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## **Small Business Development Corporation**

### **Submission to the Productivity Commission Review of Barriers to Business Entries and Exits in the Australian Economy**

**February 2015**



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Development Corporation**

## INTRODUCTION AND FOCUS OF SUBMISSION

The Small Business Development Corporation (**SBDC**) welcomes the opportunity to contribute commentary to the *Review of Barriers to Business Entries and Exits in the Australian Economy* (**Review**) being conducted by the Productivity Commission (**Commission**).

The input provided has been drawn from previous submissions and projects completed by the SBDC that are relevant to the terms of reference for this Review. It should be noted that this submission contains the opinions of the SBDC and not those of the Western Australian State Government.

An extensive range of questions have been posed by the Commission in the *Business Set-up, Transfer and Closure Issues Paper* (**Issues Paper**) to explore topics relevant to the terms of reference for this Review. The themes that form the basis for the SBDC's submission are *reducing regulatory burden* and *a fair marketplace* with commentary focussed on the following terms of reference:

- 2(c) Regulations affecting the ease of starting, operationalising or closing a business; and
- 2(d) Time spent on and cost of complying or dealing with government regulation, licensing and bureaucracy.

Small businesses make a significant contribution to the community and economy. When regulatory environments and market practices are made more small business friendly, it provides opportunities for business owners to redirect resources to growth activities, thereby increasing productivity and further enhancing their contribution to the economy.

## ABOUT THE SBDC

The SBDC is an independent statutory authority of the Western Australian Government and was established to facilitate the development and growth of small businesses in this State.

The SBDC has been providing assistance to small business owners for over 30 years. In that time, the SBDC has gathered extensive knowledge regarding the issues facing small businesses and provided informed opinion on small business issues to industry and all tiers of government.

In order to build up a comprehensive picture of Western Australia's small business sector, the SBDC has a multifaceted approach to gathering information. Statistical data about the sector is monitored from a variety of sources, including interactions with individual small businesses, as well as undertaking frequent opinion polls and other surveys of small business operators.

The SBDC uses this information to inform evidence based policy development and advocate to other government agencies for the benefit of the small business sector internally.

## REDUCING REGULATORY BURDEN

It is well understood that the burden of compliance falls disproportionately on the small business sector. As small businesses generally do not have dedicated human resource or payroll staff, changes to the regulatory environment are typically felt directly by the business owner/operator.

In recognition of this, the SBDC acknowledges the strong small business focus applied by the Commission in its reports in recent years. In particular, the Commission's work on regulator engagement with small business and development of a regulator audit framework that has led to the adoption by the Federal Government of its *Regulator Performance Framework*. In the SBDC's view, the framework provides a platform capable of driving meaningful cultural change in agencies and lead to reduced regulatory burden on small businesses over time.

The SBDC has prepared the following material on the issues facing small businesses that create regulatory burden, based on recent advocacy and project work it has undertaken. The three areas identified for the Commission's consideration in this Review are:

- taxation;
- planning; and
- establishing a business.

### Taxation

Taxation remains a significant issue for small businesses from both an affordability and compliance cost perspective. Any decision to streamline and simplify the taxation system and make compliance reporting fairer and more transparent are important initiatives to improve the ability of small businesses to operate competitively in Australia's free market economy.

The requirement to pay taxes is a given for all business operations in Australia. Associated with this direct impost is the cost of complying with the various taxes that are applied by all levels of government. This impact can be particularly burdensome given the variations and complexity in the design of taxes and their reporting requirements. Reducing the overall burden of compliance through effective taxation reform will lead to a more productive and efficient economy in which businesses of all sizes can operate and compete.

## *Business Activity Statements*

Survey after survey reveals that tax compliance reporting remains a significant issue and cause of stress for many small business operators in Australia. It goes without saying that this burden is most pronounced at the smaller end of business operations (i.e. sole traders and micro-enterprises employing less than five staff) due to the limited resources (both financial and time) and/or expertise of business operators to ensure compliance with their reporting requirements.

Despite the fact that the Goods and Services Tax (**GST**) has now been in place in Australia for the past 14 years, its reporting via the Business Activity Statement (**BAS**) continues to be a source of considerable burden. Whilst arguably GST reporting leads to better accounting and record-keeping practices, completing a BAS and ensuring compliance (e.g. accuracy, timeliness) can still be a significant and straining undertaking and can unduly impact on a business's cash flow.

A MYOB survey of which policies or initiatives small and medium business (**SME**) owners would vote for in the lead-up to the 2014 Federal Budget revealed that simplifying the GST/BAS reporting process was the key priority for 64% of the 1,032 SME respondents, and has been for a number of surveys now.<sup>1</sup>

As the ongoing provision of education and assistance to small business operators is paramount to ensuring strong BAS compliance and a fair and healthy tax system in Australia, the SBDC has some concerns about how this is likely to be achieved in future. In particular, the SBDC notes that the Federal Government's budgeted savings measure to reduce departmental funding for the Australian Taxation Office (**ATO**) by \$142.8 million over three years (from 2015-16)<sup>2</sup> is likely to impact on the ability to meet this important objective.

It is hard to reconcile how the planned total staffing reductions of 4,700 staff over the forward estimates period to 2017-18 will be able to deliver essential, ongoing assistance to the small business sector. Feedback received by the SBDC from small businesses indicates that ATO support lines and call centres already suffer from lengthy delays, which will be further exacerbated by additional staff reductions.

Further to this, the SBDC is aware that the cost to government of collecting GST is comparatively higher vis-a-vis the collection of other taxes. According to the International Research Bureau of Financial and Economic Modelling (**IRBFEM**), the ATO "admits that the GST is incredibly costly to collect compared to other taxes, at least 40 per cent more per dollar collected and this is just ATO costs".<sup>3</sup>

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<sup>1</sup> As reported by Smart Company, "Budget 2014: SMEs call for easier tax reporting", 9 May 2014, Available from: [www.smartcompany.com.au](http://www.smartcompany.com.au)

<sup>2</sup> As announced in the 2014-15 Federal Budget.

<sup>3</sup> Australian Financial Review, "GST must be on tax forum agenda", 12 September 2011, pg.51.

In line with this, the IRBFEM makes the argument that "more than half of 2.6 million BAS returns are basically a complete waste of time", based on the Henry Tax Review's finding that "a large number of very small businesses bear the compliance costs of the GST while contributing very little to overall revenue collection".<sup>4</sup> It went on to argue that the GST reporting threshold level of \$75,000 should be "raised to \$500,000 or \$1 million with possibly little loss in collections but a massive decrease in social and administrative costs".

Compounding the compliance burden are the ever-changing rules that apply to the various taxation schemes (such as changes to asset write-downs and depreciation, and small business exemptions, offsets and concessions). It is unreasonable to expect busy small business operators to be able to continually stay abreast of these constant revisions, without the need to pay for expert assistance. This complexity adds to the cost of compliance. A recent survey by MYOB estimated that the average small business spends 84 hours, or two weeks a year, collecting the GST for the Government<sup>5</sup>.

Given the fact that over 95%<sup>6</sup> of all businesses in Australia are small, reforms to the taxation system will have wide-reaching, positive outcomes for the national economy as the small business sector is a significant contributor to employment, income and export generation.

### *New business entity*

The SBDC is aware of the complexity of tax planning and reporting associated with operating under a company structure and believes consideration should be given to introducing a new low-cost, hybrid small business entity to reduce this compliance burden.

Some years ago the Institute of Chartered Accountants and Deloitte formulated a proposal for business income to be taxed when it flows to the owners of the business rather than in the business itself, known as "entity flow-through" (**EFT**). Under the proposal<sup>7</sup>:

*..companies would receive tax treatment similar to that of a partnership, while maintaining the advantages of incorporation such as limited liability. For businesses that opt in to the system, this would mean avoiding a wide range of difficult-to-administer tax mechanisms such as carry-forward company loss provisions, fringe benefits tax provisions, family trust election provisions, trust loss provisions and franking credit rules.*

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<sup>4</sup> *ibid*

<sup>5</sup> As reported by ABC News, "Small businesses spend two weeks a year collecting GST", 24 February 2015.

<sup>6</sup> Australian Bureau of Statistics, ABS Cat. No. 8165.0

<sup>7</sup> As reported by Smart Company, "Plan to cut small business tax costs", 1 May 2008, Available from: [www.smartcompany.com.au](http://www.smartcompany.com.au).

In line with this proposal, the SBDC notes that the Consultation Paper released as part of the *Henry Tax Review*<sup>8</sup> floated the creation of an EFT taxation regime, which would allow qualified small businesses to operate formally within a limited liability entity (typically a company) while effectively being treated as a partnership for taxation purposes. Under that proposal, the deemed partnership would calculate its taxable income (or loss) and allocate it to individuals based on their interest in the entity and assessed at the individual investor's personal tax rate.

The SBDC believes that the introduction of an optional EFT taxation regime could have the potential to greatly reduce compliance costs for businesses conducted through companies and trusts and allow business operators to focus on building capital and capacity.

## Planning

### State Government

The SBDC notes that poor planning and development processes can have significant and long-term impacts on the viability of many small businesses and contribute to higher operating costs.

In Western Australia, major reforms have occurred at the State Government level to improve planning and development approval processes. Some of these reforms include the drafting of a *State Planning Strategy* and inclusion of professional input for major developments through the establishment of Development Assessment Panels.

The SBDC is aware that, on occasion, restrictive planning arrangements can stymie development and competition, reducing choice for consumers and artificially enabling landlords to charge higher rents.

For instance, the SBDC is aware of a State Government entity placing a restrictive covenant on land use in a suburb in the Perth metropolitan area. The covenant effectively restricts the type of retail businesses allowed to operate in the suburb, which has provided exclusivity to one landlord to develop a shopping centre. Initially, the covenant was put in place to attract a large retail tenant to the area and create shopping facilities in the locality at a time when broader community infrastructure was still under development.

Enacted in 2003, the covenant remains in place until 2018. Throughout this period, retail development in the suburb is being severely restricted which also limits competition. Since its introduction, the locality's population has grown significantly and residents continue to raise concerns about the lack of retail amenities available locally.

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<sup>8</sup> The Treasury, "Australia's future tax system – Consultation Paper", 10 December 2010. Available at: [http://taxreview.treasury.gov.au/content/content.aspx?doc=html/pubs\\_reports.htm](http://taxreview.treasury.gov.au/content/content.aspx?doc=html/pubs_reports.htm)

This situation highlights the need for planning and development agencies to ensure that competition is not needlessly restricted and that impacts of possible future retail locations on an existing shopping centre is viability (but not specific businesses) should only be considered during strategic planning preparation and not for site-specific rezoning or individual development applications.

### *Local government*

Based on the SBDC's experience, including in providing a dispute resolution service for small business operators in Western Australia, the impact of local government decisions on small business operations is often underestimated.

The fact that there are 138 local government authorities in this State with relative autonomy to set their own planning rules, interpretations and guidance, has led to a patchwork of different town planning schemes and inconsistent planning and development application processes and decisions.

This can cause significant angst for small business operators, especially those that work across different local government areas (such as tradespeople, food-sellers and professional/personal service providers) who have to contend with varying rules, regulations, requirements and restrictions.

The SBDC has prepared a range of case studies to highlight the impacts on small businesses of local government planning decisions, including for the Commission's review - *Performance benchmarking of Australian business regulation - role of local government as a regulator*.

The State Government is proposing to introduce further reforms to make planning approvals consistent across all local governments in Western Australia and the SBDC has recently indicated its strong support for this.

### **Establishing a business**

In a recent body of work<sup>9</sup> conducted by the SBDC, the regulatory burden imposed by the Australian Tax Office (**ATO**) and the Australian Securities and Investments Commission (**ASIC**) on start-up businesses was discussed in some detail.

An Australian Business Number (**ABN**) is required from the ATO by most businesses in order to meet the requirements of the **GST**. To register for an Australian Business Name (**BN**) from ASIC, business owners must be able to provide their ABN. Although it is common for new businesses to obtain both an ABN and BN, separate registration processes are mandated by the Commonwealth.

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<sup>9</sup> Small Business Development Corporation, "Identifying regulatory burden on small business – café case study", 2015



Further to this, separate online accounts have to be created by business owners to interact with the ATO and ASIC online. The ATO has created a secure 'login system' to identify a business called an AUSkey. An ASIC Connect account is obtained by signing up with a username or logging in using an AUSkey. While an AUSkey is not required to obtain an ABN, the only way to obtain a BN is by using ASIC Connect.

### *Australian Business Account*

Over the past eight years, extensive resources have been expended across Australian government jurisdictions in the pursuit of creating a single entry point for business owners to access online services across all tiers of government. An Australian Business Account (**ABA**) for businesses to interact with government for a range of significant government registration and compliance processes (e.g. business names, trademarks, licensing and taxation) was proposed to be this single entry point.

The ABA was a key initiative of the Australian Business Number/Business Names program, which was part of the Seamless National Economy Council of Australian Governments (**COAG**) reform agenda. The SBDC became involved in the ABA initiative after Western Australia entered into a National Partnership Agreement (**NPA**) with the Commonwealth and other state/territory governments for the delivery of reforms in 2007.

An ABA has been created and it is functionally possible for businesses to access online services across all tiers of government. However, the volume of businesses and government agencies using the ABA are low and more effort is required to increase its adoption across Australia.

### *Business names and licensing*

One of the key deliverables of the NPA was the referral of powers from states and territories to the Commonwealth for the regulation of BNs. As a result, all states and territories migrated their BN registers into a single national register administered by the ASIC.

As part of the business case for a national business names register, the COAG also agreed to an ancillary project known as Business Online Services (**BOS**). This project was aimed at providing businesses with the ability to search their compliance and regulatory obligations across all three tiers of government, save the results into an online account, and to submit and pay for the transaction using Smart Form technology hosted by the Commonwealth.

As a result, all states and territories migrated their business licence information data into the national system known as the Australian Business Licence Information Service (ABLIS) and the Commonwealth created the infrastructure for the saved results and account features, which is the ABA.



The Commonwealth also provided free access to Smart Form licences that allowed regulating agencies to convert paper forms into digital forms with or without back end processing integration.

The conversions do incur some cost, however the Commonwealth then hosts the form within the ABA infrastructure which means that agencies do not have to create the platform to provide digital forms to users and users can, in theory, conduct all transactions with government through the ABA without having to create multiple accounts with each agency.

### *Multiple online accounts for businesses*

In reality, the Commonwealth Government failed to integrate the ABN and BN registers with the ABA. As a result, three online accounts for interactions with federal government exist today, being:

- ABA
- AUSkey - ABN on the Australian Business Register
- ASIC Connect - ASIC

To date, the ABA has not achieved its intended policy objective of simplifying business interactions with government. For a single business account to be possible, integration of the ASIC-Connect and AUSkey must be the starting point.

The Western Australia Government has very limited content accessible within the ABA. State agencies have been slow to adopt digital forms and still predominantly offer paper based forms converted into PDFs that require the user to download and complete by hand.

In the SBDC's view, making more government information, administrative processes and transactions accessible to businesses online and working towards a single entry point for businesses to interact with all levels of government, would produce a significant reduction in regulatory burden for small businesses.

## **A FAIR MARKETPLACE**

This section briefly outlines some of the marketplace issues and policy settings that the SBDC has provided views on recently that may be broadly relevant to the Review. It includes material on:

- small business access to justice and finance;
- extending unfair contract term protections to small businesses; and
- security of payment in the construction industry.

The SBDC is able to supply the Commission with small business case studies on these issues should further information be required.

### **Access to justice**

The SBDC provided submissions to the Commission during its 2014 *Inquiry into Access to Justice Arrangements* regarding barriers that impede the small business sector's access to justice.

The submission identified the characteristics of small business operators that make them vulnerable to legal problems and provided information about the experiences small business owners have when trying to resolve disputes. The SBDC also made suggestions for improving access to justice and minimising legal problems for the sector, along with material regarding the design of the SBDC's 'small business friendly' Alternative Dispute Resolution service.

The SBDC supports the Commission's recommendations in its report on the inquiry regarding:

- government agencies publishing their dispute resolution management plans;
- organisations that were responsible for preparing information and education materials to improve access to justice having to incorporate ADR as a central platform in those materials; and
- government agencies (at all levels) being subject to model litigant guidelines (with compliance strictly monitored and enforced).

### **Access to finance**

Access to finance remains a barrier to many small business operators from budding entrepreneurs to established businesses wanting to expand.

The SBDC is aware that many business owners start their businesses using personal savings or money borrowed through informal channels such as family or friends. Therefore, when it comes to seeking funding for the next stages of business growth they have little in the way of credit history to show a bank manager.

Unfortunately, conservative lending practices by banks also means that loans and credit facilities are rarely offered to new or establishing businesses. Using credit cards at high interest rates is not viable over the long-term.

Employing fund managers with small business experience might allow banks to better evaluate businesses, and tailor products to suit the individual borrower.

Being able to evaluate the strengths and weaknesses of a business plan, projected incomes and profit levels, would provide a bank with the key information to back a business, without jeopardising the bank's integrity.

The SBDC acknowledges that small business entrepreneurs need to help themselves by having a detailed, up to date business plan, as well as sound procedures and systems that assist to demonstrate their ability to support a loan.

### **Unfair contract terms**

During its review of the consumer policy framework, and when considering the impact of unfair contract terms on small business, the Commission noted that small business operators face many of the same issues as individual consumers when dealing with larger business. This included unequal bargaining power and a lack of resources to effectively negotiate contracts.

Additionally, small business owners lack the resources and time to effectively educate themselves on these legal matters, which put them at a distinct disadvantage when it comes to contracting with a larger business.

The SBDC believes that unfair contract terms in standard form contracts is causing significant detriment to the small business sector and legislative reform is required to remedy this disadvantage. The SBDC therefore strongly supports the Commonwealth Government's proposal to extend unfair contract term protections to apply to small businesses.

### **Construction contracts**

The construction industry is an important contributor to the national economy and is dominated by small business operators.

Security of payment and access to effective dispute resolution is particularly important in the construction industry due to the following features of the industry:

- risk is typically pushed down the construction contracting chain creating power imbalances; and
- late and short payments (i.e. partial payment) to small businesses are common.

The SBDC has recently indicated its support for policy settings that provide more security for payment in this industry by:

- prohibiting or modifying unfair provisions in construction contracts;
- implying provisions in construction contracts about payment and dispute processes if there are no written provisions about the matters in the contracts; and
- providing a means for adjudicating payment disputes arising under construction contracts.

## CONCLUSION

The SBDC looks forward to the release of the Commission's report on *Barriers to Business Entries and Exits in the Australian Economy* at which time further comment may be provided.

Please contact Jenni Collins, Assistant Director Policy and Advocacy if you would like more information regarding this submission.