

Fiscal Analysis and Governance of the City Council of Penang Island 2002-2011

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Abstract

Local governments make up the tier of governance that is closest to the masses. The inability of local governments to be financially secure was one of the reasons that saw the reorganization of local councils in Malaysia in 1976. Currently, there are still several councils that struggle with budgetary constraints, hence allowing for the federalization of certain functions of the local government. This paper looks into the financial position of Majlis Bandaraya Pulau Pinang for the duration of 2002-2011 based on an analysis of the council's Annual Reports. A general trend analysis on revenue and expenditure is employed in this study. Additionally, the rationale for certain expenditure and causes for reduced revenue are also elaborated. Assessment of the financial reports shows a surplus budget is achieved by the council for the duration of the study. Methods such as Public-Private Partnership and collaborative governance is also seen to be stabilizing factors that aid in improved budgetary management. Also noted, the expansion of the role of MBPP regarding the governance of George Town World Heritage Site and the requirement for a paradigm shift in the governing model of the council is also addressed. Moreover, a political shift in the management of the council is also noted to be a factor in its financial health.

Keywords: Fiscal Analysis, MBPP, Budget

1. Introduction

The Malaysian administration system has three tiers with the local government administering smaller portions of territories. The financial capacity of all the local units differ based on the location and the level of urbanization. Majlis Bandaraya Pulau Pinang encompasses the island of Penang, result of a merger between the City Council of George Town and the Penang Rural District Council. Under the Constitution of Malaysia, local government comes under the state control although there are coordinating bodies between the state and the federal government. Also, local councils are empowered to handle their own financial affairs through taxation and grants are provided from the federal or state coffers. Moreover, local governments in Malaysia vary in terms of financial independence and dependence on other tiers of government.

Under the Local Government Act 1976 (Sec V), local councils are empowered to collect taxes, impose charges and provide chargeable services. The act allows local governments to impose quit rent, parking charges and issue licenses for hawkers and businesses. Allocations are to be spent on services offered by the council that includes road lighting, roadwork, market and community halls.

Shortcomings in budgetary process in government expenditure remains an issue that is often debated. Public fiscal management is comprised of three main components, allocation, distribution and stabilisation (Allen, Hemming & Potter, 2013). Essentially, allocation and distribution are steps where resources are attained from various governmental functions and the process of disbursement of resources

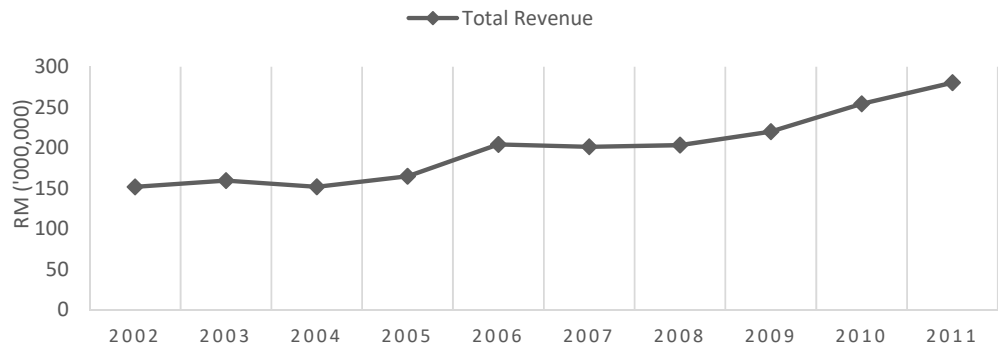
towards the management and development of economies. Meanwhile, stabilization gears towards achieving a semblance of balance in fiscal cycles and preventing large deficits or high debts to maintain sustainable economic growth.

Public fiscal management should not be relegated to bookkeeping of revenue and spending, instead it should be a comprehensive policy that sets the rules for budgetary spending (Cangiano, Curristine & Lazare, 2013). Incrementalist nature of public spending spurred by increased social spending further constrain efforts to achieve a balanced budget. Local governments do benefit from infrastructural spending although it may not be quantified directly (Hanis, Trigunarsyah & Susilawati, 2011). Investments in a public use hall or expansion of roads would indirectly increase the economic value of the area, creating a chain effect for the entry of new business that would in turn increase tax receipts for the government. Kaganova & Nayyar-Stone (as cited in Hanis, et al 2011) noted that public property wasn't viewed as a potential revenue contributor until the 1980s. This changed whereas local government assets in Malaysia, namely convention centres, halls and stadiums are rented out for private use with significant return.

2. Annual Report Fiscal Review

2.1 Analysis on revenue

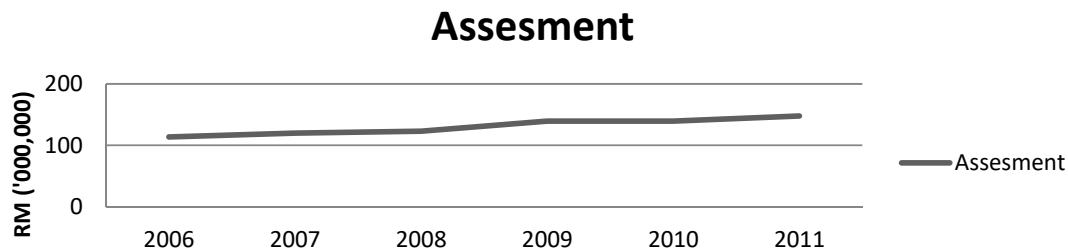
Graph 1. Total Revenue received by MBPP (2002-2011)



Source: MPPP Annual Report, (2002-2011)

Secretariat was the main unit of administration of the council, there is a clear reduction of income in 2005 as compared to the revenue in 2002. The fluctuations of revenue occur because prior to 2005, MBPP annual budget reporting does not differentiate between revenue and non-revenue income. The revenue under Secretariat includes grants and allocation provided by both the state and the federal government and varies depending on the need. The issuance of licenses for the council contributed to increased revenue for the council, with a boost of income at over 35% in 2005 compared with 2003. The surge in collections is in tandem with a higher number of applicants for the council's licenses that includes billboards, small trader license and licenses for entertainment outlet. The council reported over 1280 application for licenses in 2005.

Graph 2. Assessment and Contributions received by MBPP (2006-2011)

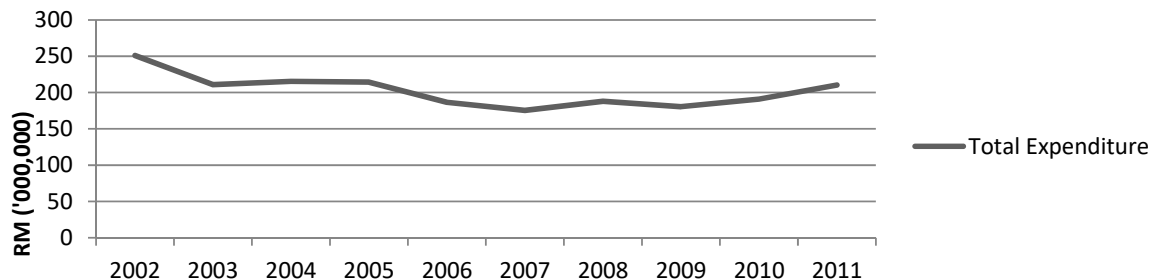


Source: MPPP Annual Report, (2006-2011)

Reorganization of the structure of MBPP commenced in 2005 and financial reporting were broken up into three parts, Rates Revenue, Non-Rates Collection and Non- Revenue income. The annual report uses the same guideline in providing the revenue from 2005 till 2011. Income from assessment rate retains the top spot as the biggest contributor to the coffers of MBPP. Assessment rates differ according to the types of land and building and is based on the estimated gross annual rental rate and is payable bi-annually. The highest assessment rate is imposed on golf tracks and racehorse tracks, at 10.30%, of which there are one of each within the jurisdiction of the MBPP. Based on Graph 2, income from Assessment rate saw a slight increase from 2006 till 2008, this is congruent with Penang's GDP growth rate that slowed down from 10.8% in 2006 to 5.5% in 2008 (Ong, 2015). Stagnation in assessment rate revenue is apparent for the period of 2009 up till 2010 due to a contraction in the state's GDP during that period. Penang experienced a negative growth rate of -10.5% in 2009 due to a global economic slowdown. The manufacturing sector downsized operation and many supporting industries closed due to decreased demand (Ong, 2015).

2.2 Analysis on expenditure

Graph 4. Total Expenditure for MBPP (2002-2011)



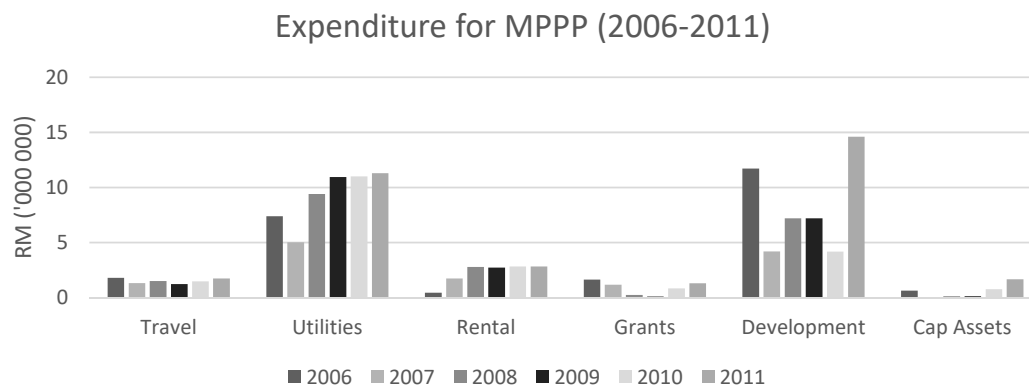
Source: MPPP Annual Report, (2002-2011)

Annual trend for spending sees a downwards movement with slight increases over the duration of the study. There's a prominent reduction in expenditure from the year 2003-2007 although a slight increase is observed from 2008 onwards.

MBPP recorded increased spending on most field except for the Department of Valuation and Town Planning. The spending for health, that includes fogging, education on health and veterinary section increased by RM 17 million from the spending in 2002 compared to what was expended in 2005. The

increase in spending can be linked with increased demand for health education and higher emphasis on food preparation cleanliness. Allocation for the Department of Town Planning increased from RM 2.14 million in 2002 to over RM 167.6 million in 2005. The increased spending is due to the transfer of the council's Landscape Unit in 2004 to the Town Planning Department. Higher budgetary allocation was also due to the introduction of the e-LAMs project (Electronic Local Authority Management System) by the council in 2005 (MBPP, 2005).

Graph 4. MBPP Expenditure 2006-2011



Source: MPPP Annual Report, (2006-2011)

MBPP spending for the duration of 2006-2011 focused on remuneration, spending on utilities and development. Expenses paid out for utilities that includes electricity and other services used by the council has seen an upwards trend every year although the year 2007 saw a reduction of spending. In 2011, the council paid over RM 113 million on utilities alone. A major portion of expenditure went to development, this includes the building of new halls, the creation of mini pocket parks within the city and refurbishment of markets and hawker centers. 2011 recorded the biggest spending on development with a particular emphasis on greening Penang.

2.3 Budget performance

Graph 5. Budgetary Surplus for MBPP (2002-2011)



Source: MPPP Annual Report, (2002-2011)

The budget for MBPP spanning the 10 years used in this study shows a surplus every year. Excess from spending fluctuated yearly with the highest surplus recorded in 2004 and 2010 at RM 64 million respectively while the year 2006 saw a surplus of RM 12 million. A big dip in balance of spending

is observed for the period between 2004 and 2006. The reduction is analogous with the decrease in revenue observed in many departments of MBPP from 2005 to 2006. While there exists a reduction of income by department, the total revenue during the period shows an upward movement. In reality, revenue and spending are not synchronously related. Reduced surplus does not equate to reduced revenue (Vanita Agarwal 2010), MBPP would have implemented expansionary budget in 2004 while being more conservative in spending in the years where the surplus was bigger. A contraction in revenue may even lead to higher spending by way of deficit budgeting as has been applied by MBPP in its budget for 2015 (The Star, 2014).

3. Discussions

MBPP maintains a budget surplus throughout the ten-year period selected for the study. The council managed to evade a deficit budget based on sound management and conservative spending ethics. As a council in an industrial state, it manages to gain higher return of revenue comparable with Majlis Bandaraya Petaling Jaya (MBPJ) which returned a revenue of RM 277 million in 2011 while MBPP received RM 280 million for the same period (MBPJ, 2012). MBPP's surplus budget streak ended in 2015 where the council is expected to run a deficit budget of RM 89.26 million (TheStar, 2014). Demands for investments in development and maintenance sees the need for a deficit budget although the council's savings is enough to maintain the overspending. Previous budget surplus may be attributed to a lower spending threshold for Development Expenditure, in 2011, it only made up 7% of the total spending of the budget. While this helped the council to spend conservatively, investments in infrastructure under the control of MBPP were lacking. MBPP is moving towards investing more on the creation of neighborhood parks, pocket parks and the upgrading of local markets, increasing expenditure for development for years to come (TheStar, 2014).

The costs for development maintenance of public properties especially those that may generate revenue would be shared between the local government and a private developer. For instance, MBPP in 2011 entered into a Public-Private Partnership with SP Setia Berhad to redevelop the Penang International Sports Arena into a major convention centre (Eng, 2013). PISA was built and maintained by MBPP in 2000, when the need arose for a new major convention center in Penang, a decision was made to save cost by refurbishing PISA, the cost for MBPP to handle the task alone would have been colossal compared with the budget available for the council.

The PPP would see SP Setia bearing the total RM 300 million in redeveloping PISA into the Spice Convention Centre (sPICE) with the company receiving 30 years concession period to maintain the unit while sPICE would still remain under the ownership of the council. PPP is congruent with trend of collaboration between the public and the private sector in reducing public cost, in preventing future deficit, more joint ventures may be created. Also, the handling of garbage on the island of Penang is handled by both the MBPP and private contractors, the council could extend the venture and reduce contractual payment by allowing the garbage collecting firms to recycle the waste and retain its profit.

On a more current note, the recognition of George Town as a World Heritage Site in 2009 had expanded the role played by MBPP. Essentially, the governance of the heritage site employs metagovernance where multiples stakeholders are involved including UNESCO, federal government agencies, parastatal agencies such as the George Town World Heritage Site, ThinkCity and local NGOs (Katahenggam, 2016). As stipulated in the Special Area Plan, MBPP is the direct regulatory force, especially in ensuring compliance of restoration work. Moreover, George Town had established itself as a heritage tourism destination, warranting a paradigm shift to balance tourism with heritage conservation. In this regard, the governance approach of Penang, especially in George Town needs to be revised due to the international exposure the city is getting. For instance, the issue of touristification of George Town is discussed on the backdrop of the sustainability in conserving heritage in the midst of development (Barron, 2017). Increased public engagement and consultation, along the lines of Regensburg World

Heritage Site in Germany would allow for a more equitable form of involvement of MBPP in governing George Town and the island (Scheffler, 2011).

Therefore, the pressure on spending would see an upwards trend, especially when higher level of expertise would be needed in the governance of the heritage enclave. Undeniably, investments from the market as well as ThinkCity's grants had allowed for restorative work in the inner city. However, heritage shophouses beyond the limit of the World Heritage Site is under the threat of development, if the council propagates adaptive reuse of the buildings, indirectly it will benefit from increased revenue from the expansion of tourism and heritage related industry on the island.

4. Conclusion

Increasing demand for better service and infrastructure would tax the budgetary system of the local government. Restructuring of Majlis Perbandaran Pulau Pinang into Majlis Bandaraya Pulau Pinang would see an increase of responsibility and spending on the part of the council. The public and every tier of government would expect more from the local government authority. While MBPP's budget had shown a surplus budget for the duration of the study, current budgets run on deficit while the council's counterpart, MPSP had managed to move away from deficit. MBPP and its predecessors have experience governing a wider range of services including public transportation and public housing. Moreover, the expansion of the council's role in governing George Town World Heritage Site and its periphery should also be noted. Application of past knowledge along with innovation would see prudent management of the council's budget materialize. The higher emphasis on Public Private Partnership now should be applied with caution to shield the council from the volatile capital market.

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