PAC REPORT ON THE MANAGEMENT CONTROL PROCEDURE OF PEMBINAAN PFI SDN. BHD.

1. INTRODUCTION

Auditor General's Report for 2013 (series 3) had reported on companies with highest liabilities, among others was the Pembinaan PFI Sdn. Bhd. The issue has been much talked about by the people and the Public Accounts Committee (PAC) has decided to discuss the issue on 18 March 2015; the 11^{th} Meeting in 2015.

2. OBJECTIVE OF PAC DISCUSSION

In accordance with the mandate given under Article 77 Standing Orders of the House of Representatives as well as Article 304 (a) Treasury Order (Amendment 2008), the Public Accounts Committee has called the Ministry of Finance to clarify the following matters:

i. The objectives of the establishment of Pembinaan PFI Sdn. Bhd;

ii. Financing and operation of Pembinaan PFI Sdn. Bhd .; and

iii.The debts of Pembinaan PFI Sdn. Bhd. and its impact on the Government’s finance.

3. SCOPE AND METHODOLOGY

Discussions have been conducted through the following approaches:

i. Invite the National Audit Department to give explanation on issues raised; and

ii. Call the Ministry of Finance to give explanation.

4. PAC LIMITATION

No limitation identified.

5. BACKGROUND OF PEMBINAAN PFI SDN. BHD.

Pembinaan PFI Sdn. Bhd. (PFI) was established on 28 September 2006. The company was a Special Purpose Vehicle (SPV) owned by Finance Minister Incorporated (MOF Inc.). Its objective was to raise funds to finance the project / activity identified by the Government. The fund raising structure was divided into two; PFI I with RM20 billion fund through a loan agreement signed with the Employees Provident Fund (EPF) in 2007 at the interest rate of 0.5% based on the interest rate of Malaysian Government Securities (MGS) and the repayment should be made in bullet payment within the period of 5 years. This loan has been rescheduled with a repayment period of 15 years from 2013 to 2027. While PFI II amounting to RM10 billion was obtained from EPF and Retirement Fund Incorporated (KWAP) with 10 years repayment period. This fund was managed by the Ministry of Finance according to the current financial procedure.

6. OUTCOME OF DISCUSSION AND FINDINGS OF THE PUBLIC ACCOUNTS COMMITTEE

The discussion session began with preliminary explanation on the issues concerned by the National Audit Department to the Public Accounts Committee. Then, all parties involved in the issue raised, namely the Ministry of Finance represented by Tan Sri Dr. Mohd. Irwan Serigar Bin Abdullah, Secretary General of Treasury and Dato' Dr. Mohd. Isa bin Hussain, Secretary of the Government Investment Company Division were called to give explanation. Matters of discussions can be generally summarised as follow:

6.1. Preliminary Explanation By The National Audit Department

The National Audit Department informed regarding the auditing carried out on PFI fund management as follows:

6.1.1 Audit Of Financial Statements

Every year the National Audit Department carries out the audit of the PFI I and PFI II Trust Accounts and PFI trust account management issues like expenses more than allocations, allocation received was not spent or spent less than 50% have been raised. Besides that, the National Audit Department also had conducted analysis on liabilities of MOF Inc. owned companies and found that Pembinaan PFI Sdn. Bhd. was among those with highest liability which was RM27.862 billion.

6.1.2 Performance Audit

The National Audit Department also had conducted a performance audit on projects that were using PFI funds, and issues that often raised were delayed project, poor construction quality, works not in accordance to the specification and weakness of the monitoring.

6.1.3 Audit on Pembinaan PFI Sdn. Bhd.

The audit on the Pembinaan PFI Sdn. Bhd. was yet to be carried out as the proclamation for audit purposes has just being acquired even though the company has been operational since 2006. The audit was not carried out on SPV companies such as PPFI because such companies did not have a proper organisation structure. The company was only managed by the Ministry of Finance.

6.2. Explanation by the Secretary General Of The Treasury, Ministry of Finance

Tan Sri Dr. Mohd. Irwan Serigar Bin Abdullah, Secretary General of the Treasury, Ministry of Finance explained regarding the management control procedures of Pembinaan PFI Sdn. Bhd. as follows:

6.2.1 The concept of Private Finance Initiative or PFI had been discussed during the tabling of the Ninth Malaysia Plan in 2006. PFI was different from Public Private Partnership or PPP under the administration of Public Private Partnership Unit (UKAS). PPP was established with funds amounting to RM20 billion and projects under PPP was not funded by the Government, but the Government only loaned 10% of the project cost, as a tipping point.

6.2.2 Through its Private Finance Initiative, a Special Purpose Vehicle (SPV) wholly owned by Minister of Finance Incorporated (MOF Inc.) was established with the aim of raising funds to finance projects / activities identified by the Government. The fund was acquired by getting loans from the Retirement Fund Incorporated (KWAP) and Employees Provident Fund (EPF). EPF and KWAP were selected because both agencies offered financing rates that were lower than commercial bank. In addition, the long-term profits derived by KWAP and EPF which was the loan interest paid by the Government will be enjoyed by the contributors of both agencies that made up of private and public officials.

6.2.3 The fund-raising structure was divided into two; PFI I and PFI II. In 2006, PFI I was launched with funds amounting to RM20 billion to finance 547 projects identified by the Economic Planning Unit (EPU) such as construction of schools, hospitals and so on. Through the PFI concept, projects that cannot be financed through the development allocations under the Ninth Malaysia Plan (9MP) due to financial constrain can be carried out sooner instead of waiting for another 10 or 20 years when the cost will be higher. Besides, the implementation of projects through PFI has managed to reduce the impact of economic recession when the Government actively implement various projects by giving contracts to local contractors. In 2012, the Government has launched PFI II with funds amounting to RM12 billion. However, until today, the loans made by the Government was only RM10 billion.

6.2.4 The management of projects under the PFI concept was in accordance with the procurement rules and procedures as prescribed by the Government similar to the projects implemented under the Ninth Malaysia Plan (9MP).

6.2.5 PFI Fund was managed through Trust Account and financing via trust account was beyond the usual mechanism of development budget (off-budget). However, the implementation of projects under PFI I was tabled in Parliament during the tabling of the Ninth Malaysia Plan and also during the tabling of 2012 and 2013 budgets for PFI II projects. International rating agencies such as Standard and Poor and Fitch were also informed about the commitment that had to be borne by the Government following the PFI implementation.

6.3. Explanation by Dato' Dr. Mohd. Isa Bin Hussain, Secretary of the Government Investment Company Division

Dato' Dr. Mohd. Isa Bin Hussain, Secretary of the Government Investment Company Division gave further clarification on PFI fund management as follows:

6.3.1 Pembinaan PFI Sdn. Bhd. (PFI) was a Special Purpose Vehicle (SPV) wholly owned by Minister of Finance Incorporated (MOF Inc.). The funds acquired by the Pembinaan PFI Sdn. Bhd. will go to the Government and place in Trust Account.

a. Private Finance Initiative I (PFI I)

i. Sources of funds amounting to RM20 billion was from EPF. Initially, the loan term was 5 years and repayment must be made in bullet payment. The loan was later restructured and repaid by instalment within 15 years period which was from 2013 to 2027. After it was restructured, the amount of loan has increased to RM22 billion after taking into account the capitalized interest within 5 years (grace period) of bullet payment.

ii. Ministry of Finance prepared the principal agreement with Pembinaan PFI Sdn. Bhd. (PFI) and the Federal Lands Commissioner (PTP) will lease the land at the nominal value of RM10 to PPFI after the principal agreement was signed and created a lease agreement. PPFI will sub-lease the land to PTP. Then, PPFI will use these assets to get funding from the EPF and after both sides agreed to the terms stipulated, the facility agreement was prepared. By this method, there was no risk to the EPF and the EPF able to offer lower lending rates to the Government.

iii. The Government will pay PPFI by instalments the land lease commitments between PTP and PPFI for the next 15 years and PPFI will use the proceeds from the sub-leases to repay its loan to FPF. Through this method, the land ownership was not transferred to PPFI or EPF. Ownership of the land and the project remained with the Government.

iv. Allocation for the land sub-lease payments by Government to PPFI was provided under the operating expenditure.

b. Private Finance Initiative II (PFI II)

i. Implementation of PFI II was different from PFI I. For PFI II, PTP identified suitable lands with value equal to the value of the loan which was RM10 billion and signed the lease agreements with PPFI. The lands assessments were done by the Valuation and Property Services Department. Then PPFI will sub-lease the land to the EPF for funds amounting to RM6.037 billion and to KWAP for funds amounting to RM3.963 billion.

ii. The Employees Provident Fund (EPF) and Retirement Fund Incorporated (KWAP) will again sub-lease the land to Ministry of Finance by signing the secondary sub-lease agreement. While PTP provided Deed of Assignment to assign the rights to the Ministry of Finance to receive funds amounting to RM10 billion from PPFI in one disbursement. The Ministry of Finance will pay the lease including the interest to PPFI gradually over a period of 10 years beginning from 2015 to 2024 based on the repayment schedule using the operating expenditure.

iii. Land / asset that was leased for PFI II was a different land / asset which was leased for PFI I.

6.3.2 PFI Trust Account Management

Funds received from PPFI was accounted in the Private Finance Initiative (PFI I) Trust Account and Special Development Activities Trust Account of Private Financing (PFI II). The Trust accounts were managed by a committee consisting of the Ministry of Finance; Accountant General's Department (JANM); Economic Planning Unit and Implementation Coordination Unit, Prime Minister's Department and Ministry of Works. Accounting records of the trust account was maintained by JANM. Balance funds that have not been used for the implementation of projects / activities have been invested in fixed deposits which were managed by JANM to get additional funding through the investment profits received.

6.3.3 Project Implementation Using PFI Fund

a. Economic Planning Unit (EPU), Prime Minister’s Department has identified the projects that need to be implemented as soon as possible but were not provided for under the development expenditure. These projects will be implemented using the PFI I funds. While for the PFI II, the projects / activities to be implemented using this fund will be determined by the Ministry of Finance. After the list of projects / activities were identified, the Ministry of Finance will channel the allocations to ministries to implement the projects.

b. Implementation of projects using the PFI fund was similar to other development projects which in accordance with the rules and procedures of procurement stipulated by the Government. Regulations pertaining to Variation Order, procedure of additional allocation application or allocation transfer applications between projects also have to comply with the current financial regulations. The projects performances were monitored by the Implementation Coordination Unit (ICU), Prime Minister's Department.

6.3.4 Project Implementation Performance Under PFI I

Overall, RM18.92 billion (94.6%) from the RM20 billion fund has been spent, where 525 out of 547 projects have been completed by 16 ministries. Whereas the remaining funds amounting to RM1.08 billion (5.4%) will be used for the completion of 22 projects that are still under construction.

6.3.5 Project Implementation Performance Under PFI II

RM7.24 billion (72.4%) of RM10 billion fund approved has been spent by 15 ministries/agencies to implement 339 projects. 77 projects (22.7%) were successfully completed, while 207 (61.1%) projects are under implementation process and 55 (16.2%) projects are still in pre-implementation stage.

SUMMARY OF PUBLIC ACCOUNTS COMMITTEE

7.1. The Government initiatives to raise funds through PFI to finance the development activities was a good concept. However, the actual PFI concept was not applied in this case. On PAC's point of view, this programme was an off-budget government’s loan. Private parties did not cover the implementation costs of the projects.

7.2 The PPFI's loan will be repaid as lease payment by the Government for the use of land owned by PPFI which was previously leased to PFI by the Government with nominal price.

7.3 The expenditure used was not presented in the Budget tabled in Parliament. Detail of project allocation which was funded by PFI was not tabled in Parliament as well (off budget expenditure).

7.4 The off-budget expenditure can create doubts over the figures produced in the budget and did not reflect the Government's real financial standing, including contingent liability figures, deficit calculation and government's debt.

7.5 Besides that, the loans under the Financial Accounts did not show up as government's liability and the expenditure was not taken into account when calculating the deficit. Therefore, the deficit remained at around 3% and the debt at the rate of 54% to the Gross Domestic Product (GDP), although the actual government loans and expenses were higher when taking into account the loan and expenditure under PFI. This loan will only be reported as government's liability upon the implementation of Accruals Accounting.

7.6 The above expenditure will put the government's commitment in operating expenditure in the future.

RECOMMENDATIONS OF PUBLIC ACCOUNTS COMMITTEE

For the purpose of future improvement, the Public Accounts Committee recommended the following:

8.1 The provisions and expenses for projects under PFI should be tabled and approved in Parliament. In addition, all forms of off-budget expenditure similar to this PFI should also be reported in a transparent manner.

Public Accounts Committee