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The Implications of Petroleum Conflict in the Context of the Federal Government and the Kelantan State Government Relations

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Abstract

Malaysia is one of those countries that rely on petroleum-based revenues as one of its main sources of national income. The majority of its oil fields are found in the coasts of Kelantan, Terengganu, Sabah and Sarawak. Upon the discovery of these, Malaysia had incorporated a national petroleum company named “Petronas” on 17th August 1974 to manage all related matters to exploration and exploitation of petroleum in the country. Subsequently, on 1st October 1974, the Parliament had passed Petroleum Development Act 1974 that, inter alia, gives the power and right for exploration and exploitation of petroleum to Petronas and to pay 5% of oil royalty to the petroleum-producing states. However, due to ideological differences between the federal government and the state government of Kelantan, this lucrative natural source has found itself at the center of conflict between the two. The study analyzes the implication of such a petroleum-based conflict against the federal-state relations within a context of a democratic Malaysia. In order to do so, as far as oil royalty payment arrangement is concerned, the concept of federalism was applied as a tool of analysis to evaluate the extent of the effectiveness of the relations between the federal government and the state government of Kelantan. Pursuant to that, the discussion of this study revolves around qualitative data approach based on documents related to the oil royalty agreement between the federal government and state government of Kelantan. The analysis has indicated that Malaysia, as a federalist country, has failed to put into practice the true concept of federalism. One of the major reasons behind this was conflicting political interests. The impacts of such could be seen from the distinctive way the federal government treated the state governments, in this case Kelantan, whose state government was formed by the opposition political party. The Malaysian federal government's extensive power and the different constitutional interpretation also contributes to the conflict especially in the context of the federal legislative policies that often being perceived as discriminating against the state government.

Keywords: Petroleum, Royalty, Federalism, Kelantan, Federal.

Introduction

Political differences in the context of a democratic state is one of the integral factors that triggered various conflicts. It can negatively affect the relations between the governments as well as pushing the peoples out to the street demanding their rights. This is not unusual in the context of where the central government perceived as failed to deliver just distribution of public goods merely due to political ideology differences. In the Malaysian context, the federal-state relations are more often than not soured into national conflict – especially when it involves a state that is being administered by opposition party that holds contrary ideology as compared to the one that control the federal government. This is precisely the case of PAS state government in Kelantan since 1990. Therefore, this research examines the issue of Kelantan state government demands of petroleum royalty from the federal government following the query by the Kelantan's side in the early 2009. Federal government dismissal of the demand by the state government triggered a mass responds among the Kelantanese. This scenario has resulted in a number of political, economic, and social implications to the state administration that shall be discussed in this article.

Concept of Federalism in the Context of Kelantan's Petroleum

Federalism as a subject in the political science discipline has drawn the interests of scholars especially since the end of World War II in 1945. Fresh from the war, new and old nation-states were concerned with finding the best possible form, formula and format of political systems to be practiced. As of today, out of 193 countries, only 24 use the federalist political system. These federalist countries, in turn, account for 45% of the world's population. In addition to that, the historical and economic factors also play a role in the emergence of federalist system. Besides, this system also has a number of major attractions. They, inter alia, include the aspect concerning the separation and division of resources and jurisdiction of power over a government and territory.

The adoption of federalism as a political system also can serve as an equalizer between the federal government and the state particularly when it comes to decision-making and public policy. In principle, the concept of federalism defines the nature of relationship between both the federal and state governments. The most important aspect of such relationship is the clear and separate jurisdiction and power delineation between the two sets of governments. Furthermore, just in many other federal states such as the United States of America as an instance, state governments enjoy certain degree of autonomous power that enables or allows them to function and run their matters within their jurisdiction effectively and systematically.

In Malaysia, the practise of federalism and the consequential division of power is clearly stated in the Ninth Schedule of Malaysian Federal Constitution that outlines separate jurisdictions and powers between the federal and state governments. The schedule has three lists known as The Common List, State List and Federal List. As the names of the lists themselves suggest, each list contains state and federal matters that fall within the jurisdiction of the federal, state and both. Nonetheless, according to Wheare (1967:33), for a country that does not implement federalism in full and freely, then it falls under a quasi-federalism system. Wheare develops his understanding of federalism from his studies on previous researches of similar topic

such as those of Livingstone (1956), Birch (1957) and Riker (1964, 1975). While Livingstone (1956:1-2) argues that federalism must emphasize on the aspect of sovereignty and control over economy, politics, social and culture, Birch (1957), defines the meaning of federalism as “in which there is a division of powers between one general and several regional authorities, each of which, in its own sphere, is co-ordinate with the others, and each of which acts directly on the people through its own administrative agencies”. Hence, in spite of the division of power between the federal and state governments, Birch insists that the system of federalism does not, in essence, denote total separation between the two governments as both are still bound by the treaty or agreement as described in the study done by Wheare.

All in all, the preceding discussion on federalism has three key points. Firstly, Wheare notes that the concept of federalism only revolves around the separation of jurisdiction between the federal and state government and for which both must be let free to run own affairs without intervention from and by one another. Secondly, Livingstone argues that federalism as defined by Wheare does not go only around the aspect of separate jurisdiction over the administrative realm. It, thus, should also extend into the realms of politics, social, economy and culture. All of these, Livingstone adds, must be coordinated and synchronized well as prescribed precisely by the constitution. Thirdly, although Birch agrees with Wheare’s contention about the concepts of power and jurisdiction in federalism, he offers different way of looking at the concepts. For Birch, the concept of freedom to rule does come with a certain limitation which, can be attributed to different and unique patterns of leadership and politics.

In the context of power division in Malaysia, Part VII of the Federal Constitution states that, except for proceeds from land and forestry resources, the federal government has the right to all major natural resources of the country. Correspondingly, it also serves as a guarantee that the state governments’ incomes derivable from state lands, mining sector and forestry will not be abridged (Mohamad, 2013:28). Besides, the constitution also states the right of the state government to impose and collect import duty for its natural resources i.e. tin, iron and petroleum as provided for by Article 110 (3A) (Mohamad, 2013: 28) This provision benefits significantly states rich in natural resources like Perak, Terengganu, Kelantan, Sabah and Sarawak.

Subsequently, Petroleum Development Act 1974 gives the power and right for exploration and exploitation of petroleum whether onshore or offshore to “Petronas” - an incorporated national petroleum company. Through this act, among other things, states vest or assign their ownership in and the exclusive rights, powers, liberties and privileges in respect of the said petroleum, and to control the carrying on of downstream activities and development relating to petroleum and its products to Petronas (The Commissioner of Law Revision, Malaysia, Petronas Act, 2006: 5). State governments, in consequence to that, are entitled to receive 5% of petroleum-based income (oil royalties) from Petronas, as provided for in Section 4 of the same act that specifically mentions “In return for the ownership and the rights, powers, liberties and privileges vested in it by virtue of this Act, the Corporation shall make to the Government of the Federation and the Government of any relevant State such cash payment as may be agreed between the parties concerned” (The Commissioner of Law Revision, Malaysia, 2006: 7).

Largely, the issue of oil royalties in Malaysia had only begun to make headlines nationwide when rival political parties won the state-level election and with that win, the right to form the state government. The cases of Terengganu in 1999 and Kelantan in 2004 can illustrate such an event. The cases of Sabah and Sarawak, on the other hand, were different as both were controlled by political parties who also happened to be part of the grand political coalition that formed the federal government. This put both to be under control of practically the same political parties. The cases of Terengganu and Kelantan, however, indicates that the federal government appeared to have denied due recognition of the right and sovereignty of the state government formed by rival political parties who had legally won the state-level election. In more ways than one, such can be seen as a deviation from the federalism concept. Besides, as Elazar (2008:2) puts it, the federalism is a system of multi-level government, mutually institutive, cooperative and respectful to and of each other's jurisdiction and scope of power. What had happened to Terengganu and Kelantan in 1999 and 2004 were evidently not what Elazar has in mind about what a federalism system is.

Implication of Oil Royalti Claim to the Relations Between the Federal Government and the State Government of Kelantan

The decision by the federal government to deny Kelantan's oil royalty has brought about a number of implications to the administration of the state government. Among others, it has halted the state's development projects as the state coffers do not have sufficient funds to finance those projects meant for the political, economic and social interests of the people. Besides, the state's income is basically much lower compared to those of other states in Malaysia. Specifically, Kelantan's state income was RM549.26 million in 2014, RM530.83 million in 2015, RM 593.80 million in 2016 and RM636.98 million in 2017 (Utusan Malaysia Online, 26 October 2016).

As a general rule of thumb, these are considered as lower than those of other states in Malaysia. Such a dire financial condition has made the oil royalty appears to be all the more important and significant for Kelantan to ensure smooth execution of developmental projects in the state. Consequently, Kelantan has filed a claim for its oil royalty from the federal government for oil explored and exploited in its coast from year 2004 until 2017 amounting to RM17 billions. As stated earlier, these oil royalties are integral to fund development and administrative expenses of the state in just as much as the need for the state to keep up with the national target to realize Vision 2020 (Kelantan Chief Minister Incorporated, 2016).

The conflict over Kelantan's oil royalty has severely strained the relations between the federal government and the state government of Kelantan. It has resulted in unfavorable and loss of spirit of consensus between the two vis-à-vis the welfare of and development for the people. As a matter of fact, such an action by the federal government represents a gross violation of the concept of federalism. It is obviously a unilateral decision because the state government of Kelantan, legally elected by the people in the national elections, has never been consulted. Pursuant to that, the federal government has stopped paying the oil royalty payment directly to the state government of Kelantan. It has been otherwise deposited into the account of Jabatan Pembangunan Persekutuan Negeri - JPP (Federal State Development Agency). JPP is put to be in

charge of managing the cash flow and expenses of the state government. Not only is this a clear denial of the right of the state government, it is also a breach of the state's sovereignty within the Federation of Malaysia. Besides, looking from the legal context, the federal government's action could be interpreted as an infringement of Article 80 of the Federal Constitution which, in the absence of mutual consent or joint agreement, prohibits the Federal Government from interfering into State's jurisdiction.

Moreover, such a deliberate action of the federal government might have as well caused a substantial impact on the state's border and in this case that of Kelantan. Assuming that the trial of Kelantan's oil royalty were to go in favor of the state i.e. coastal areas within the distance of 3 nautical miles from the shore to belong to Kelantan, then the federal government's action would have evidently and conveniently contradicted Article 2 (b) of the Federal Constitution. The article, for its part, deals with the state's borders for which delimitation or change, if any, can only be done in collusion with the Council of Rulers. In the case of Kelantan's oil royalty issue, the Council of Rulers, including His Majesty Sultan of Kelantan himself, has never consented any proposed change of the state's border.

Additionally, without the oil royalty, the state government of Kelantan has been forced to continually review and even forced to suspend or put on hold all its policies meant for the welfare of the people as stated in its 13th national election manifesto. In view of the lack of funds, the state government finds itself left with no available alternative but to adopt a policy of austerity that comes with a series of cost-cutting measures. In other words, the state has to inevitably reconsider its agenda. Since development projects usually incur huge expenses, the state government has to push developments and infrastructure projects to the lower rungs of the state's priority in favor of the other more pressing agendas. By equal measure, by denying oil royalty to the state government of Kelantan, the federal government has uncharacteristically discouraged some potential foreign investments for which the country needs to better its economic standing. In a hindsight, the history of conflicts between the federal government and state government vis-à-vis the distribution of oil royalty has directly influenced the foreign investors' confidence in the integrity of federalism and legal system of the country.

In addition to that, the inconsistent and unstable geopolitics has also affected the activities of Petronas itself since part of its revenues comes from its overseas ventures. Tan Sri Azizan Zainal Abidin, Chairman of Petronas, affirms that Petronas has sizeable interests in 24 countries with which it enjoys good relations in terms of petroleum economy. The importance of petroleum economy is proven by Petronas's oil and gas pipe development project in Sudan, acquisition of petroleum processing engine in South Africa, new mainstream joint development project in Pakistan and Gabon, oil and gas development venture in Iran as well as Thailand-Malaysia joint development project (Azizan, 2000:1).

As aforementioned earlier, the oil royalty issue has seriously put the relations between the federal government and state government of Kelantan under duress. This was evident when it has taken legal action to claim its outstanding oil royalty from Petronas and the federal government on 30th August 2010. It is a legal recourse by the state government to force both

defendants to pay Kelantan's oil royalty, derivable from its shore, direct to the state treasury (Agendadaily Online, 2014). The action taken by the state government of Kelantan is based on petroleum exploration agreement signed on 9th May 1975 which categorically states that Petronas is obliged to make cash payment to the tune of 5% from petroleum-related revenues explored and exploited in the state's shores twice a year i.e. early March and September (Agendadaily Online, 2014).

Furthermore, Kelantan's state finance had also been badly affected by the federal government's refusal to pay the oil royalty. In 2016, its revenue was RM593.80 million with a deficit of RM45.6 million. A year before, Kelantan's revenue was RM530.83 million with a deficit of RM70.69 million (Malaysiakini Online, 2015). True to form, these persistent deficits have, in more ways than one, upset the state's development and economic growth especially in the welfare context of the 1.5 million Kelantanese. Evidently, the denial of oil royalty has created a huge gap between the federal-state relations within the context of federalism which purportedly takes pride in the division of powers between the state and the federal government as provided for by the Ninth Schedule of the Federal Constitution. Needless to say, as a federal county, Malaysia has three distinct levels of governments: federal, state and local. These divisions of powers, to a great extent, are a true representation of a federalist system (Riker 1975:13). In relation to that, the separation of powers between the executive and the legislative bodies of the federal government and those of the state is also clearly stated in the Federal Constitution i.e. Article 71-81. These articles provide for a guarantee of power for the state government such as in terms of state legislation and the rights of the state government over the federal.

Going back to the oil royalty case, it is to be stressed here again that Petroleum Development Act 1974 gives the power and right for exploration and exploitation of petroleum whether onshore or offshore to Petronas. Based on the act, "Petronas is legally bound to make 5% cash payment off petroleum explored and exploited within the shores of Kelantan." As such, Petroleum Development Act 1974, co-signed by former Kelantan Chief Minister Dato' Mohammad Nasir and Petronas, has unmistakably indicated that Kelantan does enjoy the inalienable right over its Petroleum resources and with it the obligation of the federal government to make the due payment to the state government under the spirit of true federalism founded on common interests.

Research Interest

The importance of this study is the act of denying Kelantan's petroleum royalty explained by Petroleum Development Act 1974 approved in Parliament. This act had limitations and did not serve as the highest legal source in the Malaysian constitution for being contaminated with power and political interests of the central ruling party. As explained in previous discussions, the previously enforced Petroleum Development Act granted the right to any state in Malaysia with a five per cent payment method on petroleum products acquired within the waters of a state. However, in the context of this study, laws pertaining to petroleum were made without the legal function being due to unprofessional political intervention.

Additionally, the study found that the Territorial Sea Act 2012 approved by Parliament has violated the Petroleum Development Act 1974 by revoking the power and role of the original act. This study found that the Territorial Sea Act 2012 was a political game ruled by the federal government in charge of replacing the Emergency Ordinance 1969, which was abolished on 24 November 2011. It can be summarized that the Territorial Sea Act 2012 enforced by the federal government in response to deny the State Government Kelantan rights on its oil royalty.

Subsequently, the study found that Malaysia is a country that practicing the concept of federalism partially in the division of power between the federal and state governments. In this case, Malaysia is only classified as quasi-federalism which only applies part of the characteristics of federalism over the state government as explained by the Wheare scholar (1967: 33). These implications showed in the case of Terengganu and Kelantan oil royalty after the state government was dominated by the opposition, thus led the federal government to withdraw all the privileges of the state. In fact, the same situation has never happened in the case of state oil royalty of Sabah and Sarawak, while the state power is governed by a party that seals with the federal government.

At the meantime, this study is a corpus of knowledge and references to other states in Malaysia that are likely to have a petroleum resource as a guide. This is particularly important when the power of state administration is governed by different governments of the ideology of the ruling party. For example, the Kelantan State Government's act of carrying out petroleum royalty cases in the Federal Court could be guided by other states, especially in understanding the procedures and measures to be taken. Therefore, this study suggest that other states review the agreed petroleum agreements in 1974 so petroleum conflicts can be resolved by mutual agreement.

Conclusion

The oil royalty issue of Kelantan has substantial political, social and economic impacts on the people and the state. The decision of the federal government to deny Kelantan its oil royalty has had considerable impact as the preceding discussion has shown especially on the aspects of administration and management of the state. Not only has this issue caused a massive loss to the state government, it has also made the multi-ethnic society of Kelantan to suffer as much. For all that it matters for, it is only pertinent that the federal government reconsiders the oil royalty agreement so that the state of Kelantan will be able to use the much-needed oil royalty to develop the state and address the welfare of the people, as in the other states within the federation. Having said that, the federal government has to accept the fact that the oil royalty does indeed belong to the state of Kelantan, jointly shared with the federal, and to make the payment twice a year as provided for by the 1975 agreement. On a final note, this study stresses that Kelantan is more than capable of realizing all its development plans once the oil royalty is paid in full without prejudice. Yet, if the federal government continues to fail to pay or return the long overdue oil royalty, the state's administration will definitely be in a prolonged crisis due to the lack of fund and allocation.

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