to SLA and the public through Audit Reports, because of the delays in PAC reporting, the execution and the implementation of any PAC recommendations based on issues highlighted earlier by the AGO is a problem. Consequently, corrective actions over matters which should have been long dealt with so that they do not re-appear in future AGO's Reports recur. This paper begins with some literature review on the establishment of PAC. It will then look into Malaysian states' PAC work of reviewing and reporting on financial statements; issues emerging from the analysis; and finally, suggesting appropriate recommendations for consideration.

Background of Study

Jones and Jacobs (2005) in describing the system of parliamentary government maintain that it is derived from the British system, and passed on by the British to its former colonies. As inheritor of such systems of government, many countries normally have some type of PAC as part of their structure (McGee, 2002; Stapenhurst, Saghal, Woodley and Pelizzo, 2005). Such establishment had been replicated in almost all Commonwealth and also many non-Commonwealth countries such as Australia, South Africa, Hong Kong, Canada, Denmark and many others. Pelizzo, Stapenhurst and Olson (2004) in relation to PAC's establishment suggested that government reporting and legislative scrutiny of public accounts still is more common in parliamentary and semi-presidential legislatures than in presidential systems. Historically, Chubb (1952) identified and proposed two aspects of public finance of the British House of Commons, which led to the emergence of the need for committees such as PAC or the like. These two aspects were:

- a. The question of policy i.e. what shall be the amount of taxation and expenditure and to what objects public money shall be applied. This policy is vital but to view the House as only a grand forum for debate or just as a legislative production line, is to miss other important but less exciting aspects of its work (as in b); and

- b. To ensure that the policy (though it is the government's in origin, it endorses and makes its own) shall be carried out accurately, faithfully and efficiently.

Along these lines, Jones and Jacobs (2005) noted that the two aspects of parliamentary interest and responsibility for financial matters as identified by Chubb (1952) have not substantially changed. Firstly, legislature in terms of PAC, to some extent has continued to play a role in oversight and control. As an accountability machinery, PAC still exists in the same form as before. Secondly, tension that exists between state executives and the legislature, which is inherent in any parliamentary system, still subsist as before. This is because the executive branch often sees legislature as merely the place where legislation to implement their policies is passed (Krafchik and Wehner, 1999; Neal, 2003; Mendel, 2004) when actually, legislature is also the institution from which executives derive their mandate to govern (Weller, 1997).

Under parliamentary systems of government, PAC seems better equipped to allow legislature to closely scrutinize supply bills and oversee the government's programmes (Wood and Waterman, 1993; Pelizzo et al., 2004). Nonetheless, according to Wehner and Byanyima (2004), the legislature requires a strong committee because effective legislative committees are the "engine room" for the creation of laws. This is because legislature and other accountability institutions such as the AGO are mutually dependent on each other in order to be fully effective. While PAC depends on high quality audit reporting to be effective, the AGO in turn requires effective laws to ensure that the state executive takes audit outcomes seriously.

Underpinning the establishment of PAC are two related theories, namely the agency theory and the accountability theory. Literature on control by the legislature holds that legislators were inadequately reactive, in monitoring bureaucratic or executive behavior (Huntington, 1973; Ogul, 1976). Fiorina (1977) argued that lack of strong incentives to be more attentive has to be balanced against costliness of careful oversight monitoring. In this sense, not only does there exist potential agency problems but these problems may in turn, extend into issues of accountability.

This is quite true as legislature being the principal, delegates authority to the executives or the state government as the agent, who is then held to account for their conduct and performances. In this sense, the PAC-Executive relationship is concerned with performance accountability (Stewart, 1984). Another conceptual view of accountability, associated PAC establishment is the case of political form of accountability (Glyn, 1987; Strom, 2000). Regardless of the forms, with PAC's overseeing functions, it ought to be able to promote better governance within the financial accountability framework.

Shick (2002) proposed that rather than act as controller of public finance, legislature in general should aim to promote fiscal discipline, improve the allocation of public money and stimulate public bodies to manage their financial operations more efficiently. In order to do this, it is necessary to enhance the legislative capacity, particularly the PAC, to deal with the financial related issues (McGee, 2002; Shick, 2002; Loney, 2004).

PAC Establishment under the Malaysian System

Under the Malaysian context, the committee of legislature in the form of PAC has been in existence since 1900s. As a standing committee of the State Legislative Assembly (SLA), the establishment of PAC has been to perform a service to the SLA in making sure that audit queries and comments including those with regards to mismanagement and the like, are noted and PAC's recommendations are carried out accordingly by the state executives.

The PAC members are appointed by the Selection Committee of the SLA as provided under the "Standing Order of the Rules and Regulations of the SLA Meeting". In line with that, the PAC members are appointed as soon as each term of SLA sessions commences. The committee needs to have a chairman and vice-chairman appointed by the SLA, and also not more than three but not less than two other members.

It is to be noted that under the rules, a member of the SLA cannot be appointed as a chairman or a member of the PAC, if he is concurrently an Executive Council member (EXCO). In terms of assistance, the AGO or his representative can be invited to attend PAC's meetings, to observe, hear or with permission of the PAC's chairman, question those who are called upon to answer to the committee. Normally in Malaysia, the Chairman of PAC is appointed from the ruling party. Nonetheless, at least one opposition party member will sit in the committee too.

The need to form the PAC arose due to the provision under Article 107 of the Malaysian Federal Constitution (1957), where it requires the AGO to submit his reports on the national financial statements to the King or the "*Yang Di Pertuan Agong*", who will then order the report to be tabled at the House of Representatives or the "*Dewan Rakyat*". Under the same Article, similarly, at Malaysian state level, the Head of the State will order the AGO's Report to be tabled at the SLA.

In order to review the AGO's Report, and for performing a few related tasks, the *Standing Order of the Rules and Regulations of SLA Meeting* provides for the appointment of PAC members to serve the function of examining:

- that public funds were used in accordance with laws and purpose as endorsed by the budget;
- any accounting of state administrative bodies and other associations that handle state funds tabled at SLA;
- the Auditor General's Report tabled at the SLA as provided by state constitution; and
- any other matters that the PAC or the SLA think should be checked or require close scrutiny or inspection by the PAC.

Financial Accountability Cycle under the Malaysian System

The financial operations of a Malaysian state, including its departments and agencies must undergo certain processes. These subsequent explanations reflect how the

accountability in relation to financial performance of state government is executed in Malaysia (see Appendix I).

Following the implementation of a budget after bills are passed at the SLA, at this first stage, someone has to take control and be accountable to the conduct of such funds. Under this circumstance, the State Financial Officer at the state level (equivalent to a Secretary General of a Ministry at the federal level) is appointed as “controlling officer” of their entity’s expenditure (Treasury Instruction, 1957). The effect of this appointment is that, it clearly places the responsibility for the financial management of a state, on the shoulders of the Controlling Officer.

Subsequently, at the end of each financial year, State Financial Officer being the Controlling Officer needs to ensure that the government accounts are closed and financial statements are prepared to give account of the whole year conducts. Thus, the output at the second stage of accountability process is the annual financial statements prepared and submitted for AGO’s auditing and these are endorsed by the SLA. To this effect, the State Financial Controller will be answerable to “the State Legislature” or the SLA through the PAC.

Later, the auditing process conducted on the annual financial statements by the AGO at this third stage, ensures that government entities entrusted with public money have spent them in accordance to what was passed through the annual budget. The output at this stage is the Auditor General’s Report. The Auditor General Report will also be tabled at the SLA as required under the Malaysian Federal Constitution (1957) and the Audit Act (1957).

Once tabled, the PAC will review and address the issues raised in the AGO’s Report with regards to the annual financial statements. The review process is done through correspondence, hearings, and visits involving the concerned parties that include government departments and agencies. PAC will be reporting back to the SLA in the form of PAC Report, which is the final output of the accountability cycle.

Normally, after the PAC Report is tabled, the secretary of the SLA will hand a copy of the PAC Report to the State Financial Officer for recommendations or corrective actions proposed by PAC, which will be acted upon (Treasury Instructions, 1957).

Methods

Preliminary Studies on Malaysian PAC

Initial information regarding PAC was gathered from all the eleven (11) Peninsular Malaysia state governments’ websites (accessed in July 2006). It was discovered that out of eleven states that have PACs established under the *Standing Order of the Rules and Regulations of SLA Meeting*, only two (2) have proper mentioning of PAC as part of its committee systems, such as acknowledging the existence of PAC; highlighting its functions and power; including the listing of the names, photos and constituents that the PAC members represent.

In order to support the initial observations, a request was made, and one of 2005's PAC Report of a state in Peninsular Malaysia was obtained. The report received indicated that the 2005 PAC Report was made based on the AGO's Report on the state financial statements for the year 2002.

Motivation and Objectives

Based on the preliminary study, the significance of the PAC Report is at stake since it may no longer be relevant since the review was not current. In order to deal with the issue, this paper seeks to look into:

1. Whether the state financial statements of 2005 were timely submitted (state) audited by the AGO, and tabled at SLA.
2. Whether the state audited financial statements of 2005 were timely reviewed and reported by the PAC to the SLA.
3. Identifying possible grounds for setback in PAC reviewing and reporting process (if any), which can indirectly impede the financial accountability process of the state government as a whole.

Research Instrument

All eleven (11) states in Peninsular Malaysia that have a PAC established under their respective *Standing Order of the Rules and Regulations of State Legislative Assembly Meeting* were asked to participate. The use of states' PAC rather than the Federal Government's PAC is to allow better comparisons relatively in terms of power, functions and control.

The states, more specifically the State Secretary Offices, received an introductory letter and also a self-addressed stamped return envelope appealing them to supply the 2005's PAC Report for perusal. In addition, the state offices were informed that their participation was greatly expected and that their reports would remain highly confidential.

The request was made at the end of 2006. As such, it was assumed that under normal circumstances, the financial statements of 2005 would have been submitted and audited by the AGO (Malaysian Federal Constitution, 1957; Audit Act, 1957). Information on the audit certification of 2005 financial statements by AGO was accessible, using the AGO's website.

The PAC related paragraph of the *Standing Order of the Rules and Regulations of State Legislative Assembly Meeting* cautioned that the PAC should be getting a memorandum, prepared and presented by the State Financial Officer regarding actions taken on matters raised in the PAC Report, as soon as possible, before the next PAC meeting discussing the subsequent year AGO's Report is held (Treasury Instruction, 1957). Since an accounting cycle entails one financial year, the financial statements of 2005 were supposed to be reviewed and reported on by PAC by the end of 2006 or in early 2007, after the AGO's Report was tabled at the SLA.

In this study, instead of asking when the PAC Report on the 2005's financial statements was tabled, the PAC Report of 2005 was used as the basis for examination. The accounting year of the financial statements reviewed in the 2005's PAC Report helped in revealing whether the 2005's annual financial statements were timely reviewed and reported by PAC to the SLA. Indirectly, such information also provides indication on the time elapsed in PAC review and reporting work on the state's financial statements.

Results

Data Collection

Of the eleven (11) Peninsular states where letters were sent to; all states responded and are identified as state A to state K in the analysis. The 2005's PAC Reports received clearly stated certain information including the accounting year of the financial statements reviewed and reported by PAC, the date that the PAC Report was tabled at SLA and other related information.

Analysis

1. Use of Different terms

It can be seen in Table 1, although the states' PAC terms of reference are similar (based on the *Standing Order of the Rules and Regulations of SLA Meeting*) PAC had various names across states. For example, some states referred to PAC as "*Jawatankuasa Kira-Kira Wang Negeri*", whilst others termed it differently as shown in Table 1. This reflects that there is no consistency in the use of terms across states. The state PACs were formed in accordance with the respective state *Standing Order of the Rules and Regulations of SLA Meeting*.

2. Non-uniformity in Report Format

It was also noted from the PAC Reports gathered that there was no standard format for presenting the report. Each has its own layout with a number of pages ranging from seven to more than seventy. Without uniformity in PAC report presentation, comparison for the purpose of improving or benchmarking of PAC between states and Federal Government's PAC would not be possible.

3. Ratio of PAC Members to State Assemblymen

Table 2 shows the number of PAC members appointed by states from amongst the non-Executive Councillor (non-EXCO) members of the SLA. Composition of the number of PAC members at respective states ranges from five (5) to ten (10). Surprisingly, small states like A, G, and C comprise the largest percentage of members of the SLA sitting as PAC members with 33.33%, 25% and 25% respectively. Comparatively, states with larger representatives like both H and E only have 12.5% of their members of SLA sitting on the committee.

Table 1: PAC Established at State Level

State	Terms Referred to PAC	Legislation
A	Jawatankuasa Kira-Kira Wang Negeri	Perkara 101A Peraturan Mesyuarat dan Perintah-Perintah DUN
B	Jawatankuasa Kira-Kira Wang Negeri	Peraturan 75(1) Peraturan-Peraturan Mesyuarat DUN
C	Jawatankuasa Kira-Kira Awam Kerajaan Negeri	Peraturan 109A Peraturan-Peraturan DUN
D	Jawatankuasa Kira-Kira Wang Negeri	Perkara 70 Perintah-Perintah Tetap Dewan Negeri
E	Jawatankuasa Kira-Kira Wang Awam	Peraturan Tetap 76(5) DUN
F	Jawatankuasa Kira-Kira Awam Kerajaan Negeri	Peraturan 109A Peraturan-Peraturan DUN
G	Jawatankuasa Kira-Kira Wang Negeri	Peraturan 26 (1) Peraturan Mesyuarat DUN
H	Jawatankuasa Kira-Kira Raya Negeri	Fasal 110 Peraturan-Peraturan dan Perintah Tetap Dewan Negeri
I	Jawatankuasa Kira-Kira Wang Negeri	Peraturan 68 Peraturan Majlis Mesyuarat DUN
J	Jawatankuasa Kira-Kira Wang Negeri	Fasal 110(1) Peraturan-Peraturan dan Perintah Tetap DUN
K	Jawatankuasa Kira-Kira Wang Awam	Peraturan 110 Peraturan-Peraturan dan Perintah Tetap DUN

* DUN – Dewan Undangan Negeri

Table 2: State PAC Members

State	PAC Members	SLA (Seats)	Percentage (%)
A	5	15	33.33
B	5	36	13.89
C	10	40	25
D	7	59	11.86
E	7	56	12.5
F	7	36	19.44
G	7	28	25
H	7	56	12.5
I	7	42	16.67
J	7	32	21.88
K	7	45	15.55

The composition of members appears important if we were to associate the number with the quality of oversight role that the PAC member is supposed to play. What comes to our mind may include issues such as whether the formation of PAC, including the appointment of members is really important to the SLA, and the state government; or was the appointment done simply to comply with the regulatory requirements. It is also crucial that the PAC members appointed are able to sufficiently and effectively involved in carrying out the prescribed role and functions as PAC members.

None of the chairman of a PAC comes from the opposition party. This is inconsistent with the suggestions of the Handbook of Best Practices (Wehner, 2002) whereby the chair of the PAC should be occupied by member of the opposition party. State F, H and I do not have even a single opposition member sitting as a committee member of the PAC. Regardless of whether the state was ruled by the ruling or opposition party, it did not have a balanced representation of all major political parties. For example, though state K has a balanced number of seats between the ruling party and the opposition, only one member of the opposition was appointed to sit on the committee. On the other hand, in states F, H, and I where the opposition has won only one seat at SLA, none of the opposition was chosen as a member of the PAC.

4. *Submission of Annual Financial Statements*

Table 3 shows whether the state government's financial statements of 2005 were timely audited. For all states that participated, the audit certification made by the AGO on the financial statements of 2005 took place within the year 2006. This is in line with what is required under Article 107 of the Malaysian Federal Constitution 1957, which provides that the report of the AGO relating to the accounts of the state, needs to be submitted to the Ruler or *Yang Di Pertua Negeri* of that state, who then shall cause it to be laid before the Legislative Assembly. Being so, it can also be concluded that the 2005's annual financial statements of the state governments were timely submitted for audit purpose.

Table 3: Audit Certification of 2005 Financial Statements

State	Date of Certification of 2005 Financial Statements
A	20 July 2006
B	8 June 2006
C	30 June 2006
D	4 August 2006
E	14 July 2006
F	26 June 2006
G	2 August 2006
H	8 August 2006
I	27 July 2006
J	19 June 2006
K	19 June 2006

5. *Delay in Review of Audited Financial Statements by PAC*

The following Table 4 shows that the PAC Reports of certain states were not tabled in a timely manner at the LA. Based on the PAC Reports tabled in year 2005, there were some serious delays. State A, for example, has the PAC Report on financial statements of 1997 and 1998 being reviewed, reported and tabled concurrently at SLA in 2005; whilst state C and state H did not table any PAC Report at the SLA in 2005. Their latest financial statements reviewed by 2005 were for the 1999 and 2000 financial statements.

Taking into consideration that the AGO's Reports of 2005 financial statements were produced in a timely fashion (as shown in Table 3), it seems that the delay in PAC Reports was not caused by the AGO.

6. Concurrent Review of Audited Financial Statements

There was also a tendency by PAC in reviewing and reporting on a few years' state financial statements concurrently. PAC is supposed to review and report on the financial statements based on the issues raised in the AGO's Report on the related financial statements. With the setback in PAC reporting, reviewing and recommendations by the PAC this occurs years after the real events had taken place. Hence, corrective actions, penalties or punishment recommended would be too late.

Table 4: Latest Audited Financial Statements Reviewed by PAC and Tabled at DUN by 2005

State	Latest Audited Financial Statements (Year) Reviewed and Reported by PAC at SLA by 2005	Elapsed Period
A	1998	7 years
B	2002	3 years
C	1999	6 years
D	1997	8 years
E	2002	3 years
F	2002	3 years
G	2003	2 years
H	2000	5 years
I	2003	2 years
J	2002	3 years
K	2001	4 years

Conclusions

Writers expect initial findings in this paper to make a contribution to the process of improving the financial accountability cycle and government information delivery systems as a whole. The initial findings need further probe into the reasons for the untimely reporting by the PAC at the moment. The analysis made led to the following inferences, giving rise to some important issues:

1. PAC Non-review of Current Audited Financial Statements

Although the review and reporting process were done by PAC, the gap in time between AGO's audit work and the PAC Reports ranges between two (2) to eight (8) years. Hence, the significant findings highlighted by AGO that should have come under PAC's attention may no longer be relevant due to the elapsed time. Timely PAC reporting is essential as improved overseeing role by PAC, including timely report issuance, may enable the SLA to question the government's decisions and actions more effectively during the SLA sessions. Neal (2003) in her report to the Commonwealth Parliamentary Association, cautioned the consequence of reacting too late towards the findings in the AGO's Report.

2. PAC's Recommendations are Probably Outdated

Our findings are consistent with findings in other studies by Wehner (2002), Neal (2003) and Stapenhurst (2004). Authors have cautioned that one weakness in many countries that have PACs is that, despite debates in the chamber of the legislature and reports to the executive, the government often fails to address the issues raised in the recommendations of the AGO.

3. Follow-ups on AGO's and PAC's Recommendations

Based on the Malaysian Federal Constitution (1957), the Audit Act (1957) and also the *Standing Order of the Rules and Regulations of SLA Meeting*, the AGO and the PAC do not have enforcement power on state executives' divergence from the acts, rules, and regulations passed by the SLA (Hazman Shah, 1991). Thus, the state executives are the ones who have the authority to take corrective measures or impose punishment on officials regarding delinquent acts found in the financial statements. With the delay in reporting, the enforcement of findings and recommendations leads to integrity problems identified by AGO and the PAC, and takes a long time to be addressed, acted upon by the executives, resulting in the lack of sanctions to ensure compliance.

4. Authorities' Awareness of the Delay and Initiatives Taken

Since results showed that there existed serious delays in PAC reporting in some states, it is an indication that the PAC members, in particular, and members of the SLA in general, were unacquainted with the accounts, and the importance of timely PAC reporting.

As such, it is only appropriate that the question of who is responsible to monitor should be raised by the general public. Improved PAC reporting by the concerned parties is important as failure to do so would not make it easy to come to an agreement as to who would be responsible when matters regarding government financial affairs fall short, and a considerable amount of time, public money and human resource are wasted as a result of deficient or lack in accountability in reporting.

Recommendations

At this stage, the following recommended steps need to be taken:

- In addition to the SLA, the government or the executive needs to be alerted of the situation. They need to be made aware of the importance of having the state financial statements reviewed and reported to the SLA by the PAC as soon as possible. Since the financial statements produced each financial year need to be audited by AGO, the PACs need to expedite their review work on the latest AGO Reports before the subsequent year's AGO Reports are issued for review.

- The reasons affecting the accountability process from taking place smoothly, in this case the untimely PAC reporting, need to be identified and subsequently minimized in order to ensure the use of state funds is safe-guarded against abuse, waste, and fraudulent activities.
- Capturing the reasons for the lag at any stage in the accountability cycle is crucial, as remedial actions or recommendations need to be taken expeditiously and effectively. For example, when it is clearly shown that a state officer may have failed in his duties regarding public expenditure or failed to act in accordance with the code of ethics or the rules laid down, this could result in bigger problems in the future.
- Improved PAC's composition, capacity, and also work process may give a boost to PAC in terms of their work and reputation. A strong PAC of the SLA could emerge as a structural solution to the need of each party in the coalition government, including the opposition, to monitor the behavior and actions of the state executive. Lacking effective accountability and reporting systems, the malfunctioning of overseeing body may cause the public to continuously see cases of public funds being misused and powers conferred by SLA to the executives being abused, though many would claim that no such reflection was intended.

Future Research

Research into reasons causing hindrance in PAC reporting may help to overcome problems of untimely PAC reports. Since this initial work solely used documentary evidence to answer the research questions in taking into account the distinctiveness and sensitivity of the topic, further attempts to capture the reasons may have to be made through other methods of data collection such as interviews and observations in order to secure a more complete picture of the study.

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Appendix 1

Diagram I – Accountability Cycle and PAC Cycle in Malaysia

