MALAYSIA

TRADE SUMMARY

The U.S. goods trade deficit with Malaysia was $11.9 billion in 2010, down $957 million from 2009. U.S. goods exports in 2010 were $14.0 billion, up 34.4 percent from the previous year. Corresponding U.S. imports from Malaysia were $25.9 billion, up 11.3 percent. Malaysia is currently the 19th largest export market for U.S. goods.

U.S. exports of private commercial services (i.e., excluding military and government) to Malaysia were $1.7 billion in 2009 (latest data available), and U.S. imports were $1.1 billion. Sales of services in Malaysia by majority U.S.-owned affiliates were $4.1 billion in 2008 (latest data available), while sales of services in the United States by majority Malaysia-owned firms were $331 million.

The stock of U.S. foreign direct investment (FDI) in Malaysia was $13.5 billion in 2009 (latest data available), up from $12.3 billion in 2008. U.S. FDI in Malaysia is led by the manufacturing, mining, and banking sectors.

In 2010, the United States entered into negotiations on a regional Asia-Pacific trade agreement called the Trans-Pacific Partnership (TPP), with the objective of shaping a high-standard, broad-based regional agreement. This agreement will create a potential platform for economic integration across the Asia-Pacific region, a means to advance U.S. economic interests with the fastest-growing economies in the world, and a tool to expand U.S. exports, which are critical to the creation and retention of high-paying, high-quality jobs in the United States. In October 2010 Malaysia joined the United States, Australia, Chile, New Zealand, Peru, Singapore, Brunei and Vietnam as the ninth participant in the TPP negotiations.

IMPORT POLICIES

Tariffs and Import Licensing Requirements

Almost all of Malaysia's tariffs are imposed on an *ad valorem* basis, with a simple average applied tariff rate of 8.4 percent in 2010 (up from 7.4 percent in 2009). Duties for tariff lines where there is significant local production are often higher. In general, the level of tariffs is lower on raw materials than for value-added goods. U.S. companies have indicated that tariff reductions on many products would allow them to increase their exports significantly, including on such products as frozen french fried potatoes, other food and confectionary products, and restaurant equipment.

On roughly 80 products – most of which are agricultural goods – Malaysia charges specific duties that represent extremely high effective tariff rates. These tariffs appear to be aimed at protecting small and rural farmers from foreign competition. The simple average *ad valorem* equivalent across all products with a specific tariff is 392 percent. Beverages, alcohol, and wine are subject to an effective tariff of up to 500 percent when import duties and excise taxes are combined.

A large number of Malaysian tariff lines related to import-sensitive or strategic industries (principally in the construction equipment, agricultural, mineral, and motor vehicle sectors) are subject to non-automatic import licensing. Malaysia also maintains performance requirements that must be met to receive a customs waiver for operations in Foreign Trade Zones.

Malaysia has an extensive network of preferential trade relationships. Malaysia has bilateral trade

agreements with Chile, India, Japan, Pakistan, and New Zealand as well as regional agreements, as part of ASEAN, with China, Korea, Japan, India, Australia, and New Zealand. Malaysia is currently negotiating additional preferential trade agreements with Australia and members of the Organization of the Islamic Conference.

Tariff-Rate Quotas on Selected Agricultural Products

Since April 2008, the Malaysian government has maintained tariff-rate quota (TRQ) systems for 17 tariff lines, including live poultry, poultry meat, milk and cream, pork, and round cabbage. These products incur in-quota duties between 10 percent and 25 percent and out-of-quota duties between 40 percent and 168 percent. Before TRQ implementation, the applied tariff rate was zero for these products.

Import Restrictions on Motor Vehicles

Malaysia has maintained tariffs and non-tariff barriers in the automobile sector for more than 25 years. In addition, Malaysian government policies distinguish between "national" cars, (*e.g.,* cars made by domestic producers Proton and Perodua) and "non-national" cars, which include most vehicles assembled in Malaysia by non-Malaysian owned firms. Malaysia also has traffic restrictions and noise standards that affect the usage of large motorcycles.

The Malaysian government has started slowly to dismantle some of its trade restrictive measures in order to implement its commitments under the WTO and the ASEAN Free Trade Agreement (AFTA). Malaysia cut its automobile import duty from 40 percent to 5 percent by 2006 in order to meet its AFTA commitments but then imposed steep excise taxes to compensate for the lost revenue. In January 2007, the ceiling on excise taxes for most vehicle categories was reduced from 125 percent to 105 percent and on motorcycles from 50 percent to 30 percent. In November 2008, the Malaysian government indicated that Malaysia would review the National Auto Policy (NAP) and in January 2010 began implementing certain liberalizing measures. The new policy reduced the intra-ASEAN duty rate from 5 percent to zero percent in January 2010. It lifted the freeze on manufacturing licenses for luxury vehicles, pick-up trucks, commercial vehicles, and hybrid electric vehicles, and promoted green technology by providing a duty exemption and a 50-percent excise tax reduction for the manufacture of hybrid electric vehicles.

Malaysia maintains a system of approved permits (APs) that provides holders with the right to import cars and motorcycles and distribute them locally. The revised NAP extended the phase-out dates for APs to December 31, 2020 from the previous 2010 date. The AP system was designed to provide *bumiputera* (ethnic Malay) companies with easy entry into the automobile and motorcycle distribution and service sector. The AP system acts as a quota by restricting the total number of vehicles that can be imported in a given year, which is currently capped at 10 percent of the market. Moreover, many AP holders sell their permits, with the associated costs passed on to consumers, increasing the price of imported vehicles.

Malaysia continues to use an industrial adjustment fund to provide financial support for the local assembly of vehicles. Automobile companies using components sourced from locally registered manufacturing companies are eligible for tax reductions, raising concerns that this fund revives the local content program that was abolished in 2004. Many foreign carmakers in Malaysia require highly specialized components that cannot be sourced economically from within Malaysia, and are therefore unable to benefit from this fund.

Meat Import Licenses

Malaysia requires licensing for all meat imports and restricts the types of pork and poultry cuts that may be imported. These import permits reportedly are often used to restrict imports of chicken meat and pork

cuts when domestic prices are low. The Department of Veterinary Services often provides import licenses for less than the quantity requested. Malaysia also requires import licenses for wheat flour, wine, eggs, seafood, rice, liquid milk, and other dairy products such as cheese, yogurt, milk powder, ice cream and butter.

EXPORT TAXES

Malaysia taxes exports of palm oil, rubber, and timber products in order to protect domestic processing production. Malaysia is the second largest producer and largest exporter of palm oil and products made from palm oil, and accounted for approximately 15 percent of world production and 30 percent of world trade in vegetable oils in 2010. Malaysia uses export taxes of 10 percent to 30 percent *ad valorem* to discourage the export of crude palm oil and to encourage development of the local refinery sector. Refined palm oil and products are not subject to export taxes. The Malaysian government waives export taxes on exports of crude palm oil to Malaysia-invested foreign vegetable oil refineries, giving Malaysia-invested plants an advantage in foreign markets, including the United States.

GOVERNMENT PROCUREMENT

Malaysia's official policy is to use government procurement to support national public policy objectives, and the government generally favors domestic over foreign companies. These policy objectives include encouraging greater participation of *bumiputera* in the economy, transfer of technology from foreign to domestic industries, reducing the outflow of foreign exchange, providing advantages to local companies in the services sector, and enhancing Malaysia's export capabilities. International tenders generally are invited only when domestic goods and services are not available. The federal government makes extensive use of non-competitive procurement and direct negotiated awards. In domestic procurement, preferences are provided for *bumiputera* suppliers and other domestic suppliers, and foreign companies are generally required to take on a local partner before their tenders will be considered. The U.S. Government continues to raise concerns about the nontransparent nature of the Malaysia's procurement process. Malaysia is not a signatory to the WTO Agreement on Government Procurement.

EXPORT SUBSIDIES

Malaysia maintains several programs that appear to provide export subsidies. Under the Central Bank's export credit refinancing scheme, commercial banks and other lenders provide financing to all exporters at a preferential, below-market rate for both pre-shipment and post-shipment. Malaysia also provides a series of tax and investment incentives to exporters, including those through the Pioneer Status and Investment Tax Allowance programs.

The revised NAP increases the income tax exemption for high value-added exports of motor vehicles and parts. The income tax exemption is based on the percentage increase in the domestic value added of exports. If the domestic value added is at least 30 percent, then 30 percent of the export value is exempt from income tax; if the domestic value added is at least 50 percent, then 50 percent is exempt.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Malaysia was placed on the Watch List in the 2010 Special 301 report. Malaysia continues to express a commitment to protecting and enforcing IPR and to pursuing needed legislative and regulatory improvements. Some areas of IPR enforcement, especially in the business software area, improved last year, and industry reports increased responsiveness from the Ministry of Domestic Trade, Cooperatives, and Consumerism to its requests for enforcement actions. However, other areas of IPR protection and enforcement continue to represent barriers to U.S. exports and investment. Key issues cited in the report

include continued widespread piracy and counterfeiting, declining IPR enforcement efforts, and lack of *ex officio* initiated IPR investigations by customs officials, as authorized under Malaysian law. Industry reports that book piracy remains problematic, and copyright piracy over the Internet is rising. The United States continues to encourage Malaysia to accede to the WIPO Internet Treaties and the Budapest Treaty. In addition, the United States continues to urge Malaysia to provide effective protection against unfair commercial use, as well as unauthorized disclosure, of undisclosed test or other data generated to obtain marketing approval for pharmaceutical products, and to provide an effective system to address patent issues expeditiously in connection with applications to market pharmaceutical products.

SERVICES BARRIERS

Malaysia's services sector constitutes 45 percent of the national economy and has been a key driver of economic and job growth in Malaysia for several years. In an effort to establish a knowledge-based economy less reliant on manufactured exports, the government aims to increase the services sector share of GDP to around 60 percent by 2020. In support of this objective, in May 2009, the Najib Administration announced initial liberalization measures covering some 27 service subsectors. Further reforms reportedly are being considered.

Telecommunications

Malaysia made limited GATS commitments on most basic telecommunications services and only partially adopted the WTO Reference Paper on regulatory commitments. Based on Malaysia's GATS commitments, foreign companies are entitled to acquire only up to a 30 percent equity stake in existing licensed public telecommunications operators, and foreign participation is limited to facilities-based suppliers. These limitations are not reflected in Malaysian law, however, but only in ministerial policy. In certain instances, Malaysia has allowed greater than 30-percent equity participation in the telecommunications market, but the manner in which such exceptions are administered is nontransparent and is perceived by foreign suppliers as arbitrary. In some cases, the ministry permits firms to invest up to a certain equity limit, then subsequently asks them to divest to lower levels. The United States will continue to urge Malaysia to bind foreign equity limits to the full extent permissible under Malaysian law, *i.e.*, to 100 percent, to foster a more predictable and hospitable investment climate.

Malaysia has an unwritten prohibition against an Application Service Provider (ASP) selling service to another ASP license holder who would then provide service to its own retail customers. This issue is primarily limited to multi-national corporations that may seek to purchase services which combine value-added services, such as unregulated information technology (*e.g.*, back office point of sale and inventory), with regulated application services (*e.g.*, virtual private network). Given the lack of any clear policy rationale for such a limitation, and its negative impact on suppliers, the United States will continue to press for its elimination.

Distribution Services, including Direct Selling

Guidelines governing distribution services were reviewed and revised in March 2010. These guidelines include requirements for the use of locally produced products. The revised provisions require that at least 30 percent of total products (Stock Keeping Units) displayed on shelf space in department stores, supermarkets, and hypermarkets are to be products manufactured by *bumiputera*-owned small- and medium-sized enterprises. Among other provisions, the number of hypermarkets and superstores is limited based on the number of residents in the "area served" or community.

Locally incorporated direct-selling companies must allow for 30 percent *bumiputera* equity. The Malaysian government also "recommends" local content targets, which effectively translates into a

requirement. Local companies that seek direct selling licenses require paid-in capital of RM1.5 million (approximately $397,000), while companies with foreign shareholders must have paid-in capital of RM5 million (approximately $1.3 million).

Legal Services

Foreign lawyers may not practice Malaysian law, nor may they affiliate with local firms or use the name of an international firm. Foreign law firms may not operate in Malaysia except as minority partners with local law firms, and their stake in any partnership is limited to 30 percent. The Attorney General has authority to grant limited exceptions on a case by case basis under the law restricting the practice of Malaysian law to Malaysian citizens or permanent residents who have apprenticed with a Malaysian lawyer; are competent in *Bahasa* Malaysia (the official language); and have a local law degree or are accredited British Barristers at Law, provided the applicant has seven years of legal experience. Malaysian law does not allow for foreign legal consultancy except on a limited basis in the Labuan International Offshore Financial Center (see section on "Financial Services" below).

Architectural Services

A foreign architectural firm may operate in Malaysia only as a joint venture participant in a specific project with the approval of the Board of Architects. Malaysian architectural firms may not have foreign architectural firms as registered partners. Foreign architects may not be licensed in Malaysia but are allowed to be managers, shareholders, or employees of Malaysian firms.

Engineering Services

Foreign engineers may be licensed by the Board of Engineers only for specific projects and must be sponsored by the Malaysian company carrying out the project. In general, a foreign engineer must be registered as a professional engineer in his or her home country, have a minimum of 10 years experience, and have a physical presence in Malaysia for at least 180 days in one calendar year. To obtain temporary licensing for a foreign engineer, a Malaysian company often must demonstrate to the Board that they cannot find a Malaysian engineer for the job. Foreign engineers are not allowed to operate independently of Malaysian partners or serve as directors or shareholders of an engineering consulting company. A foreign engineering firm may establish a non-temporary commercial presence only if all directors and shareholders are Malaysian. Foreign engineering companies may collaborate with a Malaysian firm, but only the Malaysian company may submit the plans for domestic approval.

Accounting and Taxation Services

All accountants seeking to provide auditing and taxation services in Malaysia must register with the Malaysian Institute of Accountants (MIA) before they may apply for a license from the Ministry of Finance. Citizenship or permanent residency is required for registration with the MIA. Foreign accountants and auditors are only allowed to practice with registered Malaysian accountants, with foreigners permitted to hold no more than 40 percent of shares.

Financial Services

While Malaysia relaxed a few barriers in the financial services sector, significant barriers remain to investment in this sector. The foreign equity limitation is 70 percent for domestic Islamic banks, investment banks, insurance companies, and Islamic insurance operators. In principle, foreign equity above 70 percent is considered on a case by case basis for insurance companies if the investment is determined to facilitate the consolidation and rationalization of the insurance industry, although currently

no new licenses are being granted. Foreign equity is limited to 30 percent for domestic conventional banks. The foreign equity limitation is 70 percent for unit trust management companies providing retail services and for stock broking companies.

Advertising

Foreign content in commercials in Malaysia is limited to 20 percent. The Malaysian government in 2007 relaxed enforcement of regulations governing the appearance of foreign actors in commercials shown in Malaysia.

Audio-Visual and Broadcasting

The Malaysian government maintains broadcast content quotas on both radio and television programming. Eighty percent of television programming is required to originate from local production companies owned by ethnic Malays and 60 percent of radio programming must be of local origin. Foreign investment in terrestrial broadcast networks is prohibited and is limited to a 20 percent equity share in cable and satellite operations. As a condition for obtaining a license to operate, video rental establishments are required to have 30 percent local content in their inventories.

INVESTMENT BARRIERS

The Malaysian government retains considerable discretionary authority over individual investments in all sectors and heavily restricts foreign investment in sectors controlled by government-linked companies or in sectors the government deems strategically important. These include financial services, professional services, the oil and gas sector, telecommunications, automotive industries, plantations, and mining. Among the restrictions imposed by the Malaysian government are limitations on foreign equity (generally capped at 30 percent) and requirements that foreign firms enter into joint ventures with local partners.

The Ministerial Functions Act grants relevant ministries broad discretionary powers over the approval of specific investment projects, with each ministry often administering a complex web of regulations and policies. While investors in industries targeted by the government for increased investment can receive assistance obtaining necessary approvals from various regulatory bodies (including, in some cases, a waiver of regulatory requirements), investors in non-priority sectors face significant bureaucratic obstacles.

OTHER BARRIERS

Transparency

The lack of transparency in government decision making and procedures in Malaysia has impeded U.S. firms' access to the Malaysian market. The Malaysian government has taken steps to fight corruption, including through the Anti-Corruption Agency (ACA), which is part of the Office of the Prime Minister. The ACA is authorized to conduct investigations and prosecute cases with the approval of the Attorney General. Few senior officials or politicians have been prosecuted for corruption, however. Malaysia has slipped in its ranking on Transparency International's Corruption Perceptions Index from 26th in 2004 to 56th in 2010. Malaysia has signed, but not yet ratified, the UN Convention Against Corruption.