DRAFT

MALAYSIA

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1. Introduction

Malaysia is a leading world exporter of liquefied natural gas (LNG) and a net oil exporter, though its known oil reserves may be insufficient to satisfy domestic needs in the long term. LNG and liquid petroleum gas (LPG), a by-product of oil-refining, have supplemented oil as sources of energy. Malaysian oil is light and has low sulphur content, priced at a premium in its export market to more than offset its imports of heavy oils for manufacturing petroleum products for domestic use.

Most Malaysian oil and gas are in the exclusive economic zone (EEZ) in the South China Sea. Most oil is found offshore of Peninsular Malaysia, on the west of the South China Sea; while most LNG is found offshore the states of Sabah and Sarawak, to the south of the South China Sea.

Conflicts over oil and gas in the EEZ has been handled between neighbouring countries in the Association of Southeast Asian Nations (ASEAN), including the Joint Development Area for gas with Thailand. The Malaysian Government also has joint oil and petrol-chemical projects with other countries in ASEAN, Asian, Middle East and Africa (**www.geni.org/globalenergy/library/national_energy**_grid/malaysia/Malaysia Co untryAnalysusBrief.sshsrml)

As for other countries, Malaysia has been challenged by the need for sustainable oil and gas management. The challenge has increased with the recent price increases.

However, the more significant challenge has been oil revenue generation for development and revenue distribution. Revenue from oil exploitation in the early years of Malaysian economic development has been substantial. While newly found reserves have eased the tension of sustainable development from time to time, revenue distribution for development posed even greater challenges.

The Federation is centralised; oil and gas are federal matters and they are located offshore the less developed states of Terengganu, Sabah and Sarawak. The producing states have been allocated royalty, but there have been calls from these states for increased royalty. Other states have also shown interest in revenue-sharing.

This chapter examines Malaysian fiscal federalism, focusing on oil and gas management. It describes the well-regulated, efficient petroleum industry as well as federal-state financial relation. It highlights the centralisation of the Malaysian federal system and the need to improve federal fiscal response to regional socio-economic disparities. Finally, it concludes with current concerns for the development of Malaysian federalism in addressing public needs.

2. Federal System

Malaysia is made up of the 11 peninsular states of the previous Malayan Federation, Sabah and Sarawak, which formed the federation on 16 September 1963. The Malayan Federation gained independence on 31 August 1957 and this date is celebrated as the Malaysian national day.

Malaysia declares parliamentary democracy. There are 222 elected members (MPs) who execute a maximum 5-year office and 70 senators hold office for a maximum of two 3-year terms (Table 1). The states elect 2 senators each and the king appoints other senators on the prime minister's (PM) advice. Most senators have been from the PM's political coalition.

Malaysia is a constitutional monarchy; with rulers of royal descent in 9 states and rulers in 4 states appointed by the 5-year term king. The king is elected from the royal rulers by the Rulers' Conference. The king appoints the PM, who commands representative majority confidence, to head the federal government.

The constitution was drawn for a centralised federation to facilitate administration. The PM has headed the same national coalition since Malaysia was formed. This majority basis means a strong government and a weaker legislative parliament. Centralisation increases over time with socio-economic changes as well as constitutional amendments. Currently constitutional amendments require a 2/3 majority, and the king and Senate can only delay bill consent within stipulated periods.

Malaysia has two hierarchies of courts, the civil court and the syariah court for Islamic matters in the 9 traditional monarchies. The king appoints the head of the civil court. The 1988 sacking of the head raised judiciary independence issues; but after the 2008 general elections, the government made some compensation for the sack.

The federal government has more jurisdictions and resources than the state government. It is in charge of national, political and macroeconomic matters and related revenues, with 80-90 per cent of consolidated federal and state revenues as well as expenditures (Tables 2, 3 and 4). The state governments manage land, agriculture, forestry, local services and traditional customs, based on state constitutions. The Sabah and Sarawak governments have a few more jurisdictions as Malaysian participants with the Malayan Federation. Federal considerations override the states' in inconsistencies, and most MPs' allegiance to the national coalition leads to centralisation (Bari, 2003).

3. Petroleum Industry

The earliest records of oil in Malaysia were for Sarawak, where the indigenous people used it for lighting (see Adnan, 1982). Shell Oilfields Company Limited developed the Miri Oilfield in 1910, and oil produced and exported more than doubled to a peak 5.5 million barrels in 1929. Thereafter, offshore exploration and production grew significantly.

The Royal Dutch Shell Group was granted the first offshore producing rights, for the Lutong field off the Sarawak shore. Sarawak Shell and Shell Sabah held the only oil concessions till the Continental Shelf Act, 1966 increased bidders and concessionaires. Current companies involved in exploration/production include P, ConococPhillips, ExxonMobil (Esso), Hess, Mitsubishi, Murphy Oil, Newfield Exploration, Nippon Oil and Talisman Energy. Oil was discovered off the Terengganu coast in the late 1970s (*Mid-Term Review of the Second Malaysia Plan*).

Offshore crude oil production cost has been relatively high due to technical requirements for deepwater deposits and weather. However, the light specific gravity and low sulphur level of the oil has commanded a price premium (Wu, 1988).

Malaysian crude oil output grew from 8.892 million tonne in 1977 to 31.516 million tonnes in 2006, with per capita of 0.71 tonne and 1.18 tonnes respectively (Table 5). Oil is mainly sold overseas on contractual agreement, while spot sales of excess oil may be made. Exports more than doubled from 7.354 million tonnes to 16.866 million tonnes during the period. It rose from 12.7 per cent of export value in 1977 to 22.9 per cent in 1985, falling to 5.4 per cent in 2006 as domestic demand increased.

Local refineries contract some Malaysian oil, but economically use more imported heavy oils more suited for its fuel product needs. Imports grew from 3.961 million tonnes in 1980 to 10.236 million tonnes in 2006, though falling from 6.6 per cent of import value to 3.7 per cent. The number of refineries increased from 6 in 1977 to 11 by 1995. They include Shell's refinery in Sarawak, Petronas in Melaka and ExxonMobil in Negri Sembilan (www.eia.doe.gov_emeu_cabs_Malaysia_pdf.pdf). Net exports of crude oil grew from 7,266 million tonnes in 1980 to 17.894 million tonnes in 1995, and fell to 6.657 million tonnes in 2006.

The manufacture of petroleum products such as kerosene, liquid petroleum gas (LPG), fuel oil, diesel/gas oil and gasoline increased throughout. LPG is used in domestic industries and households. Net imports fell from 2.913 million tonnes in 1980 to zero in 2006 as processing facilities expanded.

Natural gas output grew from 93 thousand million standard cubic feet (mscf) in 1980 to 2,108 thousand mscf in 2006, per capita increasing from 0.007 mscf to 0.079 mscf. The gas is processed in the producing states of Sabah, Sarawak and Terengganu for LNG. Malaysia has one of the most extensive gas pipeline networks in Asia, supplying domestic users, Singapore and Indonesia. LNG exports increased from 9.727 million tonnes in 1995 to 21.534 million tonnes in 2006 – 4.0 per cent of export value – transported by the single largest world tanker fleet of the Malaysian International Shipping Corporation. Other petrochemical industries include urea plants in Sarawak and Kedah (*Seventh Malaysia Plan*). The major oil/gas ports are in Terengganu, Johor, Sabah and Sarawak.

Electricity from diesel station fell from 15.3 per cent in 1980 to 3.2 per cent in 2006, while that from gas turbines grew from 3.2 per cent to 64.4 per cent. Sabah and Sarawak are more dependent on diesel for electricity, though both are also switching to gas turbines.

In 2005, crude oil and condensate reserves were 5.3 billion barrels while that for natural gas was 885.2 trillion cubic feet. Based on production of 727,000 barrels per day in line with the National Depletion Policy, oil reserves were expected to last 19 years. Gas reserves were expected to last 33 years (*The Ninth Malaysia Plan*).

4. Petroleum Legislation

The earliest concessionary system for oil production was followed by equal profit-sharing between companies and the government under the Petroleum Mining Rules, 1966. The Petroleum Development Bill (1974) converts the arrangement to production-sharing. The Petroleum Development Act (PDA) established the state oil company, Petrolium Nasional Berhad (Petronas), in which is vested ownership and control over petroleum exploration and production as well as refining, processing and manufacturing of petroleum products.

Under production-sharing, private companies finance exploration, development and production of oil and gas in exchange for output shares as below.

Item	Distribution	Company	Government	
			Federal	State
		Oil		
Cost recovery	20%	20%	-	-
Royalty	10%	-	5%	5%
Balance	70%	30% of 70% = 21%	70% of 70% = 49%	-
Tax	-	Tax on 21%	Add tax	-
Total	100%	41% less tax on 21%	54% add tax on 21%	5%
		Gas		
Cost recovery	25%	25%	-	-
Royalty	10%	-	5%	5%
Balance	65%	30% of 65% = 19.5%	70% of 65% = 45.5%	-

Tax	-	Tax on 19.5%	Add tax	-
Total	100%	44.5% less tax	50.5% add tax on 19.5%	5%

Petroleum income tax was 45 per cent until 1993, 40 per cent for 1994-97 and 38 per cent from 1998. As for other industries, tax deduction is provided for the employment of the disabled, expenses on staff welfare, community projects as well as contributions to arts and culture.

The revenue over cost scheme used from 1997 accelerates cost recovery for private investments in upstream activities which meet cost targets. The private companies' share increase with higher costs and/or lower profitability as well as production (www.petronas.com.my).

Petroleum industries located on land under state government control and subject to local authority regulations (e.g. on safety of buildings, road access and sewerage) may be affected by state government actions. However, the letter of the constitution requires state governments to allow federal developmental activities and the National Land Council can initiate land regulations deemed necessary for development purpose. There are no known records of significant state government objection to the expansion of petroleum industries.

Under PDA, Petronas has become the largest operator for both upstream and downstream petroleum activities. It ranks amongst Fortune Global's 500 largest corporations, having ventured into oil and gas exploration and production as well as downstream activities in 32 countries. In Malaysia, it first exported crude oil from production-sharing in 1975, then went into exploration, refuelling and bunkering services as well as the Asean-Bintulu fertiliser project in Sarawak. In the 1980s, it started operating petrol stations, exporting LNG, implementing gas utilisation projects and exporting LPG. It expanded operations overseas, issued bonds and got listed in the Kuala Lumpur Stock Exchange in the early 1990s. It launched the natural gas taxi and Malaysia's first prototype engine in 1998 as well as produce the revolutionary PRIMAX oil from 2000 and Superbike from 2003.

5. Revenues

Government revenues from petroleum resources are in the form of royalties, petroleum tax, petroleum dividends from Petronas and export duties on petroleum. Petroleum royalties decreased from 2.7 per cent of federal government revenues for 1980-85 to 1.7 per cent for 1991-95, before increasing to 2.5 per cent for 2001-2005 (Table 6). The same amount of royalties have also been paid to the governments of producing states, Sabah, Sarawak and Terengganu, which amounted to an estimated 10 to 12 per cent of consolidated state government revenue.

The Federal Government collects petroleum tax on companies producing petroleum, export duties on petroleum as well as excise duties, sales tax and import duties on petroleum and petroleum products. Petroleum tax decreased from 12.6 per cent of federal government revenue for 1980-85 to 6.3 per cent for 1996-2000 before increasing to 11.3 per cent for 2001-2005.

Export duties are levied on Malaysian petroleum while the other taxes are on products produced predominantly from imported petroleum. Export duties and excise duties were among the first taxes levied to raise revenues. Such taxes on certain items have been reduced or abolished to increase export competitiveness, but these taxes on petroleum and petroleum products continue up to the present. However, they form a minimal portion of government revenue in comparison to petroleum tax. Export duties decreased from 7.5 per cent of federal government revenue for 1980-85 to 1.4 per cent for 2001-05.

Sales taxes have been considered as a source of revenue as Malaysia reduces or abolishes import duties according to agreement in the World Trade Organisation (WTO). However, they contribute very small portions of federal government revenue. The sales taxes are 21-25 per cent for various grades of retail petrol, 7.5-8.0 per cent for various grades of diesel and 5 per cent for lubricant. The government has postponed implementing an economy-wide sales tax system several times. The expanded scope of sales tax is expected to cause a "one-time inflation", though the one time inflation will have a lasting effect unless inflation is reversed.

Import duties were levied to protect various industries other than petroleum, for which Malaysia has the advantage of supply. However, they are being reduced or abolished as per WTO agreement.

6. Federal-State Financial Relations

Sabah, Sarawak and Terengganu have been the only states to receive cash payments of 5 per cent petroleum and gas royalties. The Terengganu Government received royalties from 1978 to March 2000, after which payments stopped while royalties were diverted to a federal-controlled fund. The Federal Government said that previous payments were made on compassionate grounds for Terengganu's high incidence of poverty. The Terengganu Government sued the Federal Government and Petronas for non-payment and its writ said that the payment stopped only after the opposition party, PAS, unseated the ruling coalition in the 1999 state election. The court ruled that Terengganu's rights were up to 3 nautical miles offshore and it could not claim royalties for the petroleum in the continental shelf (Fong, 2008:48-51, 98-102).

When Malaysia was formed, Sabah and Sarawak had declared ownership over the continental shelf. Hence they have rights over the vast petroleum and gas resources in further offshore.

There have been public calls and claims for increased royalties to the producing states over the years. Under the Malaysia Agreement, the special grant from the Federal Government to Sarawak was to be reviewed in 1969. The then Chief Minister of Sarawak claimed that the Federal Government orally assured him that Sarawak can have all offshore oil in return for a lower grant (Leigh, 1988: 133). During the 1990 election campaign, the Chief Minister of the opposition controlled state of Sabah said royalty should be increased to 50 per cent.

Calls are made for increased royalty to Sabah and Sarawak when the ruling coalition is considerably challenged after the March 2008 election. The election saw significant voter shift in support for the opposition. The coalition of opposition parties then was led by the wife of the charismatic ex-Deputy Prime Minister-cum-Finance Minister, Anwar, who as banned from contesting for election because of his imprisonment. It is alleged that Anwar was badly treated while in prison for corruption and sodomy charges, the latter which he successfully overturned. Anwar's wife resigned as MP to make way for his contest in a by-election in August 2008, after the ban for his contest was lifted. Anwar won and became the leader of the opposition. He claimed to have the support of enough MPs to declare non-confidence against the PM and gave a few unachieved deadlines for his take-over of the government, including the formation date of the Malaysian Federation on 16 September and a week later, the latter being a day before the hearing of his new sodomy charges.

Anwar said he would increase petroleum royalty to the state to 20 per cent if he took over the government. There were also reports of the ruling coalition mentioning royalty increase to 25 per cent.

Some Sarawak ministers hold that regular federal-state negotiations would ensure higher net transfers to the state rather than increased royalties, which would presumably be at the expense of jeopardising federal-state relation. They made reference to allocations for development funds (see section on regional equity).

There are various annual federal grants to the states intended for compensation, revenue-sharing, horizontal equalising, continuation of prior agreements and support. The road grant compensates a state for the use of its roads by "non-taxable" non-residents. It considers maintenance cost for the agreed road mileages. The maintenance cost traditionally lagged behind actual cost until the consumer price index was considered (Wilson and Mahbob, 1997).

Service charges at 5 per cent of federal project costs are paid to the state governments if they contribute 50 per cent to staff involvement. Reimbursements for cost incurred are also made.

Export duties on tin, iron and other minerals other than petroleum are shared between the Federal Government and the State Governments, which are assigned 10 per cent. The Federal Government is empowered to increase the assignment to more than 10 per cent, though it has never done so.

The Selangor Government currently receives RM18.3 million for the handing over of the Federal Territory of Kuala Lumpur to the Federal Government and RM7.5 million for the handing over of the Federal Territory of Putrajaya (PTPJ). State assemblymen in the opposition parties had opposed to the handing over of PTPJ (Daily Express, Sabah, 2000). The Kedah Government receives RM10,000 as a continuation of the Kedah-British agreement for handing over of territories to the central government in 1869.

The growth revenue grant is allocated if federal government revenue grows more than 10 per cent, with a cap of RM150 million to be distributed as follows – RM25 million equally shared, RM25 distributed according to state populations and RM100 equally shared by states with per capita gross domestic product below the national average. The grant is for current year and the growth of federal government revenue in previous years is not cumulatively considered, so that vertical inequality in fiscal capacity widens as the federal government revenue grows over time. The RM150 million cap was 1.9 per cent of federal government revenue in 1977, the year the Revenue Growth Grant Act was formulated. In 2007, the cap was an estimated 1.1 per cent of federal government revenue.

The capitation grant considers the state population, hence the extent of need for public services. The population size used in determining the amount of grant has been controversial as population census is taken at 10-year intervals. The exclusion of foreign immigrants, especially the illegal ones in Sabah, has also been raised (Wilson and Mahbob, 1997).

The development grants aim to reduce inter-state social disparities. The Federal Government specifies spending conditions, thereby constraining state decision-making (Umikalsom, 1991: 123).

As conditions for federating, the Sabah Government received escalating growth grants until the scheduled review in 1969 replaced them with special grants of lower values. Hence Sabah's hope for net transfer of public funds for development from federating is diminished with respect to annual federal grants (see also section on horizontal equity).

Sarawak received some fixed annual grant and escalating grant for federating until the scheduled review replaced them with special grant.

Federal grants decreased from 37.0 per cent of consolidated state government revenues in 1963 to an estimated 22.7 per cent in 2007. Reimbursements decreased from 22.9 per cent of consolidated state government revenue to 0.4 per cent respectively (Ministry of Finance, Malaysia).

Because of limited fiscal capacity, state governments have indicated interest in increasing federal grants or transfers. The tensions over petroleum royalties are well-documented. Further, an officer of the Johor State Government has proposed a share of petroleum royalties for non-producing states (Shahir bin Nasir, 1997). In 1978, the Kedah Chief Minister argued that the Federal Government should give special consideration to Kedah in the allocation of aids and grants as it contributed to 50 per cent of Malaysia's rice production (Shafruddin, 1987: 63). Some state governments have handed over certain jurisdictions to the Federal Government as their fiscal capacities are insufficient to cope (Umikalsum, 1987), leading to further centralisation.

The Sabah and Sarawak Governments can only borrow from within their states and from the federal Government, the latter condition being the only one applicable to all other states. "Borrowing" is constitutionally defined to include advance tax payments or charges which are liabilities before their due dates. This is a constitutional amendment made after the court ruled in favour of the opposition-controlled state of Kelantan in a case the Federal Government brought against it for receiving such payments to build a bridge as an election pledge.

7. Counter-Cyclical Stance

In times of needs, the Federal Government supports the state governments through certain grants and loans. The Federal Government supports the state governments through the State Reserve Fund grants if they have budgetary deficits. It provides Contingency Fund grants for unforeseen needs and advances for cash-flow difficulties through the State Advance Fund grant. Such grants increased during the 1997/98 Asian financial crisis.

The Malaysian economy was overheating in the early 1990s but grew relatively slower in the post 199/98 financial crisis era. The increase in federal grants to the state from the lowest 15.6 per cent of consolidated state government revenue in 1996 to 22.9 per cent in 2007 appear to be appropriate counter-cyclical stance. This is a change from the recessionary 1980s. At that time the government attempted to control budgetary deficits despite expected recession. Grants were a historical low portion of consolidated state government revenue in 1980. Federal support shifted from grants to loans over the long term, with some re-scheduling of loan repayment when state government could not repay on time.

Outstanding federal loans to the state government increased from 42.3 per cent of consolidated state government revenue in 1966 to 134.0 per cent in 1984 as the state government borrows for development projects. After the high economic growth of the early 1990s, outstanding loans decreased to 83.0 per cent in 1997. The post 1997/98 crisis era saw it increasing, to 109.6 per cent in 2000 (….update?).

8. Regional Equity

Petroleum and gas revenues are not specifically earmarked for horizontal equalisation. State fiscal capacities differ and federal grants have not facilitated equalisation (Wee, 2006: Table 6.5), although the more serious problem is vertical fiscal disparity. However, budgetary allocations for development by state could have been used to address regional socio-economic disparities.

Post-colonial Malaya had more modern land transport and port facilities on the west coast in which British tin mines and rubber estates were located. The central and southern states of Selangor, Perak, Melaka, Negri Sembilan and Johor as well as Penang to the north-west are "more developed" while the north and east coast states of Kedah, Kelantan, Terengganu and Pahang as well as Sabah and Sarawak are less developed" (see various Malaysia plan documents). It is noteworthy that the petroleum-producing states of Sabah, Sarawak and Terengganu are among the less developed.

However, the highest public development funds have not been allocated to the less developed states except for Sarawak (Table 7). Allocations for Pahang also decreased relatively from the highest in the Third Malaysia Plan (1976-1980) to the 9th amongst the 13 states by the Eighth Malaysia Plan (2001-2005). Further, allocations for PAS-controlled Kelantan have been amongst the lowest and decreasing relatively.

Sabah's allocations decreased relatively during tensions between the Federal Government and its state government, when its state government was in the opposition around the Fifth Malaysia Plan (1986-1990) and the Sixth Malaysia Plan (1991-1995). Subsequently UMNO, the dominant party in the ruling coalition, was formed in the state and other Sabah-based parties joined the coalition. The ruling coalition took back control of the state government and Sabah's development allocation was 2nd highest by state for the Seventh Malaysia Plan (1995-2000) and the Eighth Malaysia Plan (2001-2005). However, Sabah's relatively high population led to its relatively low per capita allocation (Table 8).

Sabah had one of the highest incidences of poverty by state since 1976 (Table 9). Three months after the 2008 general election, the president of one of the Sabah-based political parties in the ruling coalition announced a proposal for a vote of no-confidence against the PM. However, a motion for no-confidence by the then leader of the opposition was rejected by the parliamentary speaker. Six months after the election, the party withdrew from the ruling coalition.

The diverse socio-economic status and regional cultures require a mix of development programmes to address the heterogeneous needs of the different populations. For example, the Federal Government spends some RM8,500 million and RM11,900 million in 2006 and 2007 respectively on fuel subsidy to help ease inflationary pressures. Retail prices of fuel for vehicles were raised in 2008 when world market prices of oil increased, and the government did not increase subsidy. Subsequently, a rebate was given for vehicles for the purpose of reducing the impact of price increase. It was pointed out that a common means of transport in Sarawak is by boat, for which a rebate will reduce the impact of the increase in the price of diesel.

9. Governance

The British colonists left independent Malaysia a legacy of efficient administrative system, managed by qualified personnel. Although decreasing standard of education has reduced the efficiency of the civil service, it has been more effective than those in many developing countries. The Malaysian civil service can successfully audit for non-compliance of legislature and disclosures.

However, the longevity of the ruling coalition and its strong position has undermined governance. The civil service is not totally independent; it has answered to the government in contradiction to established rules.

Within a month of the 2008 election, the Minister of Tourism said that tourism memorandums of understanding with opposition states would be terminated given the change in leadership. However, the minister soon relented.

Malaysia's corruption perception index increased slightly from 5.0 in 2006 to 5.1 in 2007 and 2008. It has been mediocre, with no improvement sisnce 2001 (Malaysia Today)

Malaysia also has a blanket official secret act with unlimited period of disclosure. One of the reasons for the voter shift away from the ruling coalition in the 2008 election is said to be a reaction to corruption. This includes reaction from socially-aware urbanised voters in the three more developed states of Perak, P. Pinang and Selangor, where the ruling coalition is concerned about alternative internet access to its controlled mainstream media (Aliran, 2008). Voter shift away from the ruling coalition may continue with progressing development.

10. Conclusion

Malaysia is blessed with petroleum resources that it exports and from which the government earns resource rents. The ownership of petroleum is vested in the federal-owned Petronas, which has efficiently developed upstream and downstream activities as well as integrate its operations with international ventures.

However, there have been frictions between the Federal Government and petroleum-producing states. The states get an equal amount of royalty as the Federal Government, but the Federal Government also gets enormous revenues from petroleum tax, dividend and other indirect taxes.

Federal-state conflicts on petroleum royalty parallel conflicts over annual federal grants to the states, expected as revenue assignments are centralised. While the grants are formulated to cater for compensation to the states, revenue-sharing, horizontal equalisation, support and prior agreements, they neither effectively address vertical disparity nor horizontal disparity. This probably explains interest in petroleum royalty for non-producing states.

The Federal Government supports the state governments in times of need, e.g. provide grants when they experience cash-flow difficulties or budgetary deficits, re-schedule loans for development projects. In the post

1997/98 financial crisis era, the government adopts counter-cyclical stance to improve on "fiscal prudence" during the budgetary deficits of the 1980s.

The constitution makes for a centralised federation to facilitate administration. The longevity of the ruling coalition leads to a strong government and MPs allegiance to the ruling coalition led to further centralisation. The civil service is not totally independent; it has answered to the government and contravened established rules.

Opposition-controlled state governments have been discriminated in budgetary allocations, aggravating regional disparities when less developed states are controlled by the opposition. In the circumstances, rising oil prices have and will further aggravate disparities.

Malaysia's relative status in corruption has deteriorated and it is said that current voter shift away from the ruling coalition is a reaction to corruption. Newly opposition-controlled states are more developed, suggesting continued voter shift as development progresses.

Malaysian states are heterogeneous culturally and economically. While horizontal disparities need to be addressed, vertical disparity is the more urgent concern within the backdrop of resource constraints such as the depletion of petroleum resources.

Demand for vertical equalisation will spread as the number of opposition-controlled states increase. The alternative coalition, led by a charismatic ex-minister who is alleged to have personally experienced bad treatments under a civil service that answers to the government, may well play a more significant role in Malaysian federalism.

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Table 1. The Malaysian Federation, 2008

No.	State	Area[1] (sq. km)	Population ('000) [2]	Population per sq. km	No. of MPs[3]	Ruler's status	Major state representation	Development composite index, 2000	Region[5]
1	Johor	18,987	3,240.9	171	26	Royal	National coalition	100.5	South
2	Melaka	1,652	738.8	447	6	Appointed	National coalition	104.2	Central
3	N. Sembilan	6,657	978.2	147	8	Royal	National coalition	102.3	Central
4	Selangor	7,979	4,961.6	622	22	Royal	Alternative	103.2	Central
5	P. Pinang	1,030	1,5185	1,474	13	Appointed	Alternative	105.7	North, island
6	Perak	21,005	2,314.6	110	24	Royal	Alternative	100.4	North
7	Perlis	795	231.9	292	3	Royal	National coalition	99.9	North
8	Kedah	9,425	1,918.7	204	15	Royal	Alternative	97.8	North
9	Pahang	36,5965	1,483.6	40	14	Royal	National coalition	97.6	East
10	Terengganu	12,955	1,067.9	82	8	Royal	National coalition	96.2	East
11	Kelantan	15,020	1,560.5	104	14	Royal	Alternative	93.1	East
12	Sabah	73,622	3,063.6	42	25	Appointed	National coalition	90.0	Borneo
13	Sarawak	124,450	2,404.2	19	31	Appointe	National	96.6	Borneo

						d	coalition		
	Malaysia	329,876	27,173.6	82	222	Royal	National coalition	100.0	

[1] Federal Territory of Kuala Lumpur – 243 sq. km, Federal Territory of Putrajaya – 49 sq. km, Federal Territory of Labuan – 91 sq. km

[2] 2007 estimate, for which Federal Territory of Kuala Lumpur – 1,604,400, Federal Territory of Labuan – 86,300

[3] Federal Territory of Kuala Lumpur – 11 MPs, Federal Territory of Putrajaya – 1 MP, Federal Territory of Labuan – 1 MP

[4] Federal Territory of Kuala Lumpur – 109.6

[5] Peninsula, except for Borneo island

Source: Malaysia, Department of Statistics; Malaysia, Election Commission; Malaysia, Parliament; *The Ninth Malaysia Plan, 2006-2010*, Table 17-1

Table 2. Malaysia: Federal and State Government Functions

Federal

1. External affairs
2. Defence
3. Internal security
4. Civil & criminal law & the administration of justice
5. Federal citizenship & naturalization; aliens
6. Federal government machinery
7. Finance
8. Trade, commerce & industry
9. Shipping, navigation & fishery
10. Communication & transport
11. Federal works & power
12. Survey, inquiries & research purposes
13. Education
14. Medicine & health
15. Labour & social security
16. Welfare of aborigines
17. Professional licensing
18. Federal holidays, standard of time
19. Unincorporated societies
20. Agricultural pest control
21. Publications
22. Censorship
23. Theatres & cinemas
24. Co-operative societies
25. Prevention & extinguishment of fires

Shared Functions

1. Social welfare
2. Scholarship
3. Protection of wild animals & birds, national parks
4. Animal husbandry
5. Town & country planning
   Vagrancy & itinerant hawkers
6. Public health
7. Drainage & irrigation
8. Rehabilitation of mining land & land which has suffered soil erosion
9. Fire safety measures
10. Culture & sports
11. Housing

State

1. Muslim laws & customs
2. Land
3. Agriculture & forestry
4. Local government
5. Local public services: boarding houses, burial grounds, pounds & cattle trespass, markets & fairs,
6. Licensing of theatres & cinemas
7. State works & water
8. State government machinery
9. State holidays
10. Inquiries for state
11. Creation of offences & indemnities related to state matters
12. Turtles & riverine fishery

Supplementary List for Sabah and Sarawak

12. Native law and custom
13. Incorporation of state authorities & other bodies
14. Ports & harbours other than those declared federal
15. Cadastral land surveys
16. In Sabah, the Sabah Railway

Additional Shared Functions for Sabah and Sarawak

12. Personal law
13. Adulteration of foodstuff & other goods
14. Shipping under fifteen tons
15. Water power
16. Agricultural & forest research
17. Charities & charitable trusts
18. Theatres, cinemas & other places of amusement

Source: Government of Malaysia, *Constitution of Malaysia*, Ninth Schedule

Table 3. Malaysia: Federal and State Government Revenue

	Federal		State
	Tax Revenue		*Tax Revenue*
1.	Direct taxes	1.	Import & excise duties on
i.	Income taxes:		petroleum products, export
	Individual		duties on timber & other forest
	Companies		products for Sabah & Sarawak,
	Co-operatives		excise duty on toddy for all
	Petroleum tax	2.	states
	Development tax	3.	Forests
	Film hire duty	4.	Lands & mines
ii.	Taxes on property & capital gains:		Entertainment duties
	Real property gain tax		
	Estate duty	1.	Other Receipts
	Share transfer tax on land-based	2.	Licences & permits
	companies	3.	Royalties
2.	Indirect taxes	4.	Service fees
i.	Taxes on international trade:		Commercial undertakings:
	Export duties	5.	water, gas, ports & harbours
	Import duties	6.	Receipts from land sales
	Surtax on imports	7.	Rents on state property
ii.	Taxes on production & consumption:	8.	Proceeds, dividend & interests
	Excise duties		Federal grants &
	Sales taxes		reimbursements
	Service taxes		
iii.	Others		
	Stamp duties		
	Gaming tax		
	Betting & sweepstakes		
	Lotteries		
	Casino		
	Pool betting duty		
	Non-tax Revenue and Other Receipts		
1.	Road tax		
2.	Licences		
3.	Service fees		
4.	Fines & forfeitures		
5.	Interests		
6.	Contributions from foreign		
7.	governments		
8.	Revenues from federal territories		

9.	Refund of expenditures
	Receipts form other government
10.	agencies
11.	Revenues from federal territories
	Royalties/gas cash payments

Source: Government of Malaysia, *Constitution of Malaysia*, Tenth Schedule

Table 4. Malaysia: Federal and State Government Finance, 1963-2007 (RM million)

	Revenue		Expenditure		Overall balance (% of revenue)	
	Federal	State	Federal	State	Federal	State
1963-65	4,188 (80.5%)	1,013 (19.5%)	5,486 (80.5%)	1,331 (19.5%)	-31.0	-31.5
1966-70	9,897 (77.9%)	2,806 (22.1%)	12,496 (80.7%)	2,998 (19.3%)	-26.3	-6.8
1971-75	18,645 (80.5%)	4,513 (19.5%)	25,397 (81.6%)	5,738 (18.4%)	-36.2	-27.1
1976-80	47,189 (80.8%)	11,223 (19.2%)	58,858 (83.7%)	11,456 (16.3%)	-24.7	-2.1
1981-85	93,025 (82.5%)	19,735 (17.5%)	128,575 (84.0%)	24,547 (16.0%)	-38.2	-24.4
1986-90	114,422 (79.3%)	26,828 (20.7%)	138,218 (83.6%)	27,149 (16.4%)	-20.8	-1.2
1991-05	215,394 (85.4%)	36,780 (14.6%)	212,654 (84.8%)	38,075 (15.2%)	1.3	-3.5
1995-2000	301,265 (86.5%)	47,191 (13.5%)	327,026 (87.7%)	45,716 (12.3%)	-8.6	3.1
2001-05	461,391 (90.7%)	47,157 (9.3%)	560,137 (92.1%)	47,741 (7.9%)	-21.4	-1.2
2006	123,546 (90.7%)	12,742 (9.3%)	142,655 (92.5%)	11,568 (7.5%)	-15.5	9.2
2007 estimate	141,790 (90.9%)	14,146 (9.1%)	161,738 (91.7%)	14,735 (8.3%)	-14.1	-4.2

Note: Figures in brackets indicate per cent of total revenue/expenditure.
Sources: Ministry of Finance, Malaysia. *Economic Report*, various issues

Table 5. Malaysia: Oil and Gas Production, Utilisation and Trade

Year	1977	1980	1985	1995	2006
Crude oil and condensate (million ton.)	8.892	13.245	21.246	33.327	31.516
Crude oil per capita (ton.)	0.71	1.01	1.34	1.61	1.18
Natural gas (‘000 m. std cu. ft)	n.a.	93	2,85	1,237	2,108
Natural gas per capita (‘000 m. std cu. ft)	n.a.	7	18	60	79
GDP per capita (RM)	2,571	4,058	5,247	11,495	21,073
Incidence of poverty	37.7[1]	n.a.	20.7[2]	9.6	5.7[3]
Sabah	58.3[1]	n.a.	33.1[2]	22.4	23.9[3]
Sarawak	56.5[1]	n.a.	31.9[2]	10.0	7.5[3]

Terengganu	60.3[1]	n.a.	28.9[2]	24.3	15.4[3]
No. of refineries	6	6	10	11	n.a.
Kerosene (‘000 ton.)	n.a.	n.a.	447	1,877	3,307[4]
LPG (‘000 ton.)	n.a.	n.a.	306	1,317	3,807[4]
Fuel oil (‘000 ton.)	n.a.	n.a.	1,571	2,307	1,597[4]
Diesel/gas oil (‘000 ton.)	n.a.	n.a.	1,011	5,918	8,806[4]
Gasoline (motor spirit) (‘000 ton.)	n.a.	n.a.	1,029	2,244	5.759[4]
m. kwh electricity from diesel stations (% total electricity)	n.a.	1,560 15.3%	1,607 10.7%	2,009 4.3%	24,263 3.2%
Sabah	n.a.	510 100%	704 5.3%	914 42.6%	2592 63.2%
Sarawak	n.a.	355.3 92.7%	580 60.5%	269 10.8%	296 4.9%
m. kwh electricity from gas turbines (% of total electricity)	n.a.	325 3.2%	2,733 18.2%	23,739 50.9%	65,188 64.4%
Sabah	n.a.	-	2419 18.1%	478 22.3%	655 16.0%
Sarawak	n.a.	28 7.2%	131 13.6%	1699 68.4%	4076 68.2%
Exports of mineral fuels, lubricants (RM m.) (% of total exports)	2,101 14.0%	6,898 24.5%	12,051 31.7%	12,932 7.0%	80,871 13.7%
Imports of mineral fuels, lubricants. (RM m.) (% of total imports)	1,422 12.7%	3,554 15.2%	3,722 12.2%	4,351 2.2%	4,3054 9.0%
Crude oil exports (‘000 ton.)	7,354	11,227	16,701	19,165	16,866
Crude oil imports (‘000 ton.)	n.a.	3,961	2,252	1,271	10,239
Crude oil (% of export value)	12.7	23.8	22.9	3.6	5.4
Crude oil (% of import value)	6.6	minimal	3.7	0.2	3.7
Petroleum products exports (‘000 ton.)	270	280	1,844	6,560	13,021
Petroleum product imports (‘000 ton)	n.a.	3,193	3,864	7,402	13,021
Petroleum products (% of export value)	0.9	0.7	2.6	1.3	2.2
Petroleum products (% of import value)	n.a.	6.6	7.7	1.7	4.3
LNG exports (‘000 ton.)	n.a.	n.a.	n.a.	9,727	21,534
LNG (% of export value)	n.a.	minimal	6.0	1.7	4.0

n.a. not available

[1] 1976 [2] 1984 [3] 2004 [4] 2007 estimate

Note: Figures in brackets indicate % of total concerned

Sources: Malaysia – Yearbook of Statistics, various issues.

Table 6. Malaysia: Federal Government Revenue from Petroleum, 1971-1990 (RM million)

	Royalties	Petreoleum tax	Dividend	Export duties
1980-85	2,878 (2.7%)	13,487 (12.6%)	n.a	8,056 (7.5%)
1986-90	2,594 (2.3%)	11,304 (9.9%)	11,800 (10.3%)	6,845 (6.0%)
1991-95	3,726 (1.7%)	14,724 (6.8%)	15,500 (7.2%)	6,979 (3.2%)
1996-2000	5,678 (1.9%)	18,976 (6.3%)		4,687 (1.5%)
2001-2005	11,533 (2.5%)	52,006 (11.3%)		6,273 (1.4%)

n.a. – not available
Figures in brackets indicate % of federal government revenue.
Sources: Calculated with data from Accountant-General of Malaysia, Ministry of Finance, Malaysia, Department of Custom and Excise, Malaysia.

Table 7. Malaysia: Development Allocations by State, 1976-2005 (RM million)

	3MP 1976-80	4MP 1981-85	5MP[1] 1986-90	6MP[2] 1991-95	7MP[2] 1996-2000	8MP[2] 2001-05
More developed states:						
Johor	1,832 (2)	2,929 (4)	4,529 (1)	3,794 (2)	3,613 (4)	5,937 (4)
Melaka	328 (12)	940 (12)	520 (13)	924 (11)	1,191 (12)	2,465 (11)
N. Sembilan	617 (11)	1,131 (11)	1,302 (10)	1,548 (10a)	1,801 (11)	5,221 (5)
Perak	1,792 (3)	2,834 (6)	3,738 (6)	2,563 (7)	3,216 (6)	4,849 (7)
P.Pinang	894 (9)	1,236 (10)	1,257 (11)	1,548 (10b)	1,968 (9)	4,040 (8)
Selangor[3]	1,413 (6)	3,677 (1)	4,365 (2)	4,295 (1)	4,296 (3)	7,848 (3)
Less developed states:						
Kedah	854 (10)	2,389 (8)	2,659 (9)	2,826 (5)	3,341 (5)	5,180 (6)
Kelantan	1,019 (7)	2,848 (5)	3,621 (7)	2,064 (9)	1,850 (10)	2,905 (10)
Pahang	2,054 (1)	2,944 (3)	4,118 (3)	2,837 (4)	3,090 (7)	3,821 (9)
Perlis	156 (13)	304 (13)	560 (12)	505 (12)	953 (13)	1,581 (13)
Sabah	1,452 (5)	3,172 (2)	3,913 (4)	2,307 (8)	4,495 (2)	7,990 (2)
Sarawak	1,657 (4)	2,608 (7)	3,464 (8)	3,209 (3)	4,548 (1)	8,676 (1)
Terengganu	911 (8)	2,023 (9)	3,790 (5)	2,729 (6)	2,553 (8)	2,443 (12)

Figures in brackets indicate ranking from highest to lowest.

[1] Federal Government and Non-Financial Public Enterprise (NFPE) development
allocations only.
[2] Federal development government allocations only.
[3] Excludes the Federal Territory of Kuala Lumpur
Sources: various Malaysia Plan documents

Table 8. Malaysia: Development Allocations Per Capita by State, 1976-2000 (RM)

	3MP 1976-80	4MP 1981-85	5MP[1] 1986-90	6MP[2] 1991-95	7MP[2] 1996-2000	8MP[2,4] 2001-05
More developed states:						
Johor	1,160 (6)	1,668 (11)	2,251 (7)	1,800 (6)	1,383 (12)	2,166 (12)
Melaka	672 (13)	1,948 (7)	927 (13)	1,600 (8a)	2,026 (7)	3,877 (5)
N. Sembilan	1,064 (8)	1,884 (9)	1,876 (10)	2,100 (4)	2,188 (5)	6,072 (2)
Perak	946 (10)	1,513 (12)	1,742 (11)	1,200 (10)	1,527 (10)	2,364 (10)
P.Pinang	981 (9)	1,232 (13)	1,137 (12)	1,499 (9)	1,595 (9)	3,076 (6)
Selangor[3]	704 (12)	2,161 (5)	2,321 (6)	2,200 (3)	1,389 (11)	1,873 (13)
Less developed states:						
Kedah	740 (11)	2,057 (6)	1,962 (9)	2,000 (5a)	2,149 (6)	3,140 (5)
Kelantan	1,184 (5)	2,952 (4)	3,143 (3)	1,700 (7)	1,247 (13)	2,212 (11)
Pahang	3,247 (1)	3,240 (2)	4,102 (2)	2,700 (2a)	2,443 (3)	2,966 (8)
Perlis	1,100 (7)	1,945 (8)	3,111 (4)	2,700 (2b)	4,293 (1)	7,733 (1)
Sabah	1,521 (3)	2,831 (3)	2,856 (5)	1,600 (8b)	1,598 (8)	2,982 (7)
Sarawak	1,391 (4)	1,854 (10)	2,175 (8)	2,000 (5b)	2,285 (4)	4,188 (3)
Terengganu	1,781 (2)	3,462 (1)	5,361 (1)	3,700 (1)	2,543 (2)	2,718 (9)

Figures in brackets indicate ranking from highest to lowest.
[1] Federal Government and Non-Financial Public Enterprise (NFPE) development
allocations only.
[2] Federal development government allocations only.
[3] Excludes the Federal Territory of Kuala Lumpur
[4] Using population for 2000
Sources: Calculated with data from various Malaysia Plans and *Yearbook of Statistics, Malaysia*

Table 9. Malaysia: Incidence of Poverty by State, 1976-2004 (per cent)

	1976	1984	1987	1990	1995	1997	1999	2002	2004
More developed states:									
Johor	29.0 (12)	12.2 (12)	11.1 (12)	10.1 (10)	3.1 (12)	1.6 (10a)	3.1 (10)	1.8 (10)	2.0 (9)
Melaka	32.4 (11)	15.8 (8)	11.7 (11)	12.4 (8)	5.3 (9)	3.6 (9)	2.9 (11)	2.7 (8)	1.8 (10)
N. Sembilan	33.0 (9)	13.0 (11)	21.5 (7)	9.5 (11)	4.9 (10)	4.5 (7a)	4.1 (9)	2.2 (9)	1.4 (11)
Perak	43.0 (7)	20.3 (7)	19.9 (8)	19.4 (6)	9.1 (7)	4.5 (7b)	6.8 (8)	10.1 (4)	4.9 (7)
P. Pinang	32.4 (10)	13.4 (10)	12.9 (9)	8.0 (12)	4.0 (11)	1.6 (10b)	0.7 (13)	1.4 (11)	0.3 (13)
Selangor	22.9 (13)	8.6 (13)	8.9 (13)	7.8 (13)	2.2 (13)	1.3 (11)	1.9 (12)	1.1 (12)	1.0 (12)
Less developed states:									
Kedah	61.1 (2)	36.3 (2)	31.3 (4)	30.0 (3)	12.2 (4)	11.5 (4)	14.2 (4)	10.7 (3a)	7.0 (5)
Kelantan	67.1 (1)	39.2 (1)	31.6 (3)	29.9 (4)	22.9 (2)	19.5 (2)	25.2 (1)	12.4 (2)	10.6 (3)
Pahang	38.9 (8)	15.7 (9)	12.3 (10)	10.3 (9)	6.8 (8)	4.1 (8)	9.8 (7)	7.9 (5)	4.0 (8)
Perlis	59.8 (4)	33.7 (3)	29.1 (5)	17.2 (7)	11.8 (5)	10.6 (5)	13.6 (5)	3.8 (7)	6.3 (6)
Sabah	58.3 (5)	33.1 (4)	35.3 (2)	34.4 (1)	22.4 (3)	22.1 (1)	23.4 (2)	16.0 (1)	23.0 (1)
Sarawak	56.5 (6)	31.9 (5)	24.7 (6)	21.0 (5)	10.0 (6)	7.5 (6)	10.9 (6)	5.8 (6)	7.5 (4)
Trengganu	60.3 (3)	28.9 (6)	36.1 (1)	31.2 (2)	24.3 (1)	17.3 (3)	22.7 (3)	10.7 (3b)	15.4 (2)

Sources: various Malaysia plan documents.