

Services Trade Restrictiveness Indices for the Malaysia Model

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Our Malaysia Model uses a Two Step Approach for its inputs of Services Restrictiveness

- First: develop indices of restrictiveness of the regulatory barriers in services: both discriminatory against foreigners and non-discriminatory that affect Malaysian nationals
- Second: convert the Services Trade Restrictiveness Indices (STRIs) into ad valorem equivalents (AVEs).

STRIs: Acquire information on the regulatory regimes in selected Malaysian services sectors

- First conduct a survey of the regulatory regime in the key business services sectors—
- We used the World Bank questionnaire which has been applied to more than 100 countries.
- Completed by a law firm in Kuala Lumpur.

Need to supplement this information for updating and nuances between the law and practice

Supplemented with expert interviews

- Expert interviews included (but not limited to):
- Ministry of Transport, Department of Civil Aviation Malaysia, Malaysia Shipowners Association, National Bank of Malaysia, Association of Banks in Malaysia, General Insurance Association of Malaysia, Life Insurance Association of Malaysia, Malaysian Institute of Accountants, Attorney General's Chambers of Malaysia, Bar Council Malaysia, Malaysia Securities Commission, Malaysian Communications and Multimedia Commission, National ICT Association of Malaysia, multiple specialist professors at the University Kebangsaan Malaysia, European Union delegation in Kuala Lumpur, Malaysian freight forwarders association, MITI, PEMANDU.

Supplemented with Written Materials

- Including
- World Trade Organization (2010), Trade Policy Review of Malaysia
- Several legal acts and reports of the Government of Malaysia.

Trade Restrictiveness Indices of the barriers

- Trade Restrictiveness Indices (TRIs) are developed from this information (both discriminatory and non-discriminatory) based on matrices for each sector developed by several Australian economists including -- Warren (2000), McGuire and Schulele (2000), Kalirajan et al. (2000) and Kang (2000), also by Kimura et al.
- We will go through three examples in detail.
- This will show how the questions differ across sectors, but also what are common questions.

First Example: Banking Services in Malaysia

- First a detailed written survey was completed by a law firm in Malaysia
- Then experts were interviewed: main experts were National Bank of Malaysia and the Association of Banks in Malaysia
- What did we learn are the main regulatory barriers in banking services in Malaysia?

Summary of Principle

Malaysian Barriers in Banking

- Licensing of banks. Issuance of new licenses is subject to: i) prudential criteria, and ii) best interest of Malaysia criteria. This implies that issuance of the license comes with several requirements. The requirements are generally the same for domestic and foreign-owned banks (a “non-discriminatory” barrier), but lack full transparency.
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- Form of commercial presence. Foreign companies are permitted to enter as a locally incorporated subsidiary or by acquiring all or part of a local bank or through a joint venture. But “branch banking” is prohibited. That is, foreign banks must register as a Malaysian bank before they start operating.
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Summary of Principle

Malaysian Barriers in Banking (cont.)

- Expansion of the number of bank outlets. According to the experts view, even though Malaysia has progressively liberalized the restrictions for locally incorporated foreign banks to establish physical branches, there are still some restrictions on the number and location of additional outlets including Automated Teller Machines (ATMs).
- Raising funds by foreign banks and lending funds by foreign banks. Malaysia does not allow foreign banks to take deposits of Malaysians on a cross-border basis, i.e., under The Banking and Financial Institutions Act 1989, foreign financial institutions are not licensed to take deposits in Malaysia. Additionally, the exchange control requirement applies for lending by banks which restricts lending to foreigners.

Scoring the STRI

- This information is scored and transformed into a “Services Trade Restrictiveness index” (STRI) based on McGuire and Schuele categories.
- The STRI has been calculated for many countries by McGuire and Schuele.

McGuire and Schuele banking restrictions categories and their weights

- **Commercial Presence Restrictions**
- 0.1 Licensing regime for banks
- 0.2 Equity restriction on banks
- 0.1 Required form of commercial presence
- 0.1 Restrictions on providing some types of services
- 0.1 Joint venture restrictions
- 0.02 Movement of people to work in banks
- **Cross-border restrictions**
- 0.1 Raising funds by foreign banks
- 0.1 lending funds by foreign banks
- 0.1 restrictions on types of cross border business
- 0.05 restrictions on opening branch outlets
- 0.02 composition of the Board of Directors
- 0.01 temporary movement of people

Scoring the Regulatory Regime of Malaysian Banking and Conversion into Trade Restrictiveness Indices

- Yaghoob Jafari, “Ad Valorem Equivalent to Barriers to Services Providers in Malaysia,” August 9, 2012.
- Matrix is scored on pages 76-77.
- Detailed documentation and explanation of scoring is provided on pages 26-30.
- Documentation is crucial for transparency and critical review.

Comparison with other countries

- Table 3 from Kimura et al for comparison with other countries

Converting the Banking STRI into Ad Valorem Equivalents

- Kalirajan et al (2000) estimated the impact of a higher STRI on the net interest margins of banks across many countries. This allows calculation of the ad valorem equivalents of the restrictiveness of the barriers.
- We apply the Kalirajan estimated relationship between the STRI and the ad valorem equivalents to Malaysia—allowing an estimate for Malaysia.

Second Example: Air Transportation Services in Malaysia

- First a detailed written survey was completed by a law firm in Malaysia
- Then we supplemented this information by interviewing the following experts:
- Multiple experts in the Department of Civil Aviation under the Ministry of Transport of Malaysia; and a Professor of Transportation Economics in Malaysia.
- Written reports were also consulted, including the WTO Trade Policy Review of Malaysia.
- What did we learn are the main regulatory barriers in air transportation services in Malaysia?

Summary of Principle

Malaysian Barriers in Air Transportation

- **Domestic air transport and domestic charter flight.** Foreign airlines are prohibited from operating domestic air transport services or domestic charter flight services.
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- **Airport services.** Foreign airlines are prohibited from providing ground handling services such as fuel supply services.
- **Direct investment.** For a foreign company to be considered Malaysian, the maximum foreign equity participation permitted in an existing international or domestic air transport service supplier is limited to 70%.
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Summary of Principle Malaysian Barriers in Air Transportation (continued)

- Bilateral Air Service Arrangement (ASA).
International air transport services and international charter flight services can be supplied by foreign companies only if an intergovernmental agreement (ASA) or specific agreements exist between Malaysia and the country of the foreign supplier
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Summary of Principle Malaysian Barriers in Air Transportation (continued)

- **Discretionary imposition of restriction/subsidy.** Although by law the government is not allowed to impose selective restrictions, in practice the government has provided privileges to Malaysia Airlines (MAS), a government-linked company.
- For example, the application of the low cost airline Air Asia to use Subang airport as its hub was refused, but the government allowed Fire Fly (a subsidiary of MAS) to operate from Subang airport.
- Also, while AirAsia X preferred to use the main airports, the carrier initially had to serve alternative airports until June 2011, two months before the August 2011 share swap agreement between Air Asia and MAS which effectively meant the two were no longer competitors.
- Finally, it is not clear whether civil servants travelling by air must use MAS

Summary of Principle Malaysian Barriers in Air Transportation (continued)

- Discretionary imposition of subsidy to protect domestic air companies. Malaysian Airlines is a government-linked company and receives indirect subsidies (such as the recent airplane financing facility supported by the Ministry of Finance).

Air transportation restrictions categories and their weights

- 0.1 Required form of commercial presence
- 0.1 Equity restriction on international air transport service supplier
- 0.1 Equity restriction on domestic air transport service supplier
- Licensing regime for banks
- 0.1 Licensing or right to provide scheduled international air transportation services
- 0.1 Licensing or right to provide scheduled domestic air transportation services
- 0.1 Licensing or right to provide international chartered flights
- 0.1 Licensing or right to provide domestic chartered flights
- 0.1 License or right to provide airport services
- 0.05 Discretionary imposition of restrictions is possible
- 0.05 Discretionary imposition of subsidies to protect domestic companies is possible
- 0.05 Intergovernmental ASA agreement
- 0.02 composition of the Board of Directors
- 0.02 Permanent movement of people
- 0.01 temporary movement of people

Scoring the Regulatory Regime of Air Transportation Services and Conversion into Trade Restrictiveness Indices

- Yaghoob Jafari, “Ad Valorem Equivalent to Barriers to Services Providers in Malaysia,” August 9, 2012.
- Matrix is scored on pages 73-74.
- Detailed documentation and explanation of scoring is provided on pages 12-16.
- Documentation is crucial for transparency and critical review.

Third Example: Accounting Services in Malaysia

- First a detailed written survey was completed by a law firm in Malaysia
- Then we supplemented this information by interviewing the following experts:
- Corporate & International Affairs Department, Malaysian Institute of Accountants; Legal & Enforcement Department, Malaysian Institute of Accountants; Membership Services Department, Malaysian Institute of Accountants
- What did we learn are the main regulatory barriers in air transportation services in Malaysia?

Summary of Principle Malaysian Barriers in Accounting and Auditing Services

- Residency and local presence. Foreign accountants, wishing to provide auditing and taxation services in Malaysia must have six months prior residency.
- Licensing and accreditation of foreign professionals. Foreign accountants need to register and apply for a Practicing Certificate from the Malaysian Institute of Accountants (MIA) to set up a public practice, for certain types of services such as audit, liquidation, and tax. The Malaysian Institute of Accountants issues the license on a case by case basis.

Summary of Principle Malaysian Barriers in Accounting and Auditing Services (continued)

- Licensing and accreditation of local professionals. Local accountants wishing to provide auditing and taxation services in Malaysia must first register and become members of the Malaysian Institute of Accountants (MIA), the professional body of accountants of Malaysia. To be a member of MIA, three years of experience and an accounting or auditing degree is required.
- The ownership by non-professional investors of a part or entire accounting company is not permitted. All partners of a Malaysian accounting company must be members of the Malaysian Institute of Accountants.

Summary of Principle Malaysian Barriers in Accounting and Auditing Services (continued)

- Activities reserved by law to the profession. All core activities are reserved by law to professional accountants. (non-discriminatory)
- Multi-disciplinary practices: All owners of an accounting or auditing firm must be licensed under the Accountants Act of 1967.

Accounting sector restrictions categories and their weights

- 0.08 Are accounting or auditing corporations allowed?
- 0.08 Foreign partnership or joint venture restraints
- 0.05 Ownership restrictions for foreigners
- 0.05 Ownership restrictions for non-professionals
- 0.135 Nationality or citizenship requirement to practice
- 0.135 Residency and local presence requirements
- 0.1 Quotas or economic needs tests for foreigners to practice
- 0.1 Licensing regime for foreign professionals
- 0.05 Licensing regime for local professionals
- 0.02 Permanent movement of people
- 0.05 Core activities reserved by law to the profession
- 0.05 Limitations on Multi-disciplinary practices
- 0.05 Limitations on fee setting, advertising and marketing
- 0.02 Licensing requirements on management
- 0.02 Other restrictions
- 0.01 temporary movement of people

Scoring the Regulatory Regime of Accounting and Auditing Services and Conversion into Trade Restrictiveness Indices

- Yaghoob Jafari, “Ad Valorem Equivalent to Barriers to Services Providers in Malaysia,” August 9, 2012.
- Matrix is scored on pages 81-82.
- Detailed documentation and explanation of scoring is provided on pages 49-53.
- Documentation is crucial for transparency and critical review.

Converting the STRIs into AVEs

- For each sector, the Australian authors regressed a measure of the price of the service on the STRI and other variables that might influence the price
- The regression provides an estimate of the impact of an increase in the STRI on the price, based on international cross country data, i.e., the AVE of the STRI.
- We assume that regression applies to Malaysia.
- Then based on the coefficient from the international regression, we estimate the amount by which the price can be reduced from lowering the STRI, i.e., we have the AVE of the STRI.

What is the ad valorem equivalent of a barrier against foreign service providers?

- Example—Suppose that without any **discriminatory** barriers, the price of accounting services would be \$40 per hour.
- But the actual price is \$50 per hour.
- The ad valorem equivalent is 25%, calculated as:
- $[\$50 - \$40] / \$40 = \$10/\$40 = 0.25$
- The challenge is to obtain the data and a reliable methodology to estimate the components of this formula.