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**COMPETITION LAW AND SMES IN MALAYSIA: TO EXEMPT
OR NOT?**

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Abstract

The Malaysian Competition Act 2010 prohibits anti-competitive conducts in Malaysia. Whilst the notion of competition law is to promote economic development by protecting the process of competition, these legal obligations might leave Small and Medium Enterprises (SMEs) vulnerable as they are ill equipped to comply with the law. Consequently, SMEs might be pressured to withdraw from the market in lieu of regulatory enforcement risks. This could potentially be detrimental to Malaysia's economic interests, especially in rural areas where SMEs are the main provider of essential services. We argue that the Malaysian government should grant an interim exemption or on a case by case basis to SMEs. Such measures could offer SMEs more time for transition from the traditional or localized network based business structure into a modern competitive business.

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Keywords: Small and medium enterprises; competition law; exemption; exclusion and compliance.



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1. Introduction

The Malaysian Competition Act 2010 (CA) came into effect on 1st January 2012. CA applies to all commercial activities both within and outside Malaysia if their activities has an effect on Malaysia's markets. The CA applies to all businesses except communication, multimedia, and energy sectors. The Act established an independent body known as Malaysian Competition Commission (MyCC, 2011), to enforce competition law and monitor markets for anti-competitive conduct in Malaysia. MyCC in its task conducts advocacy, investigation, market review, grants exemption and issues leniency order. CA is actively enforced in Malaysia in compliance with the ASEAN Economic Community ("AEC") (ASEAN, 2007) as well as to streamline and strengthen the competitiveness (ASEAN 2015) of the Malaysian businesses (ASEAN, 2016). The AEC expects to increase the attractiveness of the ASEAN market, narrow development gaps and promote fair competition between the ten ASEAN Member States (Loo & Foo, 2016). However, Competition Law ("CL") development in pursuance to the CA appears to have overlooked the local Small and Medium Enterprises ("SMEs") unique socio-economic role as local champions in Malaysia's economy in certain contexts. The majority of SMEs are not ready to face the global transformation of business strategies provided by the insurgence of AEC and foreign competition. SMEs represent ninety-seven per cent of business establishments in Malaysia and are responsible for nearly 36 percent of the country's GDP. SMEs also support 65 percent of the country's employment and nearly 18 percent of Malaysia's exports. Therefore, their contributions from an economic perspective are considered significant if not substantial (Qiang & Andersen, 2016). By 2020, Malaysia aims to push SMEs' contribution to 41 percent of GDP and the share of the country's exports from SMEs to 23 percent. So it appears Malaysia's transition to a high-income economy will highly depend on SMEs contribution to GDP growth (The World Bank, 2016).

In 2013, SME Corporation Malaysia (SME Corp) a government agency under the Ministry of International Trade and Industry Malaysia redefined SMEs to reflect new economic developments, incorporate price inflation, structural changes, and business trends. SMEs are defined by sales turnover or number of full-time employees. In the manufacturing sector, SMEs are defined as firms with sales turnover not exceeding RM50 million or the number of full-time employees not exceeding 200. As for the services and other sectors, SMEs are defined as firms with sales turnover not exceeding RM20 million or number of full-time employees not exceeding 75. The definition by size, in context to small refers in the manufacturing sector to enterprises with the sales turnover ranging from RM300, 000 to less than RM15 million or full-time employees numbering from 5 to less than 75 and for medium, where the sales turnover ranges from RM15 million to not exceeding RM50 million or full-time employees numbering from 75 to not exceeding 200. In services and other sectors, sales is defined by the turnover ranging from RM300, 000 to less than RM3 million or full-time employees numbering from 5 to less than 30. Medium size refers to those with sales turnover ranging from RM3 million to not exceeding RM20 million or full-time employees numbering from 30 to not exceeding 70 (SME Corp, 2013). This new classification for SMEs allows the Malaysian government to target more policy assistance and aid for their development. Although it sounds promising, SMEs still fear CL will impact their growth and survivability in the open market. SMEs in Malaysia are also challenged by competition with cheaper imports and foreign competition. SMEs generally lack financial resources and expertise to develop their business structure to

meet the consumer demands for quality, innovation and competitive pricing. Another unique feature of SMEs in Malaysia similar to other Southeast Asian economies, is that they are usually founded by families decades ago with business practices and norms driven by traditional Asian values. Even in modern Malaysia, these business norms continue to regulate their relationships and conduct of SMEs. Now, these business norms and values are under threat because they are being demonised by MyCC through anti-competitive agreements or conducts.

The purpose of this study is to argue that Malaysian SMEs should be given an exemption or at least an interim exemption from competition laws, with a longer term view of developing specific competition policies that addresses the distinctive characteristics of the SMEs in Malaysia without contradicting the regulatory objectives of CA. The approach taken in this paper will be a combination of doctrinal analysis (black letter legal analysis) in the context of broader socio-economic reality. The justification is simple; the law does not exist in a vacuum and the government and regulators should not lose sight of Malaysia's socio-economic realities and business norms. Furthermore, law as a discipline sits oddly between social sciences and humanities, the chosen mixed research methodology reflect the interaction between legal analysis, application of economic concepts, and socio-cultural norms drawn from embedded business practices. To appreciate this claim, it is first necessary to delve into the scope and application of the CL to consider whether or not SMEs deserve to be exempted from the CA.

2. Competition Act 2010 and its impact on SMEs

Competition is regulated in Malaysia under the CA and the Competition Commission Act 2010 (CCA). CA firstly, prohibits enterprises engaging into any anti-competitive agreements whether horizontal or vertical (Section 4 of CA) with an object or effect of significantly preventing, restricting or distorting competition in any market for goods or services (see "Chapter 1 Prohibition"). Secondly, (Section 10 CA) prohibits any abuse of an enterprise's dominant position in any market (see "Chapter 2 Prohibition"). However, mergers and acquisition are not regulated nor is there any indication of any political will to do so for now.

Horizontal agreement refers to agreements entered between enterprises which operate at the same level (normally refers to competitors in the same market) whereas, vertical agreement refers to agreements entered between enterprises operating at different levels (between buyers and sellers at different stages of the production and distribution chain). These agreements are prohibited if they have an anti-competitive object or effect. A vertical anti-competitive agreement includes any price restriction, where an upstream seller imposes a fixed or minimum price that a downstream buyer must re-sell. This is considered as a form of Resale Price Maintenance (RPM) scheme which the MyCC prohibits. The other form of RPM also includes maximum pricing or recommended retail pricing which is commonly practiced among SMEs. For example, a manufacturer fixes the price for which its products are sold at the retail level. This is anti-competitive because it does not allow re-sellers or retailers to compete their price. On the same note, an exclusive distribution agreement or exclusive customer allocation agreement is also regarded as anti-competitive if there is no inter-brand competition (competition from other brands) in the market. The MyCC conducts market survey to assess how much of the market share is foreclosed to new entrants and other competitors in the relevant markets to decide whether the anti-competitive impact in

the agreements is significant. Thus, only agreements which significantly prevent, restrict, or distort competition in any market for goods or services are prohibited under the CA. The word 'significant' is interpreted as agreements having more than a trivial impact and assessed based on combined market share of all those participating in such an agreement with more than 20 per cent of the market share or if non-competitors each hold 25 per cent market share on that competition market. This approach is considered as a 'safe harbour' for deciding anti-non-trivial competitive agreements or trade association decisions which is otherwise prohibited. This prohibition applies to SMEs without any consideration for their size either at horizontal or vertical level. Any price-fixing, sharing of markets or sources of supply, limiting or controlling production, market access, technical and technological development, or investment and bid rigging are considered as infringement and may be subjected to penalty. MyCC enforcement efficiency relies heavily on complaints from the general public and business community. Unfortunately, information about SMEs market share in Malaysia is often unavailable. SMEs especially in rural areas, commonly form informal partnerships and share information through local networks. This practice is the norm for many generations in Malaysia dating back to the colonial administration (The Star, 2012). As such, these businesses are so accustomed to this norms that they are blind to the risk of infringing the CL. In the SMEs' perception, CA makes no business sense and should not be applied to them (See CHFA case). Hence, anti-competitive arrangements involving price-fixing and concerted practice are widely practiced among SME sectors like the barber business, coffee shops and matrimonial services through their trade associations. 'Concerted practice' involves informal co-operation amongst SMEs or members of business associations to knowingly set and abide by a price without any reasonable justification. CA strictly requires every competitor to make decisions independently.

These common anti-competitive conducts reflect the SMEs' level of understanding, awareness, knowledge and perception of CL. CA requires SMEs to change their business practices and norms. The use of prosecution or litigation to change could backfire because it would cause resentment or compel superficial compliance which will defeat the purpose of the law. Furthermore, in most cases SMEs can neither afford a legal counsel nor pay the fine imposed on them. In time, such regulatory enforcement risks driving SMEs out of certain sectors or areas. Studies reflect that excessive regulations constrain small businesses' survival and growth (Hassan, 2015).

3. Scope of Competition Exclusion and Exemption in Malaysia

The CA in 2010 introduced a comprehensive competition law regime in Malaysia. However, the second schedule of CA excludes: (1) agreement or conduct that complies with any legislative requirement; (2) collective bargaining for employment; and (3) an enterprise entrusted with the operation of services of general economic interest or having the character of a revenue-producing monopoly. Section 13(2) of the CA gives the Minister discretionary powers to amend the Second Schedule as long as the procedural requirements under section 13(3) of CA are met. The CA also does not apply to the communications, petroleum and energy sectors which are regulated by their sector specific regulations. Therefore, an individual exemption can be granted by MyCC under certain conditions, for a limited duration in the prescribed form and upon payment of the prescribed fee. As such, it is left to the parties concerned to demonstrate the claimed benefits according to the criteria set out in Section 5 of the CA. An

individual exemption can be cancelled or varied if there is a material change of circumstances or there is a breach or non-compliance of an imposed condition. The law also does not limit applications by single enterprises; it allows trade bodies or associations representing such enterprises to apply for a block exemption for categories of agreements entered into by the members of the association.

MyCC has received only one application for individual exemption and three applications for block exemptions filed by their trade associations on behalf of their members (The Star, 2012). The application for exemption can be made either through the Minister or MyCC, but the procedure is found to be very tedious and costly. An enterprise that seeks to apply for an individual exemption or a block exemption under the Act must submit a written application together with a fee of RM50, 000 for each application. The enterprises granted block exemptions must also pay an annual fee of RM20, 000 for every year that the block exemption is in effect. The individual enterprises that have been granted an individual exemption, must pay an annual fee of RM10, 000 for each year that the individual exemption remains in effect. These fees are claimed to cover the manpower costs for MyCC to study and review the applications. The fee imposed also acts as an incentive for companies and industries to conduct their own assessments instead of leaving the task to MyCC (Loh, 2012).

4. Significance of CL on SMEs and Trade Associations in Malaysia

Notably, the very first case of CA infringement was as an SME in March 2012 under section 40 CA. The case ruled that the public announcement of the President of the Cameron Highlands Floriculturist Associations (CHFA) to increase the prices of cut flowers by 10 percent, as price fixing agreement at horizontal level under section 4(2) of CA. However, instead of imposing a financial penalty, MyCC instructed the CHFA to cease the act of fixing prices and ordered a letter of undertaking from its members to refrain from any anti-competitive practices in the relevant market. CHFA was also asked to issue a public statement of the remedial actions. MyCC adopted a soft approach in this case because it was within their first year of enforcement. If they had imposed a fine which would have been RM20, 000 and an additional RM1, 000 for every additional day of non-compliance, the SMEs would have found it too heavy a penalty. Interestingly, MyCC came know about the act of infringement from an open press announcement by the association that indicated members of the CHFA had agreed to increase the price of flowers by 10 percent. CHFA was totally unaware that price fixing was prohibited and had incriminated themselves by advertising it openly. From the SMEs' perspective, the culture of sharing price information, amongst themselves had been a business norm (Ng, 2012) dating back to the colonial days for over a century and, in fact, is one of the main reasons for the formation of trade associations.

MyCC declared affirmatively in the CHFA case that it will investigate cartels or any form of price fixing arrangement regardless of whether the agreement involves any large multinational companies or as small as the family-run businesses or any trade organization (Ramaiah, 2013). Unfortunately, CHFA case did not serve as a lesson or warning for other SMEs. On 30 January 2015, MyCC fined twenty-five ice manufacturers, between RM1, 200 and RM106, 000 for price rigging when they announced their selling price of edible tube ice and block ice for Kuala Lumpur, Selangor and Putrajaya in the newspapers. MyCC imposes a financial penalty of not more than 10 percent of the enterprises' turnover. The MyCC Guidelines on anti-competitive agreements relating to prohibition under Section 4 of the Act states that

there is no necessity for the Commission to prove effects of the agreement once an object agreement is established.

On another occasion on 12 February 2015, MyCC charged 15 members of the Sibü Confectionery and Bakery Association (SCBA) for price fixing when their minutes of the AGM indicated that the attendees had engaged in an agreement to increase the prices of confectionery and bakery products by 10 percent to 15 percent in Sibü, Sarawak (MyCC, 2015). MyCC also fined another SME providing information technology service to shipping and logistics industry and four container depot operators to have engaged in price-cartel activities prohibited under Section 4(1) and Section 4(2) (a) of CA on 1 June 2016. The five companies were fined a total of RM645, 774 and an addition penalty of RM7, 000 for each day for non-compliance of remedial actions within 30 days from the date of the decision (The Star, 2016).

The MyCC Guidelines on Chapter 1 Prohibitions (Anti-Competitive Agreement) indicates clearly an anti-competitive agreement could also be found when competitors attend a business lunch and listen to a proposal for a price increase without objection. Therefore, competitors should avoid meetings or any forms of communication with other competitors particularly where price is likely to be discussed. Thus, the mere presence of competitors at an industry association meeting where an anti-competitive decision was made may be sufficient to be later implicated as a party to that agreement.

Price fixing appears to be the most common business arrangement amongst SMEs. Price fixing arrangement such as Retail Price Management (RPM) allows the manufacturer to provide high and sufficient profit margin to the retailers to provide retail services such as pre-sale display, product specific-information, store hours, adequate inventory, and post-sale service to increase. Price fixing in this context includes fixing the price itself or fixing an element of the price, such as fixing a discount, setting a percentage price increase or setting the permitted range of prices between competitors. It also includes setting the price of transport charges (such as fuel charges), credit interest rate terms, etc. An agreement or arrangement to indirectly or verbally to restrict price competition, such as recommended pricing is also considered as price-fixing (Nasarudin, Zuhairah, Halyani, & Haniff, 2013).

The above cases reflect SMEs and SME related trade associations are either unfamiliar and unwary or totally ignorant of their legal obligations under the CA. A survey of 2,280 respondents in 2014 by SME Corporation Malaysia with National SME Development Council (NSDC) revealed that SMEs are generally unsure whether their business practices violate CA and had very low level of awareness of CA. Only 27 percent of the SMEs were aware of CA and 42.7 percent agreed with other firms to standardise the selling price of goods/services. Meanwhile, 54 percent agreed with other firms for bidding that one firm amongst group is allowed to win bids while 56.8 percent agreed to raise prices of goods if advised by their trade association (SME Corp. Malaysia, 2015). Therefore, it would appear that unfamiliarity with the law is the prime reason for SMEs' non-compliance with the CA.

5. Why SMEs should be considered for exemption

SMEs undeniably have a key role in transition and developing a country's national economy. SMEs account for more than 90 percent of all firms outside the agricultural sector and constitute a major source of employment besides helping to generate significant domestic and export earnings (OECD, 2004). As such, SME development is a key instrument for poverty reduction efforts. However, economic

globalization has exposed developing countries to major challenges in strengthening their human and institutional capacities whilst taking advantage of trade and investment opportunities. Although governments make policies to advance trade and investment, it is the enterprises that trade and invest. Thus, globalization plus the digital economy has brought upon SMEs new challenges like the sudden increase in competition from imports and entry of new as well as large foreign investors in the domestic market. Although CL safeguards SMEs' economic opportunities from large incumbents and limits their abusive behaviour, SMEs are weaker in the sense that they rely disproportionately on traditional finance from banks which makes them more vulnerable to anti-trust abuses in the financial sector (OECD 2009).

The rise of e-commerce and online marketing also affects SMEs' competitive edge. Although, SMEs benefited by being provided access to the previously inaccessible geographical market through digital marketing with innovative start-ups and price cutting methods, the investigation on abuse of online searches (See FTC File No111 0163 Google Inc.) proves otherwise. SMEs are often found to be disproportionately affected by abuses of dominant undertakings in this area (UNCTAD, 2015). In reality, SMEs in developing countries are pressured to adjust to the competitive strategies of the Multi-National Corporations (MNCs) in different countries with overwhelming public and privately set standards (e.g. on sanitary, safety and phytosanitary) and to accommodate changes in international tastes, prices, and competitive conditions. Therefore, there are some supply-side bottlenecks in the trade and investment areas and how governments, development partners and the private sector address these constraints have implications on SMEs' economic growth potential (OECD, 2004). In this regard in developing economies like Malaysia, SMEs depend very much on the government to implement relevant policies and strategies to aid them. Granting an exemption from the CA would constitute a form of assistance from the government in terms of helping the affected SMEs to develop scale and scope, but does this justify that they deserve different treatment under the CA? The relatively weaker bargaining power and poor liquidity of SMEs makes them strongly dependent on regulatory frameworks that guarantee the reliability of transactions and secure orderly playing rules in the economy (OECD, 2000) to promote fair competition. Thus, SMEs may not be treated differently but, with the aim of providing fair competition, exemptions may be justified with some flexibility for SMEs to develop a fair bargaining power to adjust and attain the competitive edge.

6. Scope of Exemption for SMEs from Competition Law

Even though Malaysia is transitioning from a developing economy into a developed one, the peninsula has vast rural and underdeveloped land masses. Many of the SMEs are owned, governed, and operated by families (Yeung, 2004). These local companies face many challenges for survival in an adverse business environment, in particular with the Malaysia's ethnically-biased policies, through a close network of entrepreneurs (Redding, 1990), many of whom formalized their relationships by forming trade associations (El Kahal, 2001). Furthermore, this business network is a system of credit-worthiness through an institutionalized system of trust, where access to information and resources are limited to such an extent that without access or connections to these networks, many SMEs in Malaysia would not be able to manage to survive the uncertainties in a transitioning economy (Kuo, 1996). In addition, many traditions and customs of rural societies still thrive in many smaller cities, as such the business mentality

and practices of SMEs acting in concert so as to create a harmonious society remains a norm (Goh, 2002). However, since the enactment of the CA is to promote an efficient and competitive economy, logically the enforcement against SMEs for violation should be viewed as a good thing. So, why consider exempting SMEs from these laws? Experts have pointed out that the government has a critical role to play in SMEs' success through discussions on how to improve SMEs' access to market and investment opportunities (Caraballo, 2016). The government has to play an important role to enable and facilitate the linkages and access to markets, finance and technology besides removing the various barriers to entry and exit in the context of the new CL.

According to Khemani (2002), exemptions and exceptions from CL obligations should be granted for social, economic, and political reasons which incidentally do not imply the weakening of competition law enforcement. Khemani (2002) observed there are legal instruments providing for exemptions in the European Union, Canada, US, New Zealand, and many Latin American countries to facilitate transition and competition edge. This goes to show that providing exemptions is not detrimental to the competitiveness of an economy. However, grounds for exemption must be for valid economic, social or political reasons and not overly undermine the aim of CL itself. As noted earlier, Malaysia does have block exemption policies in place but no specific policies aimed at the SMEs exist.

Generally, the implementation of CL has a multiple set of values that are neither easily quantifiable nor reducible to a single economic objective. These values often reflect a society's wishes, culture, history, institutions, and other factors that cannot be ignored nor should necessarily be ignored. The survey analysis on the objectives of the competition policy over time and across several countries had indicated that the nature and scope of CL tend to vary according to the comparative needs of the nation. For example, when the Sherman Act was enacted in 1890 (and for much of the 20th century), there was an explicit preference for "pluralism" in terms of diffusion of economic power and there was a tendency towards protection of small business and local economies. In the European Union, priority is given to economic or market integration and prevention of dominance by large firms (Ramaiah, 2016). German competition laws even provide for explicit possibility of so called "SME Cartel" in their competition code for SMEs co-operation agreement (UNCTAD, 2015). Thus, this paper argues that there are grounds for justifying exemption or an interim exemption for SMEs in Malaysia.

Malaysian's SMEs, although coming to terms with transitioning from a developing to a developed economy, still require time for much of the business practices and culture to change. Whilst, this is not a good enough reason for exemption, the CA, affecting ninety-seven percent of business establishments in Malaysia, enforcing the law for the sake of enforcement could inflict economic losses to the nation. There are a few reasons for this. For starters, the law is based on neo-classical economic assumptions about markets that do not take into consideration cultural and norms of businesses from non-Western economies. Over the last two or more decades, overwhelming research has demonstrated that culture matters in Asian business management and development to such an extent that these cross-cultural differences have been taught as part of international business management courses, yet competition law specialists have only just taken notice of it (see Healey & Young, 2015; Chan, Datwani, & Young, 2016). Furthermore, Malaysia is in a transitioning economy, as such the cost of production and prices in general are low as compared to developed economies. Therefore, concerns about potential harm from economic

inefficiency and detrimental to consumers' benefits in Malaysia are perhaps not as acute as those in developed economies. Next, with the threat of regulatory enforcement, SMEs could exit certain industries that deliver moderate returns on capital compared to the cost of compliance. For rural or even remote communities, the withdrawal of certain services or manufacturers could be devastating for those communities that depend on SMEs for employment and essential services. Thus, a 'one size fit all' CL application is not appropriate for Malaysia's current stage of economic and social transition. Hence, exempting SMEs in Malaysia, at least for an interim period would provide time for SMEs to transform their businesses to meet the demands of a modern economy including complying with CA.

In addition to an interim exemption, the Malaysian government should also assist SMEs to transform their businesses. Without appropriate assistance, finance, and training, enforcing CA obligations are nothing more than a form of penalty for not being able to keep up with their counterparts in developed economies. Furthermore, rural areas in Malaysia should not be treated the same as major cities with large infrastructures and modern conveniences. If SMEs in rural parts of Malaysia are forced to leave the market due to the high cost of compliance, this would defeat the objectives of the CA. In major cities, exemptions could be given to SMEs that are in the process of modernizing. If this is not feasible, given the scale, the enforcement policies of MyCC should consider assessing the level of harms SMEs would inflict on consumers or overall competitiveness of specific industries before deciding to take enforcement action. Therefore, arguments in favour of an interim exemption are made based on economic and socio-economic grounds.

7. Conclusions and Recommendations

This paper recommends that the MyCC and legislators should consider offering an interim exemption or certain exclusions for SMEs in the interest of the local economy of certain small and rural communities from the full rigor of the competition law. Such measures should not deflect from the overall competitiveness of the market as it allows time for SMEs as the local champions to transition from traditional or localized network based business structure into a modern competitive business environment. Otherwise, the enforcement of CA would likely do more harm than good to the economy.

Under the law, the Minister or the MyCC could grant SMEs in rural areas exemption and for those in major cities on a case-by-case basis. However, there are certain technical difficulties associated with this, namely to define rural areas and coming up with criteria for those in major cities. Perhaps, the lucid and most straight forward approach for the Malaysian government is to consider instituting turnover thresholds to exclude SMEs from competition law obligations like in Hong Kong, where the combined turnover of the undertakings involved does not exceed HKD 200,000,000 in the relevant turnover period for anti-competitive conduct, and an undertaking with turnover not exceeding HKD 40,000,000 in the relevant turnover period (Hong Kong Competition Commission, 2016). Then again, the calculation of turnover for SMEs with little resources might pose some technical challenges.

Secondly, the regulator in cases of anti-competitive conducts should not necessarily take the matter before the courts, thereby requiring all involved parties to incur significant legal fees. If the impact of the conduct in question on the economy is not great, the regulator should maintain the resolution by settlement (practiced in some cases now, but not a set standard) with the party under investigation, rather

than initiate formal judicial proceedings which does not impose burdening settlement in the form of a fine or require an undertaking to stop the conduct in question, or both.

In conclusion this article acknowledges that a prime facie argument for an interim exemption for the SMEs from CA has been presented. Clearly, more quantitative and qualitative research needs to be conducted to make stronger recommendations as to the quantum of exemptions and legal economical assessment to be applied.

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