The Theory of Harm under the Malaysian Competition Act 2010

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ABSTRACT

The Malaysian Competition Act 2010 (CA 2010) seeks to promote the process of competition in the market by preventing anti-competitive conduct that harms competition. However, ‘harm to competition’ is not clearly defined in the Act and neither are its subsequent guidelines. Without proper application of the theory of harm, the competition authority will not be able to provide a consistent approach to the assessment of the competition issues especially in determining whether or not a conduct is anti-competitive. This paper aims to analyse how and to what extent the Malaysian Competition Commission (MyCC) applies the theory of harm in competition law analysis. This paper argues that there is no standard definition of what ‘harm to competition’ means in the context of Malaysian competition law. ‘Harm to competition’ may be interpreted as harm to the competitive process and consumers (final consumers). It may also be narrowly interpreted as harm to market mechanism or the ability to compete, through, for example, unjustified exclusion of rivals from the market without the need to prove that conduct was harmful i.e. reduced aggregate consumer welfare. In most situations, the issue of competitive harm is not about interpretation but rather of proof that a particular conduct really harmed competition and consumers.

Keywords: Competition, competitive harm, competition law, discriminatory abuse, theory of harm

INTRODUCTION

Competition law is the Magna Carta for market players to compete in the market. Competition law seeks to protect the process of competition from any conduct that has an effect on or harms competition.
In competition law analysis, the application of the theory of harm is important to assist the competition authority to determine whether or not a particular conduct is anti-competitive. The theory of harm will be used as a parameter to determine whether conduct by firms in the market contravene competition law provisions. The proper application of the theory of harm may result in legal consistency and predictability. It constraints the competition authority from prohibiting pro-competitive conduct or protecting inefficient firms or competitors in the market, which by itself harms competition. However, ‘harm to competition’ is hard to define and has been a source of debates among competition law scholars around the world. In the area of anti-competitive agreements such as a cartel, harm to competition may simply mean harm to consumer welfare through price increase or output limitation.

The application of the theory of harm in competition law analysis becomes more complicated in the case of exclusionary practices under the abuse of dominant position prohibition. There has been continuous debate on what ‘harm to competition’ means in developed jurisdiction such as the United States and the European countries. In the United States, the current approach to competitive harm in the context of exclusionary conduct is that there should be non-interference by the competition authority in the market unless the exclusionary conduct reduces aggregate consumer welfare in the form of output limitation (Fox, 2002). Unjustified exclusionary conduct without consumer harm may not be anti-competitive in the USA. This is important to ensure that the law will not protect inefficient firms that harm consumers. Similarly, in the EU, the main objective of the European competition law is to ensure that dominant undertakings do not abuse their dominant position by foreclosing their competitors from any market, thus having an adverse impact on consumers in the form of higher price and output or quality reduction (Commission, 2009, para 19). However, there have been arguments that the application of the theory of competitive harm in the EU is wider than output reduction or price increase. In some cases, conduct that restricts the freedom or ability to compete (or economic freedom) is considered anti-competitive even though it does not reduce consumer welfare (Fox, 2002; Gormsen, 2007; Forum, 2006).

This paper will explore the application of the theory of harm under the Malaysian Competition Act 2010. The rest of the paper will be arranged as follows: Part 2 will explore the application of the theory of harm in the area of restrictive agreement under Section 4 of the CA 2010. Due to limited space, the discussion will focus on anti-competitive by ‘object’ and will not cover anti-competitive by ‘effect’. Part 3 will explore the application of the theory of harm in the area of abuse of dominant position under Section 10 of the CA 2010, focussing on the exclusionary conduct of a dominant firm. Part 4 of this paper will explore the application of the theory of harm in a new category of abusive conduct known
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Anti-Competitive Agreement

Section 4 of the CA 2010 prohibits anti-competitive agreement that has the object or effect significantly restrict, prevent or distort competition in the relevant market. It is obvious that Section 4 is concerned with conduct that affects or harms competition in the market. Competition law differentiates between restrictions by ‘object’ or ‘effect’. Section 4(2) of the CA 2010 laid down conduct that deemed to have the object of significantly restricting, preventing or distorting competition. This provision is considered a deeming provision and MyCC is under no duty to carry out detailed economic analysis to determine whether conduct that is listed under Section 4(2) is anti-competitive (MyCC, Guidelines on Chapter 1 Prohibition, 2012). Does this mean that the theory of harm does not play an important role in competition law analysis under the object rule? The answer is no. The theory of competitive harm under ‘object’ rule is rather obvious. The legal structure of Section 4(2) was built on the premise that the objects of cartel agreements such as price fixing and market sharing are so obviously preventing competitors from competing with each other. There is a legal presumption (based on experience, for example) that the conduct creates a harmful effect on consumers, leading to price increase and output reduction with a low possibility of countervailing efficiency benefits (Walker, 2012).

The categorisation of certain conduct under the ‘object’ rule allows MyCC to dispense with full-fledged analysis of competitive harm in determining whether or not a particular conduct is anti-competitive. The issue is not whether there is proper application of the theory of harm but rather to what extent the competition authority should prove that there is actual harm suffered by the consumers. The issue of the theory of harm becomes the issue of proof rather than of application. Under the object rule, MyCC will proceed with its case against anti-competitive conduct based on speculation or abstract competitive harm without even the need to substantiate the allegations with evidence. The plausible reason for this is to reduce the burden of the competition authority to prove each and every serious cartel case and shift the burden to parties to the agreement to prove that the agreement has countervailing efficiency benefits and fulfil all the criteria under the balancing test regime of Section 5 of the CA 2010.

In order to further illustrate the application of the theory of harm, this paper will analyse the MyCC’s decision against Malaysia Airlines System Bhd (MAS) and AirAsia Bhd (AirAsia) for their market sharing agreement.

Case of MAS-AirAsia

MAS and AirAsia were charged under Section 4(2) of the Competition Act 2010 for entering into a market sharing agreement (known as Collaborative Agreement) on 9 August, 2011 followed by a supplemental
agreement dated 2 May, 2012. Based on Clause 5 of the Collaborative Agreement, the parties to the agreement, MAS, AirAsia and AirAsia X, agreed to allocate the following markets: MAS would focus on being a full-service premium carrier (FSC), AirAsia would focus on being a regional low-cost carrier (LCC) and AirAsia X would focus on being a medium-to-long haul LCC (MyCC Final Decision, 2014). The effect of this agreement was that each party to the agreement agreed to focus on their market segment and not to enter into the area that was specifically allocated to the competitors. Clause 9 of the Collaborative Agreement establishes a Joint Collaboration Committee (JCC) to implement, manage and monitor compliance with the agreement. Based on the Collaborative Agreement, MyCC found that MAS-AirAsia had breached Section 4(2) of the Competition Act 2010 for sharing the market of air transport in Malaysia between each other to rationalise their business operations. Market sharing is considered hardcore restriction and anti-competitive by ‘object’.

Before the collaboration agreement was entered into, MAS’ subsidiary, FireFly, was formed to compete with AirAsia in the domestic market. The competition had reduced AirAsia’s market share drastically (MyCC, Final Decision, 2014). Therefore, instead of competing with each other, they entered into a cooperative arrangement “to maximize their commercial revenue, by sharing market.” MyCC was of the view that “the restriction [was] obvious; MAS and AirAsia [had] agreed not to compete with each other, either themselves or through their subsidiaries, thus eliminating any possibilities of competition between the parties” (MyCC, Final Decision, 2014).

Did MyCC spell out the theory of harm in this case? The competition authority elaborated further on what we call the ‘theoretical harm of market sharing’: MyCC stated that “it provides them the freedom to impose higher prices to maximize profitability without any competition. This will eventually leave consumers to face the increased likelihood of higher airfares and fewer choices.” (MyCC, Final Decision, 2014). However, this theoretical harm was actually substantiated with evidence of output limitation. Subsequent to the Collaboration Agreement, MyCC found that MAS through FireFly’s operation withdrew its operation for flight from Kuala Lumpur to Sabah and Sarawak route, leaving AirAsia as the sole low-cost carrier for the routes.

The demand substitutability is somewhat limited for domestic flight services due to the government cabotage policy, which only allows locally-owned airlines operators to carry passenger between any two points within Malaysia and between Peninsular Malaysia and both Sabah Sarawak. In addition, flights between Peninsular Malaysia and Sabah and Sarawak are not substitutable for other transportation means. To this point MyCC found that “consumers who travelled between Malaysia and both Sabah and Sarawak were directly affected following the market exit of FireFly” (MyCC Final Decision, 2014). Even though, the MAS-Air case showed that MyCC took
into consideration the actual consumer harm, it is still not clear whether MyCC are bound to consider the same in all cases that fall under the ‘object’ category since the regulatory scheme of Section 4(2) is based on the presumption that hardcore cartel harms consumers.

**Abuse of Dominant Position-Exclusionary Conduct**

The application of the theory of harm can be extended to the case of abuse of dominant position under Section 10 of the Competition Act 2010. Section 10 of the CA 2010 prohibits a firm in dominant position from abusing its position in any market for goods or services. This means that being a dominant by itself is not an offence under the Act. However, the dominant firm has special responsibilities not to act in a manner that may hamper competition by, for example, engaging in exclusionary practices. Unlike anti-competitive behaviour under Section 4, Section 10 regulates unilateral action by a dominant firm. ‘Harm to competition’ under Section 10 may be different from ‘harm to competition’ under Section 4. Section 10(2) of the CA 2010 lays down a non-exhaustive list of abusive conduct.

Based on the Guidelines issued by MyCC, abusive conduct can be categorised into exploitative and exclusionary (MyCC, Guidelines on Chapter 2 Prohibition, 2012). Exploitative means the ability of an enterprise to maintain price above the competitive level for some time without worrying about whether consumers will switch to other producers or new competitors will enter into the market offering the same products. Exploitative conduct refers to excessive price imposed on consumers to gain higher profits and not a result of innovation. In regulating this exploitative behaviour, it seems that MyCC will look at the extent to which the abusive conduct harms consumers in the form of higher price (MyCC, Guidelines on Chapter 2 Prohibition, 2012). Exclusionary conduct, on the other hand, means the ability of an enterprise to dictate the level of competition in a market by preventing new competitors from entering into the market or significantly harming the existing equally efficient competitors by preventing them from effectively competing in the market. Based on MyCC Guidelines, the Commission will adopt the effect-based approach to determine whether or not a unilateral conduct is anti-competitive (MyCC, Guidelines on Chapter 2 Prohibition, 2012).

In order to assess the effect of exclusionary conduct, MyCC will use two main tests: whether the conduct adversely affects consumers and whether the conduct excludes competitors that are just as efficient as the dominant firm. Based on these guidelines, it can be safely concluded that ‘harm to competition’ in the context of exclusionary conduct is harm to competitive process, namely, the impairment of the ability of efficient firms to compete and also harm to consumers. It was argued that the competition authority should consider the competitive process and consumers together because it is difficult to infer consumer harm from harm to competition in the case
of exclusionary conduct (Majumdar, 2008). Focus on consumer does not mean that the competition authority should ignore harm to efficient competitors. In fact, harm to efficient competitors is important because in exclusionary cases, the impairment of rivals’ ability to constrain the dominant firm from exercising its market power is a way that harm to consumer is caused (Jacobson, 2002). On the other hand, the impairment of the ability of the rivals to compete does not necessarily reduce consumer welfare.

Jacobson (2002) offers a three-step analysis to determine whether or not an exclusionary conduct is anti-competitive. The first step is to assess the market position of the dominant firm and the condition of the relevant market. For example, if the dominant firm captures a significant part of the upstream market, it is most likely that the conduct of the dominant firm contributes to the foreclosure of the market from other competitors in the downstream market. The second step is to analyse whether the conduct impairs the ability of the competitors to compete. The impairment can be measured by taking into consideration whether the conduct: lowers the rivals’ price; increases the rivals’ cost or lowers the rivals’ demand (Buccirossi, 2010). The main important consideration is to assess the effect of the conduct on the rivals’ costs, namely, the extent to which the conduct raises the rivals’ cost and the cost increase cannot be avoided through reasonable practical means (Jacobson, 2002). For the proper application of the theory of harm and to further strengthen the competition enforcement, the competition authority may support its assessment with the possible evidence of foreclosure such as the evidence which indicates that market share of the dominant firm is maintained or expanded, actual competitors may have been marginalised or may have exited or potential competitors may have tried to enter the market and failed (Commission, 2009).

The third step is to assess whether the impairment of the rivals’ ability to compete leads to consumer harm in the form of higher price or in some other forms such as limiting quality or reducing consumer choice or preventing new products and innovations from being offered to the market (Commission, 2009). There should be a direct link between the foreclosure effect and consumer harm. To further illustrate the application of the theory of harm in exclusionary conduct, this paper will discuss the decision made by MyCC against two giant companies, Megasteel Sdn Bhd (Megasteel) and MyEG Services Bhd (MyEG).

Case of Megasteel
Exclusionary conduct denotes that there must be some forms of competition between a dominant firm and non-dominant firms. In Megasteel’s case, MyCC has decided in its proposed decision that Megasteel had infringed Section 10(1) of the Competition Act 2010 by engaging in a margin squeeze in the Hot Rolled Coil (‘HRC’) market in Malaysia. Margin squeeze is considered
an abusive conduct even though it is not listed under Section 10(2) or in the MyCC Guidelines on Chapter 2, Prohibition.

Margin squeeze happens when a firm that controls the raw material market, supplies the raw material to other firms in the downstream market to produce another finished product at a price that those who purchase it do not have a sufficient profit margin (Commission, 2009) (Industrie des Poudres Sphériques v Commission, 2000). This happens because, most of the time, the dominant firm also produces the finished product in competition with the firms in the downstream market. Megasteel is the sole supplier of Hot Rolled Coil (HRC). Entry barriers in this market are quite high. Firms need to get a licence from the Ministry of International Trade and Industry (MITI) to supply the HRC. Even though three other companies had been given a licence to produce the HRC, Megasteel remains the sole supplier due to high sunk costs and high capital investment to build a HRC plant. HRC is an important raw material to produce another kind of steel, Cold Rolled Coil (CRC). Megasteel sells HRC to the downstream players that produce CRC. However, Megasteel plays a dual role as a wholesaler and internal buyer as it also produces CRC, competing with other players in the downstream market.

In order to determine whether Megasteel has engaged in margin squeeze, MyCC applies the ‘equally efficient test’ by assessing whether the dominant enterprise could not offer its downstream product (CRC) otherwise than at loss if it had been forced to pay its own price for the output. It is important to show that the dominant’s downstream business could not operate profitably based on the price that it charged the downstream enterprises.

In the proposed decision, MyCC found out that the margin between Megasteel net selling CRC and net selling HRC was lower than the costs that it must incur in transforming HRC to CRC (MyCC, 2013). Therefore, MyCC concluded that Megasteel’s conduct had the effect of hindering the competitive process at the downstream market as an equally efficient firm cannot operate its business without incurring losses (MyCC, 2013). It can be concluded that harm to competition in this case meant harm to the competitive process of any market especially the market in which Megasteel was participating. However, there was no direct evidence to show that the competitors had been marginalised by, for example, raising their costs of operation or lowering their demand. There was also no direct evidence to suggest that the conduct had resulted in consumer harm in the form of higher price and output reduction. After conducting further analysis and taking into consideration both written and oral representation submitted by the Megasteel, MyCC found no evidence to support the allegation that Megasteel had engaged in margin squeeze by undercutting its CRC price that could hamper the competition in the downstream market (MyCC, Non-Infringement Decision, 2016).
Case of MyEG
MyCC had taken action against MyEG for abusing its dominant position in the provision and management of online renewal of Foreign Workers Permits (PLKS) in breach of Section 10(2)(d) of the CA 2010. MyEG is a monopoly in the provision of the PLKS renewal service. In order to renew the permits, the employers are required to purchase mandatory insurance, including the Foreign Workers’ Insurance Guarantee (FWIG), Foreign Workers’ Compensation Scheme (FWCS) and Foreign Workers’ Hospitalisation and Surgical Scheme (FWHS). MyEG had established a subsidiary, MyEG Commerce, to act as an agent for RHB Insurance, competing with other insurance companies and agents in providing the mandatory insurance.

MyEG had induced the employers of foreign workers to purchase both FWHS and FWCS through MyEG if the employers wanted faster and easier renewal. MyEG had also invariably created difficulties by adding additional steps for the employers to purchase the Mandatory Insurance through other insurance companies. “The other insurance companies as well as their agents who are competing with both RHB Insurance and MyEG are facing unfavourable conditions as it would invariably take a longer time to obtain PLKS approval as their policies would have to be verified” (MyCC, Final Decision 2016).

MyCC was of the view that MyEG had been leveraging its market power at the downstream market, which is the market for the sale of the mandatory insurance. The economic evidence showed that the commission earned by MyEG for the sale of mandatory insurance has increased tremendously during the period in which MyEG started to gain its dominant position in the upstream market, which is the market for the provision of PLKS renewal service. Evidence also showed that due to this discriminatory practice RHB Insurance via MyEG had captured increased sales within a short period of time, snapping larger market shares from its competitors. MyCC found that the discriminatory conduct practised by MyEG had harmed competition in the market for the sale of Mandatory Insurances for online foreign workers’ permit renewal (downstream market) in which MyEG, through its subsidiary MyEG Commerce, was a participant (MyCC, Final Decision 2016). However, MyCC did not offer any evidence that the discriminatory conduct engaged in by MyEG had reduced consumer welfare in the form of high price or output reduction.

Discriminatory Abuse
In the previous part, we have stated that in exclusionary conduct, there must be at least some form of competition between the dominant and non-dominant enterprises. The requirement to carry out ‘equally efficient test’ is to make sure that the law will not be used to protect inefficient competitors. However, there is a situation where a dominant enterprise may abuse its dominant position in a market without
even competing in that market by favouring third-party distributors over others (Colomo, 2014).

Section 10(2)(d) of the CA 2010 prohibits a dominant from engaging in discriminatory practices that may not only harm competition in which the dominant firm is participating, but also harm any upstream or downstream market. Based on the wording of Section 10(2)(d), the law does not require the competition authority to establish the competitive nexus between the dominant firm and other firms in a particular market. Firms may discriminate based on various reasons such as nationality, geographical area or even race etc. For example, in the EU case of British Airways (BA), the court held that BA had breached Section 101(d) for applying different commission rates to travel agents operating in the United Kingdom, even though BA did not compete with the travel agents (British Airways v Commission, 2007). In this situation, even though the dominant firm may not be competing in the impaired market (for example, the downstream market), the abusive conduct (discriminatory practice) will interrupt the normal process of competition in the downstream market, impeding the ability of one or more firms to compete in the downstream market by increasing its costs and lowering its profits. This leads to the emergence of a new category of abusive conduct, namely, discriminatory abusive.

There are also cases where even firms in a market in which the abuse occurs do not compete with each other. But, each firm may use the important materials to produce different products and therefore, not compete with each other. In the EU regime, there were numerous occasions in which the Commission and court applied a broad interpretation of 82(c) (now Article 102) to exploitative discrimination between customers who were not competing in the same market (Akman, 2006).

In the case of United Brands for example, it was found that conduct can be discriminatory even though the market players in the downstream market, such as distributors from different member states, did not compete with each other (United Brands v Commission, 1978). In the case of Corsica Ferries I, it was held that Article 102(c) applies even though local and international shipping lines did not compete with each other (Corsica Ferries Italia Srl v. Corporazione dei Piloti del Porto di Genova, 1994). In the case of Deutsche Post-Interception of Cross-Border Mail, it was held that “in any event, the Court of Justice has stated that the list of abuses mentioned in Article 102 itself is not exhaustive and thus only serves as examples of possible ways for a dominant firm to abuse its market power….Article 102 may be applied even in the absence of a direct effect on competition between undertakings on any given market” (Deutsche Post-Interception of Cross-Border Mail, 2002).

In this situation, the discriminatory conduct may impair the ability of firms in the different markets to compete for important inputs. They are not competing for the business but competing for the
inputs to produce outputs at the lowest cost possible. If the discriminatory behaviour impairs the ability of a firm or firms to get the supply that they want and prevents them from operating as efficiently as possible, the firms will eventually leave the market. Under this new abusive category, it is clear that competition is harmed in one way or another. However, the main issue here is whether harm to competition under the third category includes harm to consumer. Discriminatory practice may not necessarily increase price and may be in certain circumstances welfare enhancing.

CONCLUSION
From the study, it can be concluded that ‘harm to competition’ generally means harm to competitive process. The consumer harm test may play an important role in competition law assessment to determine whether a particular conduct is anti-competitive. In exclusionary abuse, for example, taking into consideration consumer harm may safeguard the risk of false conviction and over-deterrence (Nazzini, 2015). However, proving actual consumer harm is a demanding task and could hamper the effectiveness of competition law enforcement. Perhaps, what the Competition Commission needs to prove is the potential rather than the actual effect of certain anti-competitive conduct on consumers. For example, consumer harm may be implied from the fact that the exclusion of equally efficient competitors may lessen competition and further strengthen a firm’s dominant position in the market. This in the end may create a harmful effect on not only the competitive process but also consumers in the long run in the form of high price and output reduction.

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