Ease carbon tax impact on SMEs

By KIRENNESH NAIR
kirennesh@thestar.com.my

MALAYSIA will introduce a carbon tax next year, targeting high-emission industries such as iron, steel and energy – a move that could ripple through the entire supply chain and affect small and medium enterprises (SMEs).

Without a domestic carbon tax, exporters of carbon-intensive goods still risk paying levies under the European Union's carbon border adjustment mechanism (CBAM), which takes effect next year.

CBAM applies to carbon-intensive imports, unless the exporter can prove that an equivalent carbon price has already been paid in the country of origin.

An industry observer says CBAM is essentially to ensure goods made outside Europe are not cheaper than those produced within the bloc once carbon costs are included.

He warns that SMEs have little choice but to adapt, especially if they are part of supply chains serving CBAM-compliant markets.

"Even if you're not the one exporting, Scope 3 emissions mean you're still counted as part of your customer's carbon footprint. Large companies – especially multinationals – will expect their suppliers to meet carbon standards. If SMEs can't do that, they risk losing business," he tells *StarBiz 7* on condition of anonymity.

SMEs remain the dominant "artery" of Malaysia's economy by almost every key metric – making up about 97% of businesses, providing nearly half of total employment and contributing more than one-third of the country's gross domestic product.

Carbon tax, already implemented in over 36 countries, including Singapore and Indonesia, charges for greenhouse gas emissions to curb fossil fuel use and speed up the shift to cleaner energy.

While the Malaysian government has said it will channel revenue from the tax into funding green technology and research and development, no details have been revealed on how SMEs – which typically lack the financial and technical resources to track, report and reduce emissions – will be supported.

Yan Meng: Most SMEs lack the tools to measure or reduce emissions

Sue Lyn: The shift to a low-carbon economy offers long-term gains

Sim: A robust legal framework and enforcement is crucial.

Baker: Over time it could help SMEs reduce operating costs.

Siew: The carbon tax could be a catalyst for innovation if right incentives are given.

Impact on SMEs

The Small and Medium Enterprises Association of Malaysia (Samenta) supports the country's sustainability goals but warns that carbon tax could strain small businesses already grappling with high energy costs, supply chain disruptions and compliance burdens.

"Introducing carbon tax at this juncture will further erode their already-thin margins, and if we are not careful, threaten their survival," its president Datuk William Ng Yan Meng says, adding that most SMEs lack the tools to measure or reduce emissions.

"Without addressing this readiness gap, a carbon tax will be seen as punitive rather than transformative."

Malaysia Carbon Market Association (MCMA) president Renard Siew Yung Jhien notes that while the tax targets large emitters, higher input and energy costs "are likely to be passed down the value chain," squeezing SMEs with limited capacity to absorb them.

PricewaterhouseCoopers (PwC) Malaysia director of sustainability and climate change Richard Baker agrees that most SMEs will feel the impact indirectly, especially through rising energy prices, but sees a longer-term upside as low-carbon technologies become more affordable and accessible as its adoption increases.

"Over time, this could help SMEs reduce operating costs, improve resilience and enhance competitiveness in a low-carbon economy," he notes.

Ways to go about

To avoid disproportionately impacting SMEs, the government should adopt a phased, consultative approach, says Samenta's Yan Meng.

He says this should include:

> capacity-building to educate and equip SMEs on carbon tracking and reduction;

> tax incentives or credits for green technology investment;

> exemptions or tiered thresholds for smaller emitters; and

> better access to financing for sustainability upgrades.

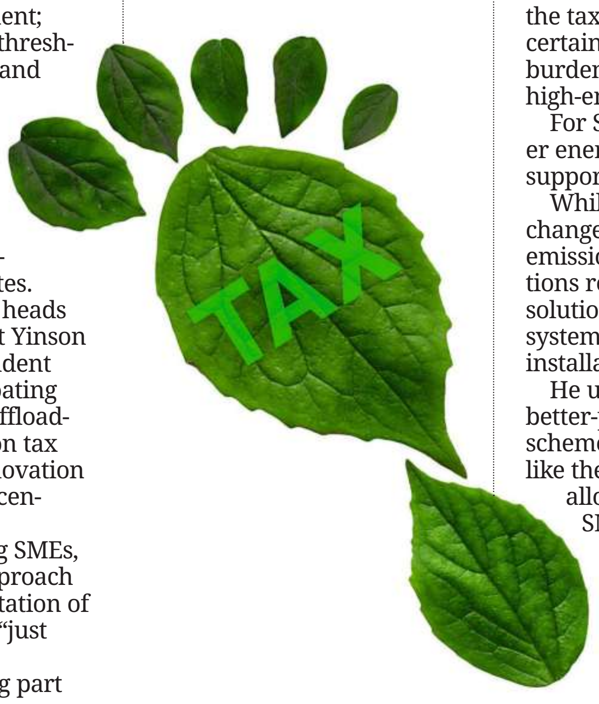
"Ideally, micro and small enterprises should be exempted, given the principle of proportionality and materiality," he notes.

MCMA's Siew, who also heads corporate sustainability at Yinson Holdings Bhd, an independent owner and operator of floating production, storage and offloading vessels, says the carbon tax could be a catalyst for innovation if paired with the right incentives.

To avoid overburdening SMEs, he says Malaysia must approach the design and implementation of the carbon tax through a "just transition" lens.

"This means ringfencing part of the revenue for targeted support measures such as energy efficiency grants, digital carbon tracking tools or capacity building programmes tailored for SMEs."

- SMEs have little choice but to adapt
- Calls for phased, fair carbon tax rollout
- SMEs seek exemptions and targeted support measures



"At its best, the carbon tax can be a lever not just for decarbonisation but also for industrial upgrading and inclusive economic growth but this requires careful policy calibration and strong institutional coordination."

KPMG Malaysia head of indirect tax Ng Sue Lynn says that while the tax will raise costs, the shift to a low-carbon economy offers long-term gains.

She says, for many SMEs, transitioning to alternative green energy solutions may incur significant upfront costs and to support this shift, "the government might consider offering targeted tax incentives and transitional assistance."

PwC's Baker cautions that SMEs already face economic pressures, including higher Sales and Service Tax, and need safeguards to avoid being overburdened.

One option, he says, is to apply the tax only to emitters above a certain threshold, ensuring the burden falls mainly on larger, high-emission companies.

For SMEs indirectly hit by higher energy costs, he says "targeted support is essential."

While small behavioural changes can help reduce carbon emissions, "substantial reductions require capital-intensive solutions like energy monitoring systems or renewable energy installations," he adds.

He urges more accessible and better-promoted financial schemes, building on initiatives like the green investment tax allowance (GITA), to empower SMEs to invest in low-carbon technologies.

GITA is a tax incentive that lets companies claim up to 100% of their investment in certified green technology – like solar panels or energy-efficient equipment – from taxable income.

"This dual strategy – protecting vulnerable businesses in the short term while enabling their participation in a low-carbon transition over the long term – supports both economic resilience and environmental responsibility."

Deloitte Malaysia country tax leader Sim Kwang Gek calls for a robust legal framework, enforcement, and enhanced green investment incentives, along with special environmental, social and governance (ESG)-related tax deductions for SMEs to encourage adoption of low-carbon solutions.

She suggests extending existing tax deductions on ESG reporting – currently capped at RM50,000 per year for listed companies and financial institutions – to SMEs, covering expenses such as emissions tracking, ESG verification and sustainability certifications.

She also points to Singapore's example, where businesses were given a three-to five-year roadmap to prepare for carbon tax.

"A planned approach starting with a low rate and a clear timeline would allow businesses to adapt," it said.

Lessons from Singapore

Singapore, which introduced South-East Asia's first carbon pricing scheme in 2019, targets facilities emitting 25,000 tonnes or more of CO^2-equivalent annually.

The city-state started with a rate of SG$5 per tonne before raising it to SG$25 this year.

The rate will climb to SG$45 by 2026 and up to SG$80 by 2030.

The tax covers about 80% of Singapore's national emissions, with no exemptions or free allowances, though from last year emitters may offset up to 5% of taxable emissions with approved international credits.

In Malaysia, BIMB Research estimates greenhouse gas emissions at 325.3 million tonnes in 2023, or nine tonnes per capita.

The power industry was the largest contributor, emitting 117.3 million tonnes (over 36% of the total), followed by transport (67.4 million), fuel exploitation (43.3 million), and industrial combustion (36.1 million).

BIMB Research estimates that the targeted industries – power, transport, fuel exploitation, industrial combustion and industrial processes – collectively emitted 288 million tonnes in 2023.

Adopting Singapore's initial S$5 per tonne rate (about RM17) the research house estimates the government could yield up to RM980mil in annual revenue.

With months before the planned rollout, Malaysia has a window to calibrate the carbon tax to achieve its environmental goals without undermining business competitiveness.

KPMG's Sue Lynn says the government should engage closely with industry players to co-develop a fair and effective framework – one that advances long-term environmental goals without compromising business competitiveness.

"From now on, businesses are encouraged to see this as the new way of doing business – and explore the long-term opportunities ahead, while keeping an eye on available government support," she adds.