



Malaysia's Commitments to Services Liberalization under the Framework of General Agreement on Trade in Services (Gats) and Asean Framework Agreement on Services (Afas)

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ABSTRACT

Since the mid 1980s substantial amount of liberalization has taken place in the area of international trade and services. Much of this is inspired by WTO and various regional bilateral agreements. The main objective of this paper is to describe the extent of openness of Malaysia's services sector by analyzing the scope and coverage of Malaysia's commitments to services liberalization under the framework of GATS and AFAS.

Keywords: Services Liberalization, WTO, GATS, AFAS and Malaysia

Introduction

During the past three decades, world economy underwent rapid structural transformation. One of the major changes is the increasingly important role of the services sector. The importance of service trade liberalization is as recognized globally as the trade of goods due to the progressed made in recent years particularly in information communication technology, finance and telecommunication markets (OECD, 2002). In most countries the services sector is now becoming the largest economic sector as well as the most important source of jobs. In 1990, the services sector contributed more than 60 per cent of GDP in most of the developed countries while in developing countries of Asia it ranged between 40 to 45 per cent in 1990. In the period 1990 to 2005, the share of services in GDP remained more or less the same in many East and Southeast Asian countries while there has been a rise in its share in most of the South Asian countries (Karthikeyan, 2007).

Moreover, trade in services also has been growing even faster than merchandise trade (Arkell, 2001). Recent statistics revealed that global trade in commercial services has grown steadily at about 6 per cent per annum between years 1990-2000 (WTO, 2005). The service sector also account for some 40 per cent of the global annual stock of foreign direct investment (FDI) (WTO, 2005). The growing importance of service sector is further enhanced by the transition from a manufacturing based-economy to the knowledge based-economy that is being actively promoted in this millennium. Most countries follow a general pattern of economic development as suggested by Fisher-Clark Theory of stages of development (Katouzian, 1970). In the first stage of the industrialization process, there is a decline in the percentage share of the agricultural sector, in terms of both output and employment, and an expansion of the manufacturing sector. Meanwhile, in the subsequent stage, the services sector becomes prominent while the manufacturing sector declines in relative importance (Miles and Boden, 2000). The vital role that services sector are playing in the domestic economy as well as in international trade has received the attention it deserves with its inclusion for the first time in the GATT Uruguay Round negotiations under the aegis of General Agreement on Trade in Services (GATS) in 1995.

The GATS is the first and only set of multilateral rules governing international trade in services. The main objective of GATS is basically to promote the expansion of trade in services, progressive liberalization of such trade through negotiations, transparency of rules and regulations, and increasing participation of

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developing countries (WTO, 2005). The GATS covers all services except those supplied by a governmental authority on noncommercial basis and not in competition with other service suppliers (Chadha, 2002). Besides services liberalization at the multilateral level under GATS, the liberalization of services has also become an interest at the regional integration in all parts of the world. For instance, at the sub-regional level, the East Asia members of ASEAN concluded the ASEAN Framework Agreement on Services (AFAS), while Australia and New Zealand have concluded the Closer Economic Relations Agreement (CER) covering services trade. Meanwhile, Southern Cone Common Market (MERCOSUR) member countries of Latin America have also chosen to follow the GATS-type approach to open their services market on gradual basis. At the broader regional level, both Asia Pacific Economic Cooperation (APEC) grouping and the Free Trade Area of the Americas (FTAA) also have included services among their wide-ranging liberalization approach (Stephenson, 1999).

With globalization, the world economy is becoming rapidly integrated. Increased trade, investment, financial and information flows are stimulating the integration process. Moreover, the fast pace of internationalization of services with the establishment of the GATS in 1995 further expedites the liberalization of services sector. This will present new opportunities as well as challenges to economies and businesses. In this regard, the services sector should respond rapidly adjusting to demands for greater competitiveness, efficiency and productivity improvements in order to achieve the objectives free flows of services. The main objective of the present paper is to examine the extent of openness of Malaysia's services sector by analyzing on the scope of Malaysia's commitments to services liberalization under the framework of GATS and AFAS.

Malaysia's Commitments under GATS

The liberalisation of services can be defined as a process whereby measures are taken to expand market access to foreign services providers or to diminish discrimination against them vis-à-vis the domestic suppliers (WTO, 2005). Access to markets can be denied not only by border policies but also by domestic policies that limit the entry of foreign services providers. According to the MITI, Malaysia subscribes to the principle of progressive liberalisation in the services sector, as part of its overall development strategy of the services sector. An increasing number of the service sub-sectors have been liberalised over the years, both autonomously, as well as through commitments at the international level. Autonomous liberalization refers to action taken by member countries to liberalize their economic sector even though they did not make any commitment to do so under GATS or any other regional trade agreements. This approach gives more flexibility for member countries to take any position in the future whereby member countries may reverse liberal market access policies to respond to adjustment concerns, regulatory failures or simply the call for greater protection.

According to Services Sectoral Classification List, there are 12 services sectors that fall under the framework of GATS, that is: *business services, construction, educational services, financial services, health and social services, communication services, distribution services, environmental services, tourism, transport, recreational and sporting services and other services not included elsewhere*. One of the most striking features of GATS is the way in which it defines services trade. GATS define services trade as occurring through four possible modes of supply (See Table 1).

Table 1: Trade in services and mode of supply

Modes of Supply	Description
Mode 1 Cross border supply	The possibility for non-resident service suppliers to supply services cross-border into the Member's territory e.g. international telephone calls.
Mode 2 Consumption abroad	The freedom for the Member's residents to purchase services in the territory of another Member (e.g. tourism)
Mode 3 Commercial presence	The opportunities for foreign service suppliers to establish, operate or expand a commercial presence in the Member's territory, such as a branch, agency, or wholly-owned subsidiary e.g. foreign banks setting up its offices/branches in other member country
Mode 4 Movement of natural persons	The possibilities offered for the entry and temporary stay in the Member's territory of foreign individuals in order to supply a service.

Generally, countries make commitments on market access and national treatment through two types of schedule of specific commitments, namely sectoral schedules of commitments (specific sectors) and horizontal schedules of commitments (all sectors). Sectoral schedules of commitments refer to commitments made by countries on market access and national treatment in specific sectors. Meanwhile, horizontal schedules of commitment are general limitations placed on market access and national treatment on all sectors unless otherwise indicated. There are three important features of the commitment process. Firstly, member countries are free to decide which service sectors they wish to liberalize. If countries are unwilling or unprepared to open up a particular service sector, they have the flexibility to do so. This flexibility and voluntary provision have enabled countries to limit their commitments in sensitive and heavily regulated government and monopoly type of service sectors (Chadha, 2002).

Secondly, countries can specify in their schedules, the limitations and exceptions they wish to maintain on market access and national treatment. Market access limitations refer to restrictions on the entry of foreign services or service suppliers into the domestic market. Meanwhile, limitations on national treatment include laws, rules, or regulations that effectively discriminate against foreign in favour of domestic services and service suppliers, or provides for market competitive conditions that favour domestic over foreign services and service providers (Chadha, 2002). A third feature of the commitments structure is that the market access and national treatment commitments are made for each of the four modes of supply. As commitments are scheduled by modes of supply as well as by sector, limitations and conditions may apply either across all mode of supply or for a specific mode.

In this regard, there are two major approaches for the liberalization of the services sector, namely the positive-list and negative-list. A positive list approach is one where countries specify sectors which are covered or offered for commitments. In other words, countries list national treatment and market access commitments specifying the type of conditions under which foreign service suppliers can enter a given market or the type of treatment that will be granted to services or service suppliers in sectors included in the schedules of commitments. The specific commitments may be modified and withdrawn after a certain period of time, subject to negotiating appropriate compensation. Meanwhile, a negative list approach requires that countries specify the sectors that are not covered by commitments (Low and Matto, 1999).

Against this background, Malaysia's commitments in services sector under the Uruguay Round were essentially binding then existing levels of access for foreign suppliers. The commitments under the market access and national treatment provisions are subject to certain conditions or limitations in the four modes of supply. These include limitations on foreign equity ownership (generally 30 per cent), the requirement of foreign service suppliers to establish a commercial presence through joint-ventures with local firms and limitations on the number of foreign personnel allowed to provide the services.

Malaysia is regarded as being defensive in the GATS negotiations due to the high level of protection of the services markets (MITI, 2005). Nonetheless, Malaysia's services offer involved a wide coverage of sectors and substantive bindings of current policies. So far, Malaysia has made commitments in 83 services activities including both the financial and non-financial sectors under the GATS. The services sector that was offered for liberalization comprises business services, professional services, telecommunication services, sea transport, audiovisual and broadcasting services, construction services, financial services, health services, tourism services, computer, travel services, rental and leasing services and entertainment services.

Malaysia also imposes several restrictions on market access and national treatment in the horizontal and sectoral schedules of commitments (refer Table 2 and Table 3). Generally, Malaysia's limitations on market access and national treatment on horizontal commitments are placed for Mode 3 (commercial presence) and Mode 4 (movement of natural persons). However, there is no limitation imposed on the horizontal commitment for mode 1 (cross-border supply) and Mode 2 (consumption abroad). As for specific sectors commitment, there is no limitation imposed on market access for Mode 1 and Mode 2. However, in Mode 3 some limitations are imposed because it deals with the establishment of foreign service providers in the domestic market. Malaysia has also been quite restrictive in terms of Mode 4 whereby most of the specific commitments are 'unbound' or there are no commitments.

Table 2: Example of Malaysia's horizontal commitments for services sector: Limitations on markets access and national treatment

Limitations on Market Access	Limitations on National Treatment
<p>Mode 3: In acquisition of assets or interest of Malaysian companies and businesses, mergers or take-overs, approval is required when;</p> <p>the acquisition of the voting rights of a Malaysian corporation by any single foreign interest or associated group of 15 percent or more, or an aggregate foreign interest of 30 percent more or exceeding RM 5million</p> <p>the acquisition results in passing of ownership or control to foreign interest</p> <p>foreign control of Malaysian corporations through managements arrangements.</p>	<p>Mode 3: a) Approval may be denied if dealings on land, property and real estate are for speculative purposes</p> <p>b) Incentives are limited to Malaysian-owned corporations</p> <p>c) NEP and NDP measures for Bumiputras are unbound</p> <p>d) Corporations in which the Government has an interest shall, in acquiring services, give first consideration to service suppliers in which the Government has an interest.</p>
<p>Mode 4: Unbound¹ except for measures affecting the entry and temporary stay of natural persons defined as follows:</p> <p>a) Intra-corporate transfer:</p> <p>i) senior managers</p> <p>ii) two specialists or experts per organisation</p> <p>These persons must be employees of the foreign service supplier for not less than one year.</p> <p>b) (i) specialists, provided that Malaysian counterparts are employed and/or Malaysians are trained by the specialists</p> <p>(ii) professionals who are recognised and registered with Malaysian professional bodies</p> <p>(iii) business visitors who received no remuneration from within Malaysia and are not engaged in direct sales activities</p> <p>The entry and stay of these persons shall not exceed a total of five years. For business visitors, the total stay shall not exceed 90 days</p>	<p>Mode 4: Unbound except for categories of natural persons specified under market access</p>

Source: WTO (2005) and MITI (2005), "Malaysia Schedule of Specific and Horizontal Commitments":
 < http://www.wto.org/english/tratop_e/serv_e/serv_commitments_e.htm > (accessed 30 August 2005).

¹ An entry of "none" in the above schedule means that a member binds himself to not having any measures which violate markets access and national treatment for a specific sector and mode of supply. This is also termed as "full commitment" or full liberalization. Unbound implies that no commitment is made for a particular mode of supply. This is also termed as "no commitment". This characterization of commitments as full, partial and none is important for assessing the nature and extent of liberalization in various services.

**Table 3: Example of Malaysia's Sector Specific Commitments for
Business Services (Professional Services) : Limitations on Markets access and National Treatment**

Business Services	Limitations on Market Access	Limitations on National Treatment
Professional Services Legal services	Mode 1 and 2: 'None' Mode 3: Only through a corporation incorporated in the Federal Territory of Labuan. Mode 4: 'Unbound'	Mode 1 and 2: 'None' Mode 3: 'None' Mode 4: 'Unbound' with exceptions
Accounting, auditing and bookkeeping services	Mode 1 and 2: 'None' Mode 3: Only through a locally registered partnership with Malaysian accountants or Malaysian accounting firms and aggregate foreign interests shall not exceed 30 percent Mode 4: 'Unbound' except as indicated in the horizontal section	Mode 1 and 2: Auditing services must be authenticated by a licensed auditor in Malaysia. Mode 3: 'None' Mode 4: 'Unbound' with exceptions The qualifying examination to determine the competence and ability to supply the service for the purposes of registration with the professional bodies will be conducted in the English language.
Taxation services	Mode 1 and 2: 'None' Mode 3: Same as above Mode 4: 'Unbound' with exceptions	Mode 1 and 2: Taxation services must be authenticated by a licensed auditor in Malaysia. Mode 3: 'None'. Mode 4: 'Unbound' with exceptions. Same as above
Architectural services	Mode 1 and 2: 'None' Mode 3: Architectural services may be supplied only by a natural person Mode 4: 'Unbound' with exceptions	Mode 1 and 2: Architectural services must be authenticated by a licensed professional architect in Malaysia. Mode 3: 'None' Mode 4: 'Unbound' with exceptions. Same as above
Engineering services	Mode 1 and 2: 'None' Mode 3: Engineering services may be supplied only by a natural person Mode 4: 'Unbound' with exceptions	Mode 1 and 2: Architectural services must be authenticated by a licensed professional engineer in Malaysia. Mode 3: 'None' Mode 4: 'Unbound' with exceptions. Same as above
Integrated engineering services	Mode 1 and 2: 'None' Mode 3: Only through representative office, regional office or locally incorporated joint-venture corporation with Malaysian individuals or Malaysian-controlled corporations. Mode 4: 'Unbound' with exceptions	Mode 1 and 2: Integrated engineering services must be authenticated by the relevant registered professionals in Malaysia. Mode 3: 'None'. Mode 4: 'Unbound' with exceptions. Same as above
Medical speciality services	Mode 1 and 2: 'None' Mode 3: Medical speciality services may be supplied only by a natural person Mode 4: 'Unbound' with exceptions	Mode 1, 2 and 3: 'None'. Mode 4: 'None' other than: practice only in private hospitals of at least 70 beds; practice to be only at a specified location and a change of location requires approval; and setting up of individual or joint group practices is not permitted. The qualifying examination to determine the competence and ability to supply the service for the purposes of registration with the professional bodies will be conducted in the English language.

Source: WTO (2005) and MITI (2005), "Malaysia Schedule of Specific and Horizontal Commitments".

< http://www.wto.org/english/tratop_e/serv_e/serv_commitments_e.htm > (accessed 30 August 2005).

Malaysia's services sector is highly protected compared to other sectors in the economy because it is far less developed and competitive than other sectors. Malaysia's commitments to services liberalization have been progressive in nature whereby foreign services providers are only allowed in sectors where domestic suppliers are ready to compete. At the moment, Malaysia offers ten out of twelve services sectors for liberalization under GATS. The largest number of services sub-sectors that was offered for liberalization is business services followed by construction services and financial services. Distribution services and environment services are the only services sectors which are not offered for liberalization at the moment.

Malaysia's Commitments under AFAS

The ASEAN Framework Agreement on Services (AFAS) was signed during the Fifth ASEAN Summit on December 15, 1995. The AFAS was aimed at enhancing cooperation in the service sector among ASEAN members by eliminating intraregional trade restrictions and expanding the scope of liberalization in services beyond those already undertaken under the GATS. In other words, the AFAS is meant to be GATSplus. This is because, there is no specific provision exists in ASEAN concerning particular issues related to services. ASEAN members countries have chosen to follow the liberalizing modality of the WTO's GATS and open their services market on gradual basis (Stephenson, 1999).

To date ASEAN has concluded five packages of commitments through successive rounds of negotiations since 1 January 1996 (Round 1, 1996-1998; Round 2, 1999-2001; Round 3, 2002-2004; Round 4, 2005-2006; Round 5, 2007-2009). The final destination of ASEAN liberalization is the removal of all trade barriers by 2020, however the problem lies in choosing the most appropriate approach to achieve the stated objective remained a major hurdle for member states. AFAS is aimed at substantially eliminating restrictions to trade in services among ASEAN countries in order to improve the efficiency and competitiveness of ASEAN services suppliers. AFAS provides the broad guidelines for ASEAN member countries to progressively improve market access and ensure equal national treatment for services suppliers among ASEAN countries in all four modes of services supply. In addition, AFAS also provides rules for related aspects such as mutual recognition, dispute settlements, institutional mechanism, as well as other areas of cooperation in services.

Malaysia had made commitments to liberalise 40 services activities covering all modes of supply for common sectors and sub sectors (which includes tourism and travel related services, e-commerce, other services sectors, construction services, maritime transport services and distribution services) under AFAS. These commitments reveal that the country has substantially allowed the access of foreigners in services sector.

Concluding remarks

In light of these developments, the services sector is increasingly promoted as the most promising sector to enhance and expand economic development in most countries, including Malaysia. This is further supported by the liberalization of the services sector that is being promoted in various bilateral, regional as well as multilateral trade arrangements. Even though Malaysia has made substantial commitments under GATS and AFAS, there is still a great potential to further liberalize the services sector. However, at the moment, Malaysia has adopted progressive liberalization as domestic service providers are less competitive and require more time to build their capacity. Thus future negotiations on services liberalization will be conducted on a gradual basis according to the capability of domestic service providers to compete with foreign service providers. In this context, it is important that Malaysia develops the quality and capability of its domestic services sector in line with the global market requirements. Even though the liberalization of services may exert serious structural adjustment for sensitive industries (such as unemployment, loss of productive capacity and marginalization of domestic firms), the process of liberalization is an opportunity to export services in which Malaysia has a competitive edge. However, the success of the Malaysian services providers would depend on their ability to undertake the necessary investment in capital and human resources and adopt new forms of organizational and management techniques to improve their competitiveness.

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