

Competition Policy Review

**SUBMISSION by the OFFICE OF THE AUSTRALIAN SMALL BUSINESS
COMMISSIONER**

JUNE 2014

We are writing to provide some observations on small business aspects of the competition policy review.

Importance & challenges of competition

Sound competition policy is a key element of an open market economy; stimulating economic performance and offering consumers (including small business) a broader choice of products and services at more competitive prices. Ensuring a healthy competitive business environment is one of the key ways that government can encourage small business.

When it comes to setting competition policy, small business benefits from a level playing field on which to compete and a framework that is easily understood and provides certainty. The elements of clarity and certainty in this area are of extreme importance – the business environment is improved by ensuring that law, regulation and administration are simple to understand and easy to comply with. The business environment may be further improved by asking the question as to whether regulation is even necessary and, when it is, working with business to provide for appropriate outcomes.

While small business benefits from an open market economy, there are also a number of challenges when it comes to competing in the marketplace. This is often a product of economies of scale that provide larger businesses with a competitive advantage over smaller businesses. For example, larger businesses with higher volumes of credit card transactions are in a position to negotiate lower merchant fees. Higher usage rates also allow larger businesses to get better pricing on utilities.

Similar competition issues arise in the labour market where small business competes with other business for labour. Small business operators in regional Western Australia have spoken to us about how they struggle to compete with mining companies for workers and tradespeople due to the wages that large mining companies can offer. Similarly, the Tasmanian Small Business Council has advised that small businesses compete with wages offered by government agencies where 26% of family incomes in Tasmania are from government employment.

Power imbalance

Competition is key to the vast bulk of the interactions that we have with small business, although it is rarely articulated in that way. The lens of competitive pressures and uncompetitive practices does not tend to be applied by small business, but rather concepts such as unfairness, inappropriate behaviour and administrative and compliance burdens. These concepts can be easily recast as competition issues. For example:

- Difficulties that small businesses have in resolving disputes (compared to larger business) can be viewed as a barrier to the operation of small business;
- Administrative processes that apply regardless of the size of a business can disadvantage small business; and
- The form of government procurement practices can limit the ability of small business to compete with larger businesses for contracts.

Central to these issues (and a recurring issue raised with our Office) is the imbalance of power between large and small businesses. For example, in February this year we released a report to the Minister for Small Business, the Hon Bruce Billson MP, on the small business concerns raised in the construction of the ASIO Building (Commonwealth New Building Project).

The primary concern raised by some stakeholders on this project was that more sophisticated prime (or even subcontractors) can take advantage of the imbalance of power to transfer the responsibility, risk and cost for variations to smaller subcontractors and secondary subcontractors. These small business subcontractors do not have access to the same level of professional skills and advice to effectively represent themselves alongside larger businesses. This can impact critical matters such as clearly determining to which matters a party is obligated under a contract.

The possession of market power of itself is not unlawful. In fact, it would be impossible to undertake projects of this size and complexity without the involvement of powerful participants in the construction industry. However, our report found that the contracting practices of all participants need to improve and improvements could have a significant impact on small businesses' ability to compete in the market, such as:

- Providing targeted education and information to assist small businesses to remain profitable and avoid insolvencies;
- Providing for better small business understanding of rights and obligations (for example through colour-coding of contracts);
- Ensuring that risks are borne by the party best placed to manage them;
- Improving the mechanisms by which small businesses receive payment.

Framework for governmental activity

Government has a role in improving the business environment, with two enduring core responsibilities, namely provision of information and justice. These pillars have a strong competitive focus.

Our Office has a credo that *'No small business should fail through lack of access to information'*. The facilitation of access to information is a core responsibility of government. It is appropriate for government to commit resources to information and other supporting services, especially where the behaviour of businesses participating in a particular sector is regulated. Access to information is a key component of a competitive marketplace.

The second enduring core responsibility of government when intervening to regulate business is to provide an appropriate system of justice. Previously, provision of justice focussed on placing wrongdoers in prisons. Refinements and sophistications over time have developed various means of providing systems of justice, which are not confined to punishment of offences against the Crown but extend to finding justice for those in private conflicts. Alternative dispute resolution has emerged as an appropriate measure of according justice in business dealings.

Access to justice is another key component of a competitive marketplace. A small business focuses on plying its trade or profession. Disputes will arise from time to time, but small businesses will often not have the skills and resources on hand to deal with these incidents that arise in the course of business but are not a part of the *ordinary* course of that business. These types of business disruption are not easily catered for by small business and, depending on the particular dispute, can impact small business disproportionately, particularly where there is unequal bargaining power.

Levers to improve the business environment

Between the pillars of information and justice lie the various levers that can be used to influence the business environment to ensure a competitive environment. These include:

1. **Small business management** – Businesses need to be skilled in what they do, able to access the right information and services and develop their management skills to allow them to conduct business in the most effective way;
2. **Small business & the marketplace** – Where market impediments are removed and businesses act according to good practices and behaviours, small business is able to thrive.
3. **Government as a business** – Government is a participant in business as a purchaser and vendor of goods and services and can have a significant impact on the businesses that it interacts with and the business environment more generally; and
4. **Government as a regulator** – Government is responsible for the infrastructure within which business is conducted, and can assist small business through effective regulation and impede it through bad regulation (this includes the way that regulators administer the law).

Our observations below draw on these levers to improve the competitiveness of the business environment.

Approach to regulation (& deregulation)

There are three broad elements to regulation that impact the business environment:

1. The choice to regulate an area and the design of any law;
2. The response required of business to comply with that law; and
3. The way that regulators choose to approach non-compliance and other administrative requirements.

The approach that government and regulators take in respect of each of these elements has an impact on the competitiveness of the market.

For example, introducing legislative requirements in an area can differentially impact businesses. The requirement that a certain approach should be taken (or not taken) may mean that smaller businesses cannot be as competitive as larger businesses that may be more diversified and able to cope with the requirement. This may result in a barrier to small business entry and/or a restriction on the nimbleness of small business in competing in the market.

As a result, the decision whether or not to regulate an area and the form of any regulation should be very carefully considered from a competitiveness perspective. It is the view of our Office that, as a general matter, when government intervenes it should do so in partnership with the participants in the industry. Partnership requires real consultation that responds to issues raised by business and collaboration in the design of regulation.

In designing regulation, the response required by business (and government) should be commensurate with the issue being addressed. The aim here should be to require the minimum compliance necessary to achieve the objectives and to be very clear about how the compliance burden is set (especially how the sharing of the burden between business and government is configured). Consideration of the full range of effective options should be had.

In designing and implementing regulation, the approach that regulators adopt to that regulation can have an even greater impact. Where regulators work with business to achieve outcomes through education and collaboration, a healthy environment can be obtained that addresses uneven impacts across the business environment. In contrast, an approach that focuses on enforcement and penalties can disproportionately impact small business that does not have the structures and resources to devote to administrative requirements. Heavy-handed approaches to regulation can act as a barrier to small business market access and limit the profitability of small business.

In dealing with the stock of regulation (and acting as a barrier to new regulation), the government's deregulation agenda will have a significant impact. Its five key areas of focus (volume, duplication, consultation, post-implementation reviews and the role of regulators) represent a comprehensive way to consider and reform existing regulation and improve the competitiveness of the business environment for small business.

In our engagement with small business, we stress the importance of the deregulation agenda, encouraging small business to question why a regulation exists and, if this question does not produce a satisfactory response, whether the regulation is ripe for deregulation action. Further, we encourage regulators to adopt a facilitative approach to administration of regulation, with a focus on educating to comply rather than leaping to enforcement of compliance.

Another observation we make is to note the savings and benefits to business of deregulation and also to include, as a component of benefit, the reduction in emotional stress associated with compliance. Though difficult to quantify, reducing stress is a real benefit of deregulation and one that will increase the ability of small business to compete in its core business activities.

Small business responsibility (& industry codes)

There is much within the control of small businesses to competitively participate in the marketplace. This ranges from taking advantage of information and services provided by government through to applying professional management practices.

Small businesses should seek to educate themselves in these areas. In particular, our Office encourages small businesses to accompany any education with access to their advisors (accounting, legal and others) as well as joining relevant industry and professional organisations. Support obtained through these channels can be a critical factor in small business success.

Small business can also find significant support for their ability to compete through industry codes of conduct. Industry codes can be a valuable tool to set out agreed practices of businesses within particular industry sectors. For example, in the franchising area the emphasis on the availability of clear information can assist small business to properly enter into and be successful in franchise agreements (such as, the provision of an information sheet for prospective franchisees, reminding franchisees of their entitlement to a disclosure document, greater transparency around funds allocated for marketing and the increased ability for prospective franchisees to engage with ex-franchisees). Perhaps of even greater importance is the proposed Franchise Code of Conduct's treatment of restraint of trade clauses that will bring a consistent approach across the industry and support small business' ability to continue to compete in markets following the end of a franchise.

Industry codes also have the advantages that they can provide more flexibility than regulation, be determined by the sector and allow for self-regulation. However, there have also been some concerns raised with our Office that while the current industry codes are mostly effective, they lose effectiveness as they become more complex and begin to resemble legislation. Also, some recent codes have clauses that provide for financial penalties for breach. Even in industry codes, heavy-handed approaches to enforcement can have a disproportionate impact on small business.

Dispute resolution

Disputes are a particularly difficult issue for small business since they generally arise periodically and in unusual circumstances. They can also pose a significant cost for small business that extends beyond the financial cost of lost business and pursuing resolution (such as legal costs) to the opportunity cost and emotional stress involved.

The opportunity cost includes what the small businessperson would otherwise have achieved for the business using their time and effort. For small business, resolving a dispute takes someone out of the business. Added to this cost is the emotional stress that disputes have on small business operators. This impacts the ability of a small business to compete whilst a dispute is on foot.

Alternative dispute resolution that operates with speed, at low cost, informally and collaboratively will generally be of greater benefit to small business – principally because it facilitates parties continuing their commercial relationships. Also, the potential cost of legal proceedings will in many small business disputes outweigh the amount in dispute. Drawn out legal proceedings with the possibility of appeal will generally also mean that the parties do not deal with each other commercially while the action proceeds and the breaking of this business relationship is likely to persist beyond.

Some additional benefits of alternative dispute resolution of small business disputes include:

- Its use in early intervention;
- Focusing the parties on what is commercially important (not every legal issue) and not needing to follow legal approaches;
- Control remaining with the parties to the dispute;

- Allowing for creative outcomes that are commercially realistic/pragmatic (not being about finding fault and “winning”); and
- Its high success rate in small business disputes (the success of mediation conducted or organised by the State Small Business Commissioners consistently exceeds 80%).

In terms of competition, it is also worth noting that methods of alternative dispute resolution may be subject to confidentiality between the parties. This means that an agreement is more easily reached in situations where the setting of a precedent could otherwise pose a difficulty for either party. However, this feature of mediation can have an impact on competition since the terms of an agreement that, say, one small business obtains is not transparent to other businesses.

The focus of alternative dispute resolution is on resolving disputes after they occur. It is of even greater benefit for small businesses to get education, adopt good business practices and develop approaches to avoid disputes arising. When a dispute does arise, businesses then may have the ability to recognise the importance of business relationships, treat the dispute like any other business issue, seek advice and look for speedy resolution through mediation or other means.

We note that the Victorian Small Business Commissioner (VSBC) has produced a constructive, educative study, entitled *Forming and Maintaining Winning Business Relationships*. The report identifies key behaviours to assist forming and maintaining successful business relationships, and emphasises pre-agreed dispute resolution processes as an important behaviour. The report can be accessed on the VSBC's website.

Industry codes of conduct also assist with the resolution of disputes. This can be achieved by providing for low cost dispute resolution mechanisms and clearly articulating the processes where there is a dispute. This includes covering factors such as how costs are to be borne by parties, the location for mediation and so forth.

We also believe that, although there may be reason for specific pre-mediation activities focused on particular industries in industry codes, good process coupled with good commercial mediators will produce successful results regardless of the industry. For efficiency, industry codes could set out agreed practices for an industry but then refer matters for alternative dispute resolution to a single point (regardless of the industry).

Government leadership

The Competition Policy Review Issues Paper (14 April 2014) focuses on government business activities such as providers of goods and services (electricity, gas, water, postal services and so forth). However, governments also act in a business-like manner when procuring goods and services and these actions impact on the competitiveness of the business environment. When acting as a business, governments can use the opportunity to display leadership and act as a model business. For example, governments can seek to resolve disputes early and use best practice in doing so.

Another example is the way that government conducts its procurement. Processes can be designed to facilitate small business tendering for work. Government leadership such as this

can have a significant impact on the business environment and mean that small business is more effective in its ability to compete.

In addition, governments provide very effective means to support the ability of small business to compete through positions such as ombudsmen and small business commissioners. These positions and their offices can provide leadership in dealing with particular and systemic issues that impact the ability of small business to compete.

Further government leadership in supporting the competitiveness of the business environment is also provided by the Australian Competition and Consumer Commission (ACCC) and the state consumer affairs and fair trading organisations. However, there appears to be a misunderstanding in the small business community about the role of the ACCC and some of the state organisations. For example, given that the ACCC deals with issues of competition, fair trading, false advertising and so forth, small business regularly approach the ACCC to deal with individual matters despite the organisation being focused on business matters that affect industries as a whole.

We are aware that a high percentage of the calls to the ACCC Small Business Information Centre are not within its focus. Although it is appropriate for the ACCC to determine if a complaint is a relevant matter for it to consider, the dispute resolution information and referral tool being developed by the Office of the Australian Small Business Commissioner ("Dispute Support") will be a valuable resource that can be used by the ACCC and the small businesses themselves to determine the most appropriate, low-cost dispute resolution service for individual disputes.

Conclusion

There are three main observations that may be drawn from this submission:

1. **Regulatory impediments** to competition should be construed very broadly and encompass not merely legislative rules themselves but also the cumulative compliance burden and the way that regulators behave;
2. **Small business** should not be viewed as a passive party in the business environment, but is capable of adopting more robust practices to strengthen its competitiveness (through avenues such as industry and professional associations, advisors and industry codes); and
3. **Government** has a leadership role when it participates as a business and also in providing information and access to justice. This includes its role in good regulation (using consultation and collaboration) and in providing mechanisms to ensure that the small business voice is more generally heard across government (such as through ombudsmen and small business commissioners). The deregulation agenda will also assist small business to compete.

As the review proceeds, we are available to talk further with you about specific issues and matters impacting the competitiveness of the business environment.