



Corporate Governance, Ownership Structure and Expropriation of Rights: Case of Malaysian Small and Medium Enterprises

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ABSTRACT

Small and medium enterprises (SMEs) serve as the financial backbone of the developed and developing economies, and a major contributor in many countries' gross domestic product. A sustainable SME sector is vital for a developing country like Malaysia where SMEs represent 99.2% of the overall business establishment and a major employment sector in the country. Although, the Malaysian SME sector faces a critical problem, which results in 50% of SMEs collapse during the first 5 years of operation and a 60% rate of failure among SMEs. In addition, unauthorized use of company property, misappropriating company funds, making false statements, illegal investment schemes and many other allegations have been put on the Malaysian SME owners and directors in the past. The objective of this paper is to investigate the Malaysian SMEs structure, past allegations and the corporate governance (CG) practices in the medium sized manufacturing SMEs. This study has adopted a qualitative approach, face-to-face interviews were conducted with SME owners/directors, and regulatory body officials. The results show that the Malaysian SMEs are mainly family based and higher management positions are kept by the family. Furthermore, it was revealed that there is no CG code for the SMEs. This provides room for the family to expropriate minority shareholders' rights and perform illegal activities. Hence, the results stressed on the need of the implementation of CG code for Malaysian SMEs.

Keywords: Corporate Governance, Ownership Structure, Family Ownership, Foreign Ownership, Expropriation of Rights

JEL Classification: L25, L26, L60, M10, Y2

1. INTRODUCTION

Since the past, issues of minority shareholders' rights in small and medium enterprises (SMEs) have become a major concern for researchers, regulatory bodies, policymakers and practitioners (Agyemang et al., 2015; Agyemang and Castellini, 2013b; Okpara, 2010). This is because of the inequality in the decision making process, where minority shareholders can talk, criticize or try to raise their voices in general meetings, but they do not have influence on any part of the decision making (Agyemang et al., 2015; Cory, 2005; Berglof and Claessens, 2004). Minority shareholders are invited to attend general meetings; however, the majority shareholders influence most of the meetings. Such block holders have the greater decision-making power and influence the board and management of the firm (Agyemang et al., 2015; Bohrer, 2007; Cory, 2005; Roe, 2003; Hirshey, 2003).

By having less equity share in the firm, minority shareholders seem powerless in the selection of board members and fail to influence the corporate decisions, which need shareholders' approval (Bohrer, 2007; Denis and McConnell, 2003). Some shareholders take advantage of their ownership capability to contradict with their counterparts from the management. Majority shareholders mostly influence the selection process of choosing the board chairperson, chief executive and other board and management people in the organization (Herman, 1981). Therefore, if certain equity holders have the influence over the selection of the board, management and other key people of the organization, then there is little or no doubt that they can use control on both the board and management (Agyemang et al., 2015; Agyemang and Castellini, 2013a; Berglof and Claessens, 2004; Carlsson, 2003).

In most countries, within a weak legal system, owners of the firms can take resources out of the firm for their own benefit.

They simply expropriate the rights of the minority shareholders (Johnson et al., 2000; Glaeser et al., 2001). Therefore, most of the majority shareholders, who are involved in the expropriation of the shareholders' rights, belong to the owner's family. Several evidences and studies on minority shareholders' rights were conducted on the developed economies (Bohrer, 2007; Cory, 2005; Holmen and Knopf, 2004; Volpin, 2002; Ehrhardt and Nowak, 2001), however, scarce literature is available on developing countries (McGee, 2009; Berglof and Claessens, 2004). Therefore, this paper examines this issue by analyzing the ownership and board of directors (BoDs) structure and their practices within Malaysian SMEs. Particularly, this paper covers the following four-fold objectives:

1. Examine the ownership and BoDs structure in Malaysian medium sized SMEs
2. Investigate the expropriation of minority shareholders' rights
3. Investigate the past allegations of fraudulent activities
4. Find out the need for a corporate governance (CG) code for the Malaysian SMEs.

2. LITERATURE REVIEW

2.1. Malaysian SMEs

SMEs are major contributors to the Malaysian economy. They represent 65% of the total employment in the labor market and 99.2% of the overall business establishments in Malaysia (Bank Negara Malaysia, 2006). Malaysian SMEs contribute 32% of the gross domestic product (GDP) and 19% of the total export value of the SMEs' (National SME Development Council, 2006). Compared with other Asian countries, the total export value of Malaysian SMEs is below the average line, which is 19% (Ndubisi, 2008). The Malaysian government has taken several initiatives, such as; ICT growth for SMEs knowledge-based development and the ninth Malaysia plan, effective from 2006 to 2010, to promote SMEs in the country to achieve a high contribution from SMEs in the economy. It is to encourage and empower the growth and establishment of the SMEs in the country (Rachagan and Satkunasingam, 2009). It has been discussed since decades that SMEs are the major components in the economic growth of any country. Similarly, SMEs are the major source of employment in many developed and emerging markets. So far, in Malaysia, SMEs are the major contributors in the overall employment sector by contributing 57.4% in 2012. Compared with the previous year, the rate of employment increased significantly to 6.5% in 2012. It shows that every year the numbers of employees are increasing in the SME sector (SME Corporation Malaysia, 2012-13). SMEs have a major contribution in the overall employment compared to the large sized firms (Table 1).

Most of the Malaysian SMEs are family owned, 72% family owned firms exist in Malaysia and this is the situation in many

developing countries. Moreover, 60% of the SMEs are family concentrated and such SMEs do not practice CG (Himmelberg et al., 2004). In such kinds of firms, families have control over the management of the firm (Claessens et al., 1999; Claessens et al., 2002; Khatri et al., 2002). According to Ibrahim and Samad (2011), family concentration in Malaysian firms increased from 57.7% to 67.2% and the cut off level for voting has increased from 10% to 20%. They further expressed that, the Malaysian SMEs structure reflects concentrated ownership and has high agency cost due to the fraudulent behavior of the majority shareholders.

2.2. CG Issues on Malaysian SMEs

CG failure within the SMEs is a big threat to the Malaysian economy, as SMEs are the major contributors to the country's GDP (Bank Negara Malaysia, 2006; National SME Development Council, 2006), and the major employment sector of the country (SME Corporation Malaysia, 2012-13). Malaysian SMEs are the model of family concentrated ownership (Claessens et al., 2000), and where ownership become more concentrated, chances for the protection of the minority shareholders rights will be low (Silva and Majluf, 2008). In such type of firms, the family has the power of decision-making, their relatives and close friends are being hired as the members of the BoDs. Similarly, top management positions are kept within the family (Rachagan and Satkunasingam, 2009) and such firms do not have good CG practices (Himmelberg et al., 2004). Lack of competencies in the business owners and lack of skills and expertise among the people holding management position have caused the failure of most SMEs (Silva and Majluf, 2008).

Most of the SMEs failed to follow the CG reforms from the Companies Commission of Malaysia (CCM), and it has caused many fraudulent activities, such as providing fake financial and annual reports, and illegal investment schemes, which lead to high monetary loss of the outside investors (Longenecker et al., 1999). Good CG practices lead firms to good corporate performance. The failure of many SMEs is the result of poor CG practice (Wahab et al., 2007). The problems discussed above have an adverse effect on CG practices on the SMEs. Due to such problems, most of the SMEs fail, and in Malaysia the estimated failure rate was 60% (Chong, 2012; Ahmad and Seet, 2009; Portal Komuniti KTAK, 2006; Qureshi et al., 2015).

Good CG practices lead firms toward good corporate performance. Malaysia has a CG code; the Malaysian Code of CG (MCCG), but it was implemented to the public listed companies. Similarly, the CCM is working hard to meet the good CG practices for the SMEs in the country. The CCM is an agency that incorporates companies, registers businesses and provides business information to the public. The Companies Act 1965 says that every company registered under CCM needs to abide by the CG practices (Companies Commission of Malaysia, 2012).

Table 1: SMEs, large firms and total employment (2009-2012)

Employment Sector	2009	2010	2011	2012	% share 2012
SME employment	4,100,952	4,389,823	4,562,815	4,854,142	57.4
Employment in large firms	2,800,097	3,294,714	3,403,549	3,606,829	42.6
Total employment	6,901,049	7,684,537	7,966,364	8,460,971	100

Source: Department of Statistics, Malaysia. SME: Small and medium enterprises

The CG mechanism can be divided into two major mechanisms: Internal and external control. The main external control mechanisms are the market for corporate control, managerial labor markets and concentrated shareholding by block-holders. On the other hand, there are two essential internal CG mechanisms: The director's shareholding and BoDs. Due to weak market control, the internal corporate control mechanism plays a vital role in the emerging economies (Ahmad and Seet, 2009).

The Asian Financial Crises of 1997 put their marks on Malaysian firms as well, and it revealed the poor CG practices in the country (Wahab et al., 2007). Most of the companies suffered from over leveraging, allegations of cronyism and poor legal protection for investors against expropriation due to corporate insiders (Claessens et al., 1999). These issues became worse due to the lack of corporate take-overs in Malaysia and politically connected firms in the country (Ahmad and Seet, 2009; Faccio and Lang, 2002).

An internal CG mechanism is essential for successful CG. Most of the Malaysian SMEs have failed to follow the CG rules. Due to this imbalance, many SMEs are involved in various fraudulent activities, such as lodging of false and misleading particulars, illegal deposit taking, and illegal investment schemes. The illegal investment schemes have affected many investors and involved huge amounts of money. According to the CCM, all companies registered under the CCM are required to submit their annual reports, annual returns and tabling accounts as well as conduct annual general meetings. In spite of that, most of the SMEs have failed to follow these guidelines, and it was found that SMEs in Malaysia tend to submit misleading statements (CCM, 2012). Most of these issues occur due to the concentrated ownership (Claessens et al., 2000). The company owners, directors and secretaries were found involved in various fraudulent activities. For instance, the CCM published few fraudulent cases with offenders' names, penalized amount and imprisonment time. Most of the directors and secretaries were found guilty in the unauthorized use of company property, making false statements to the CCM, gaining benefits for themselves, offering illegal

investment and withdrawing company's funds without approval (Table 2).

Malaysian SMEs are family concentrated companies, where most of the SMEs are run by families with concentrated ownership (Claessens et al., 2000). Most of these companies are inherited by their own children. Numerous studies were conducted on the majority shareholders and expropriations of minority shareholders' rights in Malaysia (Himmelberg et al., 2004; Ahmad and Seet, 2009; Abidin et al., 2009; Chong, 2012). Nevertheless, Malaysia is a different case with respect to agency problem; here, agency problem occurs between the majority and minority shareholders. Indeed, Lai (2004), mentioned that the agency problem in Malaysian firms arise between the majority and minority shareholders. In such case, the majority shareholders have the power of control over the minority shareholders (Claessens et al., 2002; Morck et al., 1998).

2.3. Ownership Concentration

Ownership concentration is one of the important mechanisms of CG that influences the agency costs (Jensen and Meckling, 1976). The effect of ownership concentration and firm performance has been discussed thoroughly in literature, particularly, focused on the companies in the United Kingdom, United States and other developed countries. Literature suggests both, positive and negative relationships between ownership and corporate performance. For instance, Shleifer and Vishny (1986) discussed the positive and important role of the majority shareholders for the firm's success, and the share prices increase when the percentage of shares held by them increase. Grossman and Hart (1986) describe that the majority shareholders play important role to foster their business; they play active roles in decision making by using their monitoring job.

On the other hand, ownership concentration can cause conflicts between majority and minority shareholders; thus, it leads to poor firm performance (Pinto and Augusto, 2014). The divergence encourages obstructive problems where the controlling

Table 2: List of penalties, offences charged by the CCM to different stakeholders

Offence	Penalty/imprisonment	Legal act	Date
Unauthorized use of company property	5 years imprisonment or RM 30,000 fine	Companies act: 1965	27-09-2013
Non-compliance offences	S.143 (1) – Fined RM 500 in default 7 days imprisonment S.165 (4) – Fined RM 300 in default 3 days imprisonment S.169 (1) – Fined RM 3,000 in default 2 weeks imprisonment	Companies act: 1965	26-09-2013
Making false statement to registrar	8 months imprisonment and RM 40,000 fine	Companies act: 1965	19-09-2013
Breach of fiduciary duties	5 years imprisonment or RM 30,000 fine	Companies act: 1965	04-09-2013
Misappropriating company's funds amounting to RM 149,000	5 years imprisonment or RM 30,000 fine	Companies act: 1965	28-08-2013
Failing to lodge annual return to the CCM	7 days imprisonment or RM 600 fine	Companies act: 1965	19-08-2013
Furnish false information in form C to CCM	2 years imprisonment or RM 50,000 fine	Business registration act: 1956	29-07-2013
Making false statement to the CCM	5 months imprisonment with RM 5,500 fine	Business registration act: 1956	16-07-2013
Offering illegal investment scheme to public	5 years imprisonment or RM 100,000 fine	Companies act: 1965	08-07-2013
Withdrawing company's funds without approval	5 years imprisonment or RM 30,000 fine	Companies act: 1965	26-06-2013
Authorizing to make a loan to his/her friend/family	RM 27,000 fine	Companies act: 1965	13-06-2013

Source: Companies Commission Malaysia, Press Releases (<https://www.ssm.com.my/en/press-public>). CCM: Companies Commission of Malaysia,

shareholders can take wealth from the minority shareholders for their personal benefits. Minority shareholders always fear for being expropriated through inefficient investment, which produce a higher cost for the company (Porta et al., 1999). Sheifer and Vishny (1997) claimed that, in some countries, agency cost is more affected by the conflicts between the controlling and minority shareholders rather than the separation of ownership and management.

Similarly, some other studies endorsed that, the majority shareholders can be disadvantageous to firm performance. In the case of majority shareholders, if they are more interested towards their own benefits, they can expropriate the value for their private benefits at the expense of the minority shareholders (Agyemang et al., 2015; Porta et al., 2000). Furthermore, there are chances of conflicts between the majority shareholders and minority shareholders, where the block-holders have voting rights whereas the minority shareholders do not have any and between the large equity holder and small equity holder who has little or no possibility to inspect or monitor the management (Melis, 2000). Another study, Konijn et al. (2001) on US firms found that, the ownership concentration has a negative effect on firm performance. Further, they stated that, there might be chances for private benefit of control, perhaps disadvantageous for minority shareholders.

2.4. Expropriation of Shareholders' Rights

Expropriation of the minority shareholders rights occurs when the majority shareholders take profit from the firms for themselves rather than to return it to the minority shareholders. It means that, the control shareholders can make private benefits at the other shareholders' expense. It consists of misappropriation, resisting potentially beneficial take-over offers, and the selling and buying of assets without shareholders' consent. Furthermore, related lending, diverting corporate opportunities from the company, hiring unqualified family members for managerial positions, rewarding themselves with undue pay without performance, taking managerial benefits such as spending profligately and using corporate jets (Wan-Hussain, 2005).

Mergers between affiliated companies that drain off resources out of the bidder or the target, ineffective cross subsidization of investment among divisions, excessive diversification, targeted share repurchases, and diluting share issues which discriminate against minority shareholders are some approaches of deceiving the shareholders (Wan-Hussain). There have been accusations that, in Malaysian firms, the majority shareholders enrich themselves at the shareholders' expenses through fake invoicing, forced bailout, and mutualizing proceeds from capital raising exercises (Rachagan and Satkunasingam, 2009).

The expropriation of shareholders' rights has been described as the misalignment of interests among shareholder groups or extensive ownership of cash flow rights. Expropriation leads to the majority management, isolation from external corporate control mechanisms, lavish salaries and dividends, or family members in the BoDs without required qualifications (Young, 2002). The likelihood for expropriation of shareholders' rights with the lower financial performance and inadequate investment opportunities in

the area restrict the investment and interest of foreign investors; this results in real low turnover on regional stock exchanges (Rachagan and Satkunasingam, 2009).

The reason for expropriation is that the family members are the majority shareholders of the firm and they can take resources out of the firm for their own benefits. As they have the power of being the majority shareholders in the firm (Shleifer and Vishny, 1997). Such kinds of expropriation reduce the market value of the firm (Dahya et al., 2008). Firms with majority shareholders involved in the expropriation of shareholders' rights do not perform proficiently. Past researchers have found a negative relationship between shareholders' expropriation and firm value (Dahya et al., 2008; Shleifer and Vishny, 1997; Porta et al., 1999; Morck et al., 1998; Lins, 2003; Qian et al., 2010).

An expropriation activity by family majority shareholders enhances their personal utility and foster poor firm performance (Anderson and Reeb, 2003). Poor firm performance can be seen as inferior returns, weak growth, and poor stock market valuations (Bennedsen et al., 2007; Cronqvist and Nilsson, 2003; Maury, 2006; Perez-Gonzalez, 2006).

According to Morck and Yeung (2003), in the emerging economies, most of the businesses belong to certain business groups and families. Generally, the majority shareholders control decision making in such firms, and they are liable for the consequences (Silva and Majluf, 2008). Whereas, the majority shareholders can enjoy the opportunity to expropriate the firm's resources for their own benefit. Thus, it will then affect the other shareholders (Shleifer and Vishny, 1997).

3. METHODOLOGY

This paper is exploratory in nature and the qualitative approach has been adopted for this paper (Silverman, 2008). For the greater understanding of the research area, the qualitative approach was chosen. This approach would help the researcher to explore new dimensions that were not expected by the researcher (Stebbins, 2001; Wolcott, 2009). Six face-to-face interviews were conducted with four regulatory body persons and two SME managers. Further subsections discuss the sample size, data collection, and methods of analysis.

3.1. Sample Size

The selection criteria for the sample were two-fold, all the interview partners needed to be an SME owner or director, and those from regulatory body. Where, the SME had to be a medium-sized manufacturing firm, and located in Malaysia. Whereas, for the regulatory body, interviewee had to be the head of his/her department, served in the same department for the past 2 years, and have an office in Malaysia. The selection criteria are discussed as below;

1. SME: The SMEs selected as respondents were based on the SME definition by SMECorp Malaysia. A manufacturing sector SME must have >75 and <200 employees, or annual sales turnover from 15 to 50 million.
2. Regulatory body: The regulatory body person had to be

the head of his/her department, and at have least 2-3 years' experience in the same department. The respondents must be aware of the Malaysian SME sector, its policies and programs.

3.2. Data Collection

For this study, data was collected from different sources including annual reports by regulatory bodies, past literature, official websites of regulatory bodies and interviews. The following sections further describe the data sources and data types:

1. Annual reports: Information was gathered from the annual reports of Malaysian regulatory bodies. This information provides insight of different dimensions of SMEs, such as the SME definition, number of SME establishments and SMEs' share in the employment sector.
2. Past literature: The past literature supported the identification of the ownership structure and CG issues of Malaysian SMEs.
3. Websites: Information about the expropriation and other fraudulent activities were gathered from the CCM's official website. Archival data gathered from the company website helped to support the interview responses.
4. Interviews: Based on the data collected from the annual reports and company websites. This study conducted six face-to-face semi-structured interviews. The interviews were conducted from high officials to acquire adequate information about the SMEs establishment, ownership structure, and expropriation of the shareholders' rights. Interviews were conducted between October and December 2013.

This research was carried out with semi-structured interviews to gain understanding of the interviewees by giving them the opportunity to respond freely within the predefined subject (Silverman, 2008). The interviews consisted of three sections: Ownership structure, BoDs, and expropriation of the shareholders' rights (Appendix A for interview protocol). The interviews were digitally recoded and transcribed accordingly.

3.3. Method of Analysis

The aim of the qualitative study is to understand the commonalities and differences between responses. Therefore, the thematic analysis approach was used to analyze the collected data (Stebbins, 2001; Wolcott, 2009). In the analyses process, the researcher followed a repetitive process in which patterns and themes were analyzed. This process was carried out simultaneously to achieve the greater objectivity.

4. RESULTS

In many emerging economies, the CG issues such as; CEO's duality, ownership concentration, shareholders' rights, board composition, independent non-executive directors and corporate disclosure in SMEs are the major problems. Similarly, Malaysian SMEs face similar problems. Interviews had been conducted to gather information regarding issues in the Malaysian SME sector. Thematic analysis allowed the researcher to explore and identify the critical issues among Malaysian SME sector. All of the interviews were labeled for proper identification. For example, RegB1, the abbreviation RegB represents the regulatory body, and 1 refers to the number of the order and SME1 represents

the SME while 1 refers to the number of the order (Tables 3 and 4). The research findings are structured as follows: First, the ownership structure of the SMEs. Subsequently, the board structure and selection of the board are discussed. Finally, the expropriation level and different ways of expropriation are presented.

4.1. Ownership Structure

The first aspect investigated was on the ownership structure of SMEs. Based on the interviews conducted, it can be seen that most of the Malaysian SMEs are solely family owned. Four respondents agreed that the decisions are made by the head of the family. Normally, the family head is the one who controls and makes all the firm's decisions by him/herself. The following quotes illustrate these points:

RegB1: "... in most of the SME here, majority firms are run by family members. Through generations they are doing this business. It is like one family member retired other take charge, all in the family [...]. Family head is the boss of the company. He/she can decide what is good for the company."

RegB2: "... not all, but majority of the SMEs registered under companies act 1965 are family oriented. [...] and it is difficult for us (as a regulatory body) to control such firms."

RegB3: "... Malaysian SMEs are pure reflection of family based business where family members are assigned all the management and other sort of jobs. [...] Mostly they are the bosses controlling their workforce [...]."

SME1: "... My grandfather started this business and this is our 3rd generation doing this (business) [...]. Yes, I think as a family we understand this business better and that's why we kept the management of our company within the family. I am the general manager here and doing good, making profit [...]. We have some non-family member also in the management [...]. No, they (board members) are not involved in the decision making. Because as a family we believe that we can do justice in making decisions, we know what is best for us (as a company) and how to make more money."

In summary, the findings indicated that most of the SMEs are family controlled. Family owners believe that, they can understand and make better decisions for their firms. In addition, the result shows that, most of the Malaysian SMEs are ownership concentrated.

Table 3: Respondents from SMEs

Company code	Industry	Number of employees	Position of interviewee	Market
SME1	Manufacturing	43	Owner-manager	Local
SME2	Manufacturing	78	Owner-manager	Local and export

Source: Author's analysis. SME: Small and medium enterprises

Table 4: Respondents from regulatory bodies

Company code	Office	Position of interviewee
RegB1	Regulatory body	Deputy director
RegB2	Regulatory body	Branch manager
RegB3	Regulatory body	Compliance manager
RegB4	Regulatory body	HR manager

Source: Author's analysis

Furthermore, the results also revealed that, family controlled firms are also difficult to manage by the regulatory bodies.

4.2. BoDs

The next aspect examines the SMEs' BoDs. Based on the interviews conducted, the findings indicated that family members have control over the BoDs. One respondent expressed that, in SMEs there is no formal board. Most of the decisions are made outside of the boardroom. Family members are also involved in decision-making and other sort of controlling activities. The following quote illustrates the point by one of the regulatory body:

RegB4: "... normally, in SMEs there is no formal concept of BoDs [...] yes there are board members but majority of the decisions are taken by the chairperson of the company or the family head [...]. Of course, head of the family decides what is better for the firm and sometimes his/her decisions go wrong.

In addition, another regulatory body describes the composition of the board as consisting of close relatives or family members. The respondents also expressed that, they received enormous complaints against the board and its functions. Therefore, it makes a board more sceptical, because it hinders the development of the SME itself, and it is not in the favor of their shareholders. An independent and autonomous board creates more opportunistic environment for all of its stakeholders. The following quote illustrates this point:

RegB1: "... not all, but most of the SMEs have their own people from family on the board [...]. They are also highly paid as compared to the market (salary compare to the non-family director). I think, somehow, this is not good. Because we receive many complaints from different shareholders regarding boards [...].

SME2: "... for the company registration requirement we must have at least two board members, so we have them [...] of course, they take most of the decisions for our firm [...] it depends, when the CEO feels, he can abandon the decisions made by the board."

In summary, the results show that, the family members mainly dominate the positions of the BoDs in SMEs. They appoint their family members and family friends to the board. This allows them to run the business under their own self-control. Similarly, it can be seen from the responses that the powerful person in the firm can overrule the board decisions; it can be either a major shareholder, the key person in the family or the CEO.

4.3. Expropriation of Shareholders Rights

The next aspect that was explored was on the expropriation of the shareholders' rights. Expropriation means when the majority shareholder or owner takes the profit for his/her own benefit, rather than pass it to the shareholders. Malaysian SMEs, as discussed, are ownership concentrated and chances for expropriation in such firms are high. The following quotes illustrate this point:

RegB1: "... we received a lot of complaints regarding company owners and directors that they have been involved in different sort of offences. Most commonly, we received complaints against owners using company's fund for their own good. Also many owners were found guilty in unauthorized

use of company assets and property [...]. As you know, Malaysian SMEs are family based and this has negative impression on outside investors. We also received complaints regarding illegal investment schemes. Where people lost huge amount in such false schemes [...]."

The above results revealed that the SME owners have been found guilty in different offences. It shows how ownership concentration affects investors' trust and ownership concentration allows owners to expropriate the shareholders' rights. Press releases were issued by the CCM, and mentioned the persons involved in different fraudulent activities. The press releases consisted of the company name, alleged persons' stake in the company, offence, court's ruling according to the Companies Act 1965 and the Business Registration Act 1956. Details of such offences are illustrated in Table 2. Due to ethical consideration, the accused persons' and companies' names are not provided in the list.

According to the press releases, most of the directors were involved in using the firms' money without the shareholders' consent and they were convicted for unauthorized use of company's property. Moreover, the directors were also found and charged for breaching fiduciary duties, making false statements to the registrar of the CCM, offering illegal investment schemes, failing to lodge annual return to the registrar of the CCM, approval of directors' friends/family for loans without approval from the board. In many cases, directors of different companies have been charged for having benefits for themselves. Most of the convicted directors were the majority shareholders in the business. In addition, a few business owners were also charged for lodging false reports to the CCM. Directors, business owners and others found guilty were charged against the Companies Act: 1956 and Business registration Act: 1965. They were penalized with huge fine and some of them were also sentenced to imprisonment for a certain time period. In some cases, both a fine and imprisonment were charged to the offender (Press Release 2013, CCM).

Furthermore, the CG code is a regulatory document, which helps to manage and direct firms, systematically. It was asked from the regulatory body regarding the CG code for Malaysian SMEs; they mentioned that there is no CG code available for SMEs. They also emphasized the need of the code for SMEs, as they think it is necessary to have a regulatory system for internal control for the SMEs. The following quotes illustrate the point:

RegB1: "... There is no CG code available for SME. [...] I think weak legal system enables SME to be unfair and unethical. [...] yes, they are found guilty (SME owners and directors) for misusing company funds and other resources."

RegB3: "... Malaysian SMEs need a comprehensive code of governance just like it is available for public listed firms [...]. Code of CG for public listed companies cannot be implemented on SMEs, as there is huge difference in managing and the way of doing business is different, SMEs are smaller in size compared to large public listed firms [...]. Malaysia has no CG code for SMEs."

REGB4: "... public listed companies are different from SMEs in many ways, just like the management, BoD, ownership and size of the business. [...] we can't directly replicate the

CG code to the SMEs; it won't fit at all [...] SMEs need a comprehensive governance code to avoid the irregularities in the business.”

In summary, the interviews revealed the need of a CG code for SMEs. However, due to the difference in management and business sizes among SMEs and large public listed companies, the MCCG cannot be replicated on SMEs. Thus, the findings indicate the need for further investigation on SMEs in terms of the CG practices and to propose a code, which can be implemented according to the SMEs' needs and dynamics.

5. SUMMARY AND DISCUSSION

As discussed in the literature review section, prior studies have mixed results; both positive and negative relationships with the ownership concentration with the expropriation and firm performance. However, most of the prior studies were focused on the developed countries. In this study, we have attempted to analyze the ownership structure of the Malaysian SMEs, and its impact of the ownership structure on the expropriation of the minority shareholders rights, past allegations and the CG practices in the medium-sized manufacturing SMEs.

The purpose of this study was four-fold: (1) Examine the ownership and BoDs structure in Malaysian medium sized SMEs, (2) investigate the expropriation of minority shareholders' rights, (3) investigate the past allegations of fraudulent activities and (4) find out the need for a CG code for the SMEs. Primary data was gathered through interviews with two SMEs, registered under the CCM and four regulatory bodies to provide a comprehensive insight into the subject matter. The secondary data was gathered from annual reports, past literature and the CCM's official website. Malaysian SMEs are family concentrated as illustrated in the results and also supported by past literature (Himmelberg et al., 2004). Majority shareholders/family owners have the incentive over management decisions and selection of the key persons in the firm.

The study revealed that the majority shareholders have influence over the business activities, and in certain situations, large equity holders can overrule the board decisions. Even though Malaysian SMEs have family members and close friends on the board (Rachagan and Satkunasingam, 2009), the CEO/family head or majority shareholder is more influential in the decision making process. According to the code of ethics by the CCM the BoDs cannot use the company property for their own benefits, and the BoD needs to disclose all contractual interests to the company. In contrast, the directors in Malaysian SMEs have been found guilty for using company property for their own benefits without the approval of other shareholders (Table 4). Such illegal activities reduce the firm value (Berglof and Claessens, 2004; Denis and McConnell, 2003) and allow the majority shareholders to expropriate the minority shareholders rights. Such types of SMEs are more inclined towards the family interests. It can be seen from the press releases of the CCM, the different illegal activities and the legal charges for such offences. Most of the firm owners and directors have been found guilty and charged for numerous illegal

offences, e.g., unauthorized use of company assets, offering illegal investment schemes, using profit for their own benefit, making false statements and many others discussed in the Table 4. A weak legal system and the absence of a CG code for SMEs allow owners to perform such illegal activities.

Ownership concentration and expropriation of shareholders' rights have an adverse effect on firm performance (Umrani et al., 2015; Agyemang et al., 2015; Chong, 2012; Wahab et al., 2007; Konijn et al., 2001; Porta et al., 2000). Past literature indicated the high failure rate among Malaysian SMEs and 50% of SMEs collapse during their first 5 years of operations (Chong, 2012; Khalique et al., 2011; Ahmad and Seet, 2009; Portal Komuniti KTAK, 2006). The results of this study revealed the ownership concentration and expropriation of minority shareholders rights by company owners and directors. Ownership concentration could be one of the reasons for this poor performance.

Furthermore, respondents expressed the need for a CG code for the Malaysian SMEs. In Malaysia, the code of CG has only been implemented on public listed companies. However, public listed companies and SMEs are different from each other in size, business, profit and management of the firm. The public listed companies are more managed and auditable as compared to SMEs. This is because of the mandatory requirements stated in the CG code. Hence, the results highlighted the problems faced by SMEs in the absence of a CG code, particularly for SMEs. Therefore, further research is required to explore the dynamics and categories to propose a CG code for SMEs.

Note: This paper is extended version of our conference paper “*Corporate Governance Practices and Problems Faced By SMEs in Malaysia*” published in *Global Business and Management Research: An International Journal*, Vol. 7, No. 2 (2015)

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APPENDIX A

Interview Protocol

Questions for SMEs

1. What is your position in this organization?
2. How many employees do you have in your organization?
3. What is the market for your finished good? (Local or International)
4. How is the decision making process of your organization?
5. Does your firm have the BoDs?
6. Who are the members of the board?
7. Does the Malaysian SMEs have CG code?

Questions for regulatory body personal

1. What is your position in this organization?
2. What is the Malaysian SME ownership structure?
3. How SMEs make their decisions?
4. Do the SMEs have BoDs?
5. Are the board members are active in decision making process?
6. Who are the members of the board?
7. Does the Malaysian SMEs have CG code?
8. Do you know about expropriation of rights?
9. Do you think the absence of CG code enables the expropriation of rights?