TREATMENT OF

MICRO, SMALL AND MEDIUM ENTERPRISES (MSMEs)

UNDER COMPETITION ACT, 2002

Presentation to:

Associations of MSMEs

By

AUGUSTINE PETER

Economic Adviser

Competition Commission of India

Tel: 011 26701681: Fax: 011 26107131:

email paugustine@nic.in

www.cci.gov.in

India International Centre, Annex.

27-11-2008

WHAT COMPETITION LAW MEANS TO MSMEs

" Competition law is a kind of a Constitution of market economy, which protects SMEs and their operating conditions from the abuse of market power "

Mr. Mauri Pekkarinen, Minister of Trade and Industry, Finland

WHAT COMPETITION LAW MEANS TO SMEs

- Korean Fair Trade Commission (KFTC): Competition regulation aims at:

  " creating a foundation on which parties to transactions who have different economic power can compete freely and fairly on a level playing filed"

- Sec 1.1 of the Canada Competition Act provides that:

  " [the purpose of this Act is to maintain and encourage competition in Canada …in order to ensure that small and medium sized enterprise have an equitable opportunity to participate in the Canadian economy …."]

COMPETITON LAW

EVOLVING PHILOSOPHY:US

- Competition law was established in the US (1989)with a view to protecting the interests of small producers and farmers Even before that in the various States of the US anti-trust legislations were enacted with the same objective
- Even as late as in 1960s and 70s the US courts favoured protection of smaller competitors , even at the expense of efficiency losses (e.g. Brown Shoe Co. v United States)
- This changed in 1980s, influenced by the Chicago School, with economic efficiency becoming the prime goal of anti-trust policy, with a view to enforcing consumer welfare

COMPETITON LAW
EVOLVING PHILOSOPHY:US

- The philosophy that emerged was that competition law should intervene only when conduct by enterprises produce ‘inefficient outcomes’
- Social political considerations became irrelevant
- This also made that dominant firm exclusionary strategies would not be objectionable, in case efficiency enhancement is involved
- Productive efficiency became the overriding concern of anti-trust

TPA AND SMALL BUSINESS

THE CASE OF AUSTRALIA

- The ACCC, Australia, has long recognized that small business doesn't have the same sort of resources as big business to address education and compliance
- For some time now there is a dedicated small business unit within the ACCC to focus on the sector.
- However, ACCC believes that it is not the role of competition policy to favour one sector over another – **competition policy** is not about preserving competitors, it **is about promoting competition.**

TPA AND SMALL BUSINESS

THE CASE OF AUSTRALIA

- This was perhaps best put in the final report of the Senate Committee considering the effectiveness of the Trade Practices Act (TPA) in relation to small business, which noted
- *"…the Committee recognizes that there is a significant difference between protecting competitors, and protecting particular competitors. The entry and exit of competitors from the market is a normal part of vigorous competition. Market efficiency is often enhanced by driving inefficient competitors from the market. To summarize the Committee's views on this issue, the purpose of the Act is to protect competition. This can best be achieved by maintaining a range of competitors, who should rise and fall in accordance with the results of competitive rather than anticompetitive conduct.* ***This means that the Act should protect businesses (large or small) against anticompetitive conduct, and it should not be amended to protect competitors against competitive conduct."*** ***[1]***

[1] Senate Economics References Committee "*The effectiveness of the Trade Practices Act 1974 in protecting small business"* page xi, para E.3

DEFINITION OF (M)SMEs

Source	Definition
World Bank since 1976	Firms with fixed assets (excluding land) less than US$ 250,000 in value is a small scale enterprise
Grindle et al (1989:90)	Small-scale enterprises are firms with less than or equal to 25 permanent members and with fixed assets (excluding land) worth up to US$ 50,000.
USAID in the 1990s	Firms with less than 50 employees and at least half the Output is sold (also refer to Mead, 1994).
UNIDO's Definition for Developing Countries:	**Large** - firms with 100+ workers **Medium** - firms with 20 – 99 workers **Small** - " " 5 – 19 workers **Micro** - " " < 5 workers
UNIDO's Definition for Industrialized Countries:	**Large** - firms with 500+ workers **Medium** - firms with 100 – 499 workers **Small** - " " ≤ 99 workers

DEFINITION OF (M)SMEs
ABSOLUTE VS RELATIVE

- Absolute definition Vs relative definition of MSMEs
- In the context of competition law, the concepts of 'relevant market' (Geographic and Product) and the 'effects' based approach to analysis of harm leads to recognition of relative definition of MSMEs
- An enterprise is small or big is determined in relation to the rest of the players in the same relevant market
- Competition Act, 2002 specifies the factors to be taken into by the Commission before determining the dominant nature of any enterprise

RATIONALE FOR
SPECIAL TREATMENT OF MSMEs
UNDER COMPETITION LAW

- MSMEs make a major contribution to GDP, exports, etc.
- Serves employment objective
- Higher degree of creativity, innovation etc.
- Their disadvantage *vis-à-vis* large enterprises, due to their:
  - inability to access the capital market
  - vulnerability to cyclical and structural fluctuations
  - inability to compete with larger rival for procurement of raw materials and human resources
  - Inability to benefit from 'economies of scale'

ADVANTAGES OF BEING MSME

- More flexible
- Able to adjust to the needs of specific customers

EXPLICIT EXEMPTIONS FOR MSMEs
UNDER CERTAIN JURISDICTIONS

- Competition laws of:
  - Germany
  - Japan
  - South Africa …

  includes explicit references to SMEs

EXEMPTIONS
GERMANY

- Cooperation among SMEs enjoy special treatment under German Competition Law
- However, relative concept of SME: Not based on absolute size (asset, turn over, number of employees etc)
- Not applicable to (horizontal) agreements with EU relevance (sec. 3 ARC)
- Should be aimed at rationalization of commercial transactions by inter- enterprise/company co-operation
- Competition should not be adversely affected by the cooperation

EXEMPTIONS
GERMANY

- Cooperation should improve competitiveness of the cooperating (M)SMEs (e.g. extension of production, improvement in quality diversification of production range, rationalization of distribution or purchase or a joint advertising measure
- In exceptional case cooperation of (M)SMEs with large enterprises may also considered for exemption provided it is essential to bring about competitiveness of the (MSMEs) SMEs

EXEMPTIONS
GERMANY

- Right to ‘no action’ decision
  - In respect of cases as indicated above, parties have a ‘right to’ a so called ‘no-action’ provided:
    - No practice or experience for such a cooperation exist at the cartel authority
    - The cooperation sets a precedent for many other cases
    - Considerable investments are to be made in connection with the agreement

EXEMPTIONS
GERMANY

- No action decision exemption expires on 30 June 2009
- After this date SMEs will not have the right to claim a no-action letter but will be subject to the same rules with regard to ‘no-action’ letters as other companies

EXEMPTIONS

GERMANY

German Federal Cartel Office

- *De minimis* Notice (No. 18/2007) related to 'agreements of minor importance'
- Special provisions related to cooperation between (M)SMEs

- New Notice makes a distinction between
  - Agreements between competitors (horizontal) *and*
  - Agreements between enterprises operating at different levels (vertical)

EXEMPTIONS
GERMANY

I. *Market share thresholds* for agreements of minor importance
   - Horizontal agreements of minor importance (if market share of parties less than 10 per cent of the relevant market) will not be acted against
   - Vertical agreements to be treated as of minor importance if they have a joint market share of 15 per cent of relevant market
   - When there is doubt as to if the agreement is horizontal or vertical the *de minimis* limit will be 10 per cent

EXEMPTIONS

GERMANY

- When there is suspicion of cumulative market foreclosure, a lower *de minimis* threshold of 5 per cent will be applicable

(Such cumulative foreclosure is assumed in case 30 per cent or more of the affected market is covered by parallel networks of agreements entered into by suppliers or dealers, where those agreements have a similar effect on the market)

EXEMPTIONS
GERMANY

- ***De minimis exemption is not applicable to hard core cartels (price fixing, market allocation, quantity / supply limiting or bid rigging)***
- ***De minims* exception is only discretionary rule and there is no absolute legal guarantee.**
- **However, the Federal Cartel Office may not decide not to initiate administrative immediately, but may give time for the parties to abandon the practices objected to**

EXEMPTIONS

SOUTH AFRICA

- **The South African Competition Act 89 of 1998 became operative in September, 1999.**
- Its prime objective is:

  To maximize consumer welfare by efficiently allocating resources
- **It has also social objectives as follows:**

(i) "to ensure that small and medium-sized enterprises have an equitable opportunity to participate in the economy; *and*

(ii) " to promote a greater spread of ownership, in particular to increase the ownership stakes of historically disadvantaged persons"

Of these:

(i) Above, is designed to cater to black economic empowerment companies; and

(ii) Above, is designed to cater to (M)SMEs

EXEMPTIONS
SOUTH AFRICA

Experience shows that in SA success rate has been high for SMEs in their competition complaints in respect of *per se* prohibited cases and abuse of dominance, viz.

- *Per se* prohibited practices:
  - Price fixing, market sharing, resale price maintenance
  - Because in these cases the Act does not require the complainant to actually prove a substantial prevention or lessening of competition in a market
- *Abuse of dominance*
  - Because the relevant provisions outlaw exclusionary practices which are most likely to be perpetrated against SMEs, who are already in the market or who are trying entry

NATIONWIDE V SASOL OIL (PTY) LTD, SA

DAVID VS GOLIATH

- The complainant, a small vineyard pole producer in the Eastern Cape, charged Sasol Oil, its main supplier of a vital chemical-treatment input in the pole manufacturing process, with discriminating against it in favour of larger customers in terms of price.
  - The Complainant was a sole proprietor
  - Pitted against an army of Sasol lawyers

  Making it a ‘David v Goliath’ case

NATIONWIDE V SASOL OIL (PTY) LTD, SA

DAVID VS GOLIATH

- Sasol was giving its larger customers lower price in the form of discounts based on volume of chemical they purchased
- Nationwide poles charged that Sasol was charging it more for the chemical input than it was charging other larger competitors without any economic justification for this discrepancy
- **This made the complainant's input cost much higher than its larger rivals**

NATIONWIDE V SASOL OIL (PTY) LTD, SA

DAVID VS GOLIATH

- **This made it difficult for it to compete equitably by selling on its own treated poles to its downstream competitors**
- The SA Competition Tribunal upheld the charges raised by the complainant and held that:
  - the purpose of sec 9, the Act's provision prohibiting price discrimination, was to express the legislatures' desire to maintain accessible, comparatively structured markets, markets which accommodate new entrants and which enable them to compete effectively against larger and well established incumbents

NATIONWIDE V SASOL OIL (PTY) LTD, SA

DAVID VS GOLIATH

- The difficulty of small business proving anti-competitive effect was acknowledged by the SA Competition Tribunal in the Nationwide Poles, when it remarked:

  " ….. on a consumer welfare test small business will always fall precisely because it is not able to correlate harm that is inflicted upon it to harm that is inflicted on the broader market. A small firm will always be met with the response that its trouble are, in relation to the market as a whole, *de minimis*, that is, that they have little, if any, effect on competition in the market as a whole"

NATIONWIDE V SASOL OIL (PTY) LTD, SA

DAVID VS GOLIATH

- The SME-friendly policy aspirations ventilated in the Nationwide Poles case allowed the Competition Tribunal to apply a lower threshold test for interpreting "likely to substantially prevent or lessen competition" in evaluating this concept in its decision.
- It acknowledged that since the legislature could not have intended small firms to be non-suited in proving anti-competitive effect under section 9, all that the complainant had to prove was competitive relevance. In other words, it had to establish that the complainant was relevant to competition, as opposed to a mere narrow claim to protect its own commercial interests (Nationwide Poles and Sasol Oil (Pty) Ltd 72/CR/Dec03 at para 103)

COMPETITION ACT, 2002

TREATMENT OF MSMEs UNDER COMPETITION ACT, 2002

- Competition Act, 2002 does not look at the size of the enterprise as such, whether in terms of capital or turnover or number of employees
- Absolute size is not relevant. Relative size is what matters
- It looks at the effects of 'acts' by enterprises, irrespective of their size, defined in whatever manner
- 'Effects' in the 'Relevant Market' is the concern
- Effects have to be 'adverse' and 'appreciably so', to be caught under the provisions of Competition Act, 2002

TREATMENT OF MSMEs UNDER COMPETITION ACT, 2002

- While there is no specific provision explicitly referring to MSMEs in the Act, there are a number of provisions indicating social and developmental objectives as follows:

(i) The preamble indicates that "it is an Act to provide, keeping in view the economic development of the country……."

(ii) It is an Act aimed at establishing a Commission

" to ensure freedom of trade carried on by other participants in market, in India, and for matters connected therewith or incidental thereto"

COMPETITION LAW PROVISIONS AIDING MSMEs

MERGERS

- Merger regulation under CA, 2002 ensures conducive operating conditions for SMEs
  - By regulating mergers that would create or strengthen market power
  - By excluding SMEs from regulation through high thresholds. Indian thresholds are, perhaps, the highest in the world

COMPETITION LAW PROVISIONS AIDING MSMEs

ANTI-COMPETITIVE AGREEMENTS

- Though four types of horizontal agreements viz. the price fixing, market sharing, quantity/supply limiting, bid rigging, collusive bidding are specifically identified for mention in the Act (sec 3) they are not *per se* prohibited
- There is only presumption of anti-competitiveness in their cases. It is for the accused party to rebut such a presumption
- Agreement among MSMEs will have a good chance of rebutting the presumption
- Other horizontal agreements and vertical agreements are governed by *Rule of Reason*

COMPETITION LAW PROVISIONS AIDING MSMEs

ANTI-COMPETITIVE AGREEMENTS

- The Act may be seen to specify three factors explicitly as relevant for rebuttal of presumption viz.:
  - Accrual of benefits to consumers
  - Improvements in production or distribution of goods or provisions of services
  - Promotion of technical, scientific and economic development by means of production or distribution of goods or provisions of services

COMPETITION LAW PROVISIONS AIDING MSMEs

ANTI-COMPETITIVE AGREEMENTS

- The developmental objectives embodied in the Act, if obtained by any of the four types of agreements governed by presumption, it appears possible that Commission would give due weightage to them
- Besides, efficiency enhancing joint ventures are exempt from the presumption rule, irrespective of the category of enterprise
- The duties of the Commission (Section 18) include "ensure freedom of trade carried on by other participants, in markets in India"

COMPETITION LAW PROVISIONS AIDING MSMEs

ABUSE OF DOMINANCE

- While inquiring whether an enterprise enjoys a dominant position or not, under Section 4, the Commission shall have due regard to all or any all the thirteen factors specified in Section 19 (4).
- These factors include the following:
  - Market share of enterprise;
  - Size and resources of enterprise;
  - Size and importance of competitors;
  - Economic power of enterprise including commercial advantage over competitors;

Contd.,

COMPETITION LAW PROVISIONS AIDING MSMEs

ABUSE OF DOMINANCE

- Entry barriers including barriers such as regulatory barriers, financial risks, high capital cost of entry, marketing entry barriers, technical entry barriers, economies of scale, high cost of substitutable goods or services for consumers;
- Market structure and size of market;
- Relative advantage by way of contribution to economic development, by the enterprise enjoying a dominant position having or likely to have an appreciable adverse effect on competition;
- Any other factor which the Commission may consider relevant for the inquiry.

COMPETITION LAW PROVISIONS AIDING MSMEs

ABUSE OF DOMINANCE

- Certain types of abuses by dominant enterprises are treated as *per se* anti-competitive by the Competition Act, 2002
- The requirements are only two:
  - To prove dominance
  - To prove the specified conduct by such dominant enterprise

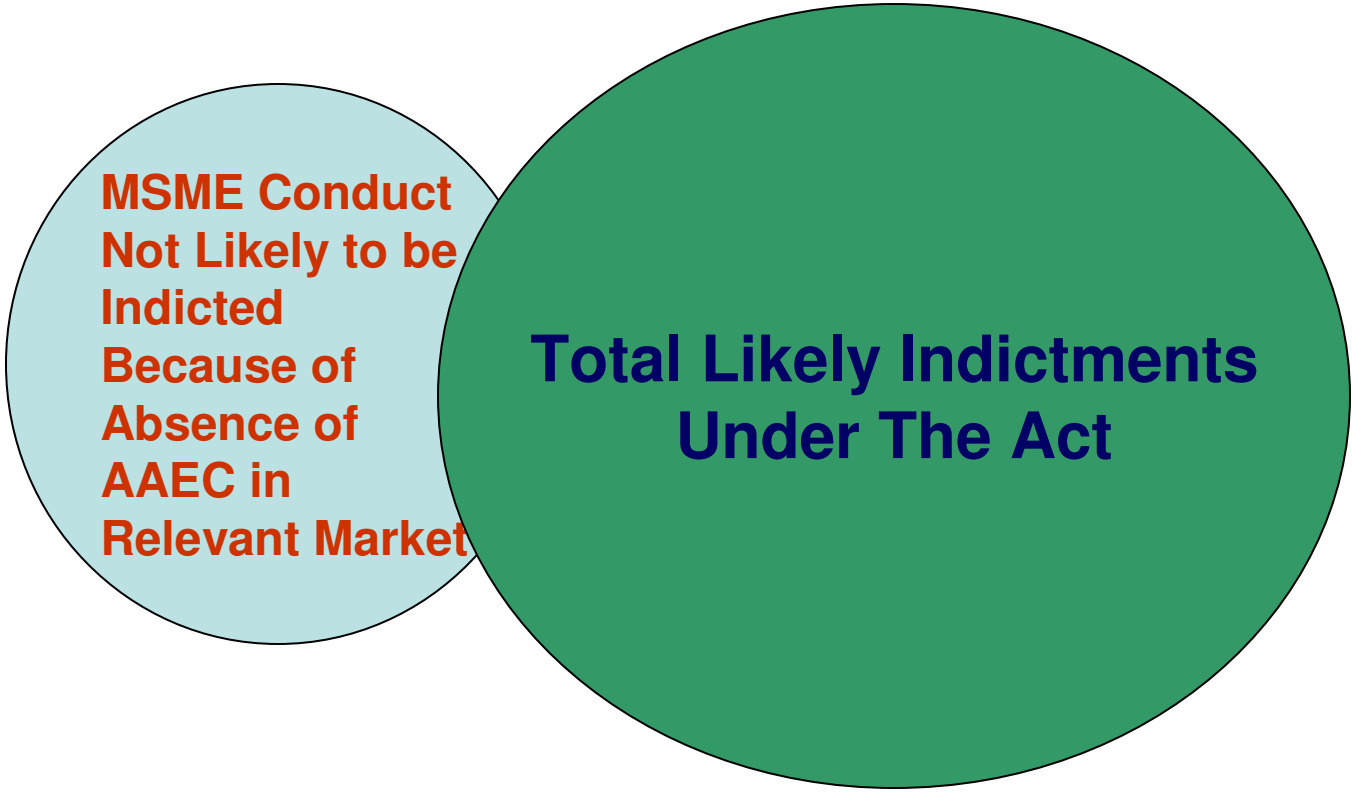
COMPETITION LAW PROVISIONS AIDING MSMEs

ABUSE OF DOMINANCE

Conduct by dominant enterprises, prohibited *per se*

- Imposing unfair or discriminatory price or condition in purchase or sale, including predatory pricing
- Limits or restricts production of goods or provision of services or market therefor
- Limiting scientific development to the prejudice of consumers
- Denial of market access in any manner
- Conclusion of contract subject to supplementary obligations
- Use of position in one relevant market to enter into or protect other relevant market

TREATMENT OF MSMEs UNDER COMPETITON ACT, 2002



APPEARANCE BEFORE COMMISSION

- Accessibility to legal assistance is normally difficult for MSMEs
- However, Competition Act, 2002 (Section 35) envisages that a person or an enterprise may either appear in person or authorize one or more Chartered Accountants or Company Secretaries or Cost Accountants or Legal Practitioners or any of his or its offices to present his or its case before the Commission

IN SUM …

- Presence of an enforceable competition law is in the interest of MSMEs
- Competition law recognizes only the relative definition of MSMEs and not the absolute definition
- Indian law does not have specific provisions on MSMEs
- However, development related provisions in the preamble and the Act may be relied on to give special consideration to issues involving MSMEs
- MSMEs may stand largely protected from accusation of violation of competition rules, because of the concept 'appreciable adverse effect on competition': However, there is need to see how the jurisprudence evolves
- On the other hand the concept of 'relevant market' poses a question mark !

IN SUM …

- MSMEs can relatively easily challenge Abuse of Dominance cases, given the factors for identification of 'dominant enterprises', in the Act
- Merger between MSMEs stand excluded from Merger regulation because of the high thresholds
- MSMEs can make successful case against mergers and get 'remedies' built in, to protect their interests
- There may be need for more specifically defining 'appreciable adverse effect' on competition as the Commission proceeds with enforcement in the coming days

==

THANK YOU

==