

Client Alert

May 2016

For further information, please contact:

Adeline Wong
+603 2298 7880
adeline.wong@wongpartners.com

Meng Yew Wong
+603 2298 7902
mengyew.wong@wongpartners.com

Elizabeth Nightingale
+603 2299 6442
elizabeth.nightingale@bakermckenzie.com

Trans-Pacific Partnership Agreement - Introduction to the “21st Century Trade Agreement”

The Trans Pacific Partnership Agreement (“TPPA”) is a free trade agreement (“FTA”) signed among 12 member countries on 4 February 2016, comprising Australia, Brunei, Chile, Canada, Japan, Mexico, Malaysia, New Zealand, Peru, Singapore, the United States and Vietnam, having a combined market of 793 million people and GDP of USD 27.5 trillion representing some 40% of the global economy.

Being an FTA, the terms of the TPPA must be consistent with Article XXIV of GATT 1994 and Article V of GATS (allowing WTO member countries to form ‘free trade areas’) as such agreements represent a departure from the most favoured nation (“MFN”) principle under the WTO. Under Article XXIV of GATT 1994, WTO member countries may form customs unions or free trade areas provided that the duties cannot be higher and the regulation of commerce cannot be more restrictive with respect to non-FTA countries. Where any contracting party wishes to increase duties with respect to other non-FTA countries, this will result in withdrawal of concessions and compensatory payments being made in accordance with Article XXVII of GATT 1994.

Under Article V of GATS, WTO member countries are allowed to enter into any agreement to liberalise trade in services provided such agreement has substantial sectoral coverage and provides for elimination (or substantial elimination) between parties of existing measures and/or prohibiting newer discriminatory measures at entry into force of the agreement or within a reasonable time frame.

‘High Standard’ FTA

The TPPA is a ‘high standard’ FTA as it seeks to include in its ambit various “WTO-plus” chapters which are trade issues or topics not covered today in WTO rules, or which seek to cover WTO issues or topics in a way that is superior to that under the WTO. For countries which have entered into high standard FTAs with the United States such as Singapore and Korea, it may not be uncommon to find chapters on competition policy (including with respect to state owned enterprises), government procurement, e-commerce, labour standards, and environmental standards, albeit at varying levels of commitments or subject to carve-outs.

For Malaysia however, given that we have been unable to reach a conclusion of the Malaysia-United States FTA after more than ten years since its inception (negotiations began in June 2005 and were temporarily suspended), there are various chapters within the TPPA which would be regarded by many as falling 'outside' the scope of typical FTAs that Malaysia has signed previously. To date, Malaysia has FTAs with more than 20 countries, either bilaterally¹ or as a member of ASEAN², with primary focus being given on liberalisation of trade in goods, services and investments (limited sectors).

Unlike the traditional FTAs that have been negotiated by Malaysia based on a 'positive list' approach, where market access and national treatment commitments for trade in services are based on an exhaustive list (i.e., only services sectors which are specifically committed to are opened for investment), the TPPA is negotiated on a 'negative list' approach, whereby any services sector which is not specifically excluded or carved-out is open to other member countries.

Impetus for Malaysia to join the TPPA

FTAs are commonly viewed as a key tool to achieve higher levels of trade between member countries who seek greater integration of their economies. This is generally achieved not only through liberalisation of tariff and non-tariff barriers which allow freer movement of goods, services, and investments, but also through focused efforts by each member country and governments in setting up specific working level groups to facilitate discussions around achieving the objectives of enhancing trade and investment whilst recognising that investment in capacity building through technical cooperation and collaboration is also an important part of economic integration.

Malaysia is a relatively 'trade dependent' nation, given the size of its economy and population and international trade is therefore important to sustain Malaysia's economic growth and development. Throughout the years, Malaysia has been viewed favourably as an investment destination by many foreign multinationals, including from the TPPA member countries. This was largely due to tax incentives given out by the Malaysian Government to attract companies to manufacture in Malaysia and various trade facilitation measures including the setting up by the Government of free trade zones.

These policies have helped shape Malaysia's transition from relying on the primary agriculture sector to the secondary industrial sector. As Malaysia seeks to move towards developed nation status, more efforts are being placed on developing the tertiary services sector which have seen a steady increase in terms of contribution to the GDP growth of the country.

By being an early adopter of the TPPA, Malaysia sends the signal that it would like to remain at the forefront of regional and global trade through playing a central role in being part of the 'high standards' rule-making process to ensure that Malaysia continues to remain an attractive location for foreign investment and allow its nationals to gain market access internationally. The TPPA is accordingly an important step towards cementing the country's aims of being an integral player in the global economy.

¹ (i) Malaysia-Australia; (ii) Malaysia- Chile; (iii) Malaysia-India; (iv) Malaysia-Japan; (v) Malaysia-Turkey; (vi) Malaysia Pakistan

² (i) ASEAN comprises 10 member countries: Malaysia, Singapore, Indonesia, Thailand, Vietnam, Philippines, Cambodia, Laos, Myanmar and Brunei which together form the ASEAN Free Trade Area; (ii) ASEAN-Japan; (iii) ASEAN-Korea; (iv) ASEAN-China; (v) ASEAN-India; (vi) Australia & New Zealand.

If Malaysia is not part of the TPPA, there is a likelihood that Malaysia may lose out to other economies as a preferred investment destination, such as Vietnam for manufacturing activities of textiles, electronic & electrical products, automotive parts and other products for export to key TPPA member countries, and even Singapore as a location of regional headquarters for many foreign multinational companies as a gateway into South East Asia.

Conversely, by not joining the TPPA, Malaysian companies who are looking at outward expansion would also be at a disadvantage by competing with other TPPA member countries who would be in a position to enjoy better tariffs and greater market access for goods and services such as the government procurement space in the United States which is valued at between RM 165 million to RM 655 million. There will be four new markets where Malaysia will greatly benefit from increased trade and investment - the United States, Canada, Mexico, and Peru.

TPPA Architecture

The TPPA consists of 30 Chapters, divided into several key categories. For purposes of this introduction, we will attempt to fit these chapters into seven general categories as follows:

Category 1: General Provisions	<ul style="list-style-type: none"> • Chapter 1 - Initial provisions and general definitions • Chapter 29 - Exceptions • Chapter 30 - Final provisions
Category 2: Trade in Goods	<ul style="list-style-type: none"> • Chapter 2 - National treatment and market access for goods • Chapter 3 - Rules of origin and origin procedures • Chapter 4 - Textiles and apparel chapter • Chapter 5 - Customs administration and trade facilitation • Chapter 6 - Trade remedies • Chapter 7 - Sanitary and phytosanitary measures • Chapter 8 - Technical barriers to trade
Category 3: Investment	<ul style="list-style-type: none"> • Chapter 9 - Investment
Category 4: Trade in Services	<ul style="list-style-type: none"> • Chapter 10 - Cross-border trade in services • Chapter 11 - Financial services • Chapter 12 - Temporary entry for business persons • Chapter 13 - Telecommunications • Chapter 14 - Electronic commerce
Category 5: Business Environment	<ul style="list-style-type: none"> • Chapter 15 - Government procurement • Chapter 16 - Competition policy • Chapter 17 - State-owned enterprises and designated monopolies • Chapter 18 - Intellectual property • Chapter 19 - Labour • Chapter 20 - Environment
Category 6: Member Development and Technical Cooperation	<ul style="list-style-type: none"> • Chapter 21 - Cooperation and capacity building • Chapter 22 - Competitiveness and business facilitation • Chapter 23 - Development • Chapter 24 - Small and medium-sized enterprises
Category 7: Transparency and Dispute Settlement	<ul style="list-style-type: none"> • Chapter 25 - Regulatory coherence • Chapter 26 - Transparency and anti-corruption • Chapter 27 - Administrative and institutional provisions • Chapter 28 - Dispute settlement

Given the length and breadth of each chapter under the TPPA, we will discuss the relevant commitments and implications for Malaysia in our upcoming alerts. At this stage, we will highlight key features under each category and what the chapter seeks to achieve.

Key Features

Category 2 - Trade in Goods

As with other conventional FTAs on trade in goods, the goal is to arrive at a regional agreement where countries can support each other by being more efficient in their productions and supply chains. This necessarily entails principles and obligations regarding tariff elimination among partners including significant commitments beyond partners' current WTO obligations as well as elimination of non-tariff measures.

There are comprehensive rules of origin on various products to ensure consistency in determining when a product is deemed to 'originate' from one member country to be able to benefit from preferential tariff in the importing member state. Specific rules have been included for textiles and apparel, including additional commitments and carve-outs made by individual member countries on various sectors including the automotive sector.

Within this category also lies the various customs administration and trade facilitation measures (which should be predictable, transparent and that expedite and facilitate trade), including on tackling technical barriers to trade (whilst still allowing regulators to protect health and safety and other legitimate policy objectives), and sanitary and phytosanitary measures to enhance animal and plant health and food safety.

Category 3 and 4 - Trade in Services and Investment

Within these chapters lie member countries' commitments to provide market access to various services sectors based on the various modes of supply and entry of business persons, on the basis of securing a fair, open, and transparent market for services trade including services supplied electronically. There are significant carve-outs made by Malaysia in this aspect across various areas of service sub-sectors to protect key national interest areas and affirmative policies, including in the area of financial services wherein financial regulators are allowed to take action to ensure integrity and stability of financial markets.

The investment text provides substantive legal protections for investors and covered investments of each TPP country based on the concept of 'National Treatment', MFN and 'Minimum Standard of Treatment' which requires member countries to accord investments of other parties treatment in accordance with applicable 'customary international law principles' including fair and equitable treatment, and full protection and security. These principles are intended to promote non-discrimination, provide a minimum standard of treatment, set rules on expropriation, and prohibits performance requirements that distort trade and investment.

The Investor-state dispute settlement (ISDS) mechanism is also contained within the investment chapter which allows private parties to bring member governments to arbitration for a breach of the obligations under the investment chapter (with safeguards allowing TPP countries to regulate in the public interest). Claimants may submit claims under the ICSID Convention and ICSID Rules of Procedure for Arbitration Proceedings (provided both parties are party to the ICSID Convention), the UNCITRAL Arbitration Rules, or any other arbitral institution and rules as agreed between the parties.

Within this category is also e-commerce, a WTO plus commitment to enhance the viability of the digital economy by ensuring that digital downloads are not subject to customs duties and regulations made in this arena are facilitative and supportive of digital trade, whilst recognising the need to enhance consumer protection.

Category 5 - Business Environment

This is potentially one of the more sensitive areas for Malaysia given that existing rules surrounding government procurement would need to be re-written and be more transparent in procuring entities at the central government level of goods, services and construction services. Procuring government agencies will need to ensure that procurement is conducted in a fair, transparent, and non-discriminatory manner, although specific carve-outs and flexibilities have been negotiated by Malaysia through procurement amounts and categories of goods and services supplied (via gradual reduction in preferences over a period of time).

Within this chapter also sits competition policy for state-owned enterprises ("SOE") which contains disciplines to require SOE's to act in accordance with commercial considerations and not to distort competition in the market through non-commercial assistance. Malaysia has managed to secure some carve-outs and flexibilities, particularly relating to its ability to carry out certain social and economic development programmes, albeit with greater focus and transparency. Given that SOEs manage national resources, however, complying with the TPP will have positive consequences as a result of greater competitiveness and good governance..

Significant "WTO-plus" provisions on intellectual property, labour standards and environmental protection are also contained within this category. Given the length of these chapters, these would necessitate a separate discussion in subsequent alerts.

Category 6 - Member Development and Technical Cooperation

Commitments by member states under this category seek to enhance domestic and regional economic integration via cooperation and capacity building, particularly for small and medium-sized enterprises (“SMEs”) and development of regional production and supply chains. In particular, SMEs have often raised difficulty in understanding and being able to utilise trade agreements due to lack of resources compared to other large enterprises. The commitments under this category include improving trade and investment disciplines, relevant institutions, and providing a mechanism to help all TPP countries in effectively implementing the TPPA and realising its benefits.

Category 7 - Transparency and Dispute Settlement

The regulatory coherence chapter aims to promote good regulatory practices by TPP member countries in developing and implementing regulatory measures, including where necessary obtaining impact assessments of such measures to assess the need and the availability of other alternatives of the regulation being introduced. They include ensuring that regulations are clearly written and available to the public (if possible, online), and that existing regulatory measures are periodically reviewed to determine if they remain the most effective means of achieving the desired objective whilst allowing public input in any decision making process.

The dispute settlement mechanism under this category allows member countries to bring another TPPA member country to dispute settlement proceedings when there are failures to implement commitments and obligations under various chapters from market access, labour, environment, trade in services, intellectual property rights, SOE’s, and others. This mechanism may be triggered if consultations for the early resolution of any of these issues fail.

There are specific timeframes in place to ensure an efficient system, where a panel may be requested within 60 days after the date of receipt of a request for consultation (or 30 days after the date of receipt of a request for perishable goods). Panels are composed of three objective international trade and subject matter experts.

Next Steps

The 12 member countries have two years to ratify the TPPA, upon which the agreement will enter into force. If the TPPA is not ratified by all parties before 4 February 2018, it will enter into force after ratification by at least six states which together have a GDP of more than 85% of the GDP of all signatories. This means that if either the United States or Japan fails to ratify the TPPA, the agreement will not enter into force.

In the interim, the Malaysian Government has set up a national consultative committee to push forward reforms to existing legislation. Based on information released by the Malaysian Government to date, a total of 26 amendments will have to be made in 17 laws to be able to ratify the TPPA. These are summarised as follows:

- i. six amendments, involving enforcement under the Customs Act 1967 and the Free Zone Act 1990;
- ii. two amendments involving origin under the Customs Act 1967 and Free Zone Act 1990;
- iii. nine amendments involving intellectual property rights in the field of patent, copyright, trademark, geographical indications and enforcement under:
 - Trade Mark Act 1976 and Trade Mark Regulations 1997,
 - Patent Act 1983 and Patent Regulations 1986,
 - Copyright Act 1987,
 - Geographical Indications Act 2000,
 - Anti-Money Laundering and Anti-Terrorism Financing Act 2001,
 - Protection of New Plant Varieties (New) 2004 Regulations 2008 and Protection of New Plant Varieties 390/2008 and 389/2008,
 - Communications and Multimedia Act 1998,
 - Control of Drugs and Cosmetics Regulations 1984, Directive No. 2/2011 (relating to “data exclusivity”).
- iv. 10 amendment involving labour, as follows:
 - Trade Union Act 1958,
 - Industrial Relations Act 1967,
 - Passport Act 1966,
 - Minimum Standards of Housing and Amenities Act 1990,
 - Private Employment Agencies Act 1981,
 - Anti-Trafficking in Persons Act 2007,
 - Children and Young Persons (Employment) Act 1966,
 - Sabah and Sarawak Labour Ordinance of the Labour Chapter;
- v. Amendments related to anti-corruption and involving the enforcement under the Malaysian Anti-Corruption Commission Act 2009 in respect of transparency; and

vi. Revisions on existing government procurement regulations to ensure consistency regarding the implementation of regulations under the Treasury Instructions.

Stay tuned for our upcoming chapter specific alerts.

www.wongpartners.com

Wong & Partners
Level 21, Suite 21.01
The Gardens South Tower
Mid Valley City
Lingkaran Syed Putra
59200 Kuala Lumpur

©2016 Wong & Partners. All rights reserved. Wong & Partners is a member of Baker & McKenzie International, a Swiss Verein with member law firms around the world. In accordance with the common terminology used in professional service organizations, reference to a "partner" means a person who is a partner, or equivalent, in such a law firm. Similarly, reference to an "office" means an office of any such law firm.

This may qualify as "Attorney Advertising" requiring notice in some jurisdictions. Prior results do not guarantee a similar outcome.