

Chapter 1

Introduction and Background to the Inquiry

1.1 The Senate referred this inquiry into small business employment to the Employment, Workplace Relations and Education References Committee on 20 March 2002, with a reporting date of 19 November 2002. On 23 October 2002 the date was extended to 12 December 2002, and on 12 December 2002 it was extended again to 6 February 2003.

1.2 The committee was asked to examine and report on the following matters:

- the effect of government regulation on employment in small business, specifically including the areas of workplace relations, taxation, superannuation, occupational health and safety, local government, planning and tenancy laws;
- the special needs and circumstances of small business, and the key factors that have an effect on the capacity of small business to employ more people;
- the extent to which the complexity and duplication of regulation by Commonwealth state and territory governments inhibits growth or performance in the small business sector; and
- measures that would enhance the capacity of small business to employ more people.

Conduct of the inquiry

1.3 A media release was distributed to major media outlets on 21 March 2002. The inquiry was advertised in the *Australian Financial Review* of 22 March 2002 and the *Weekend Australian* of 23–24 March 2002. Information on the inquiry was also disseminated to networks of academics with an interest in small business. Submissions were invited from a wide range of interest groups and organisations and individuals with an interest in small business employment or regulatory reform issues. Relevant Commonwealth government and state and territory ministers were also invited to make submissions.

1.4 A total of 96 submissions were received, predominantly from organisations, including a significant number from industry associations and regional groups. Very few submissions were received from small business, although the committee subsequently consulted a large number of small business proprietors through a series of roundtable discussions in cities across Australia.

1.5 Most state and territory governments chose not to make submissions or formal appearances before the inquiry. The Western Australian government, however, provided submissions on both small business and training issues and gave evidence at the public hearings in Perth. The Queensland government provided a submission and

evidence on industrial relations matters and provided an informal briefing on small business policies and programs during the committee's visit to Brisbane. The South Australian government assisted the committee by arranging a visit to its Centre for Innovation, Business and Manufacturing at Woodville and provided information on small business policies and programs. The committee appreciates those contributions but also regrets that more governments did not contribute and provide their perspectives on small business employment and regulation issues.

1.6 The committee conducted public hearings and roundtables with small business proprietors or their representatives in Perth and Albany in Western Australia and in Melbourne, Launceston, Sydney, Brisbane and Adelaide and held 2 days of public hearings in Canberra. It also visited the Eastern Suburbs Business Enterprise Centre in Sydney, the Capital Region Enterprise and Employment Development Association (CREEDA) business incubator in Canberra and the Port Adelaide business incubator. An informal lunch meeting with small business owners was hosted by the owners of the Hughenden Hotel, Sydney, for which the committee expresses its appreciation. The committee wishes to thank all those who assisted with the roundtables and site visits which provided an opportunity for it to hear directly from small business people and obtain an appreciation of the impact of Commonwealth and state government programs on small business. In particular, the committee also wishes to thank the small business proprietors and advisers who gave up their valuable time to attend the roundtable discussions and share their concerns, insights and suggestions. Their participation made a significant contribution to the report.

Context of the inquiry

1.7 Small business plays a significant role in the Australian economy and society:

- it accounts for 96 per cent of all business in the private sector (excluding agriculture): there were 1,122,000 small businesses in the non-agricultural private sector in 2001;
- it provides employment for over three million people (3,300,000) or 47 per cent of the non-agricultural private sector workforce;¹ and
- it accounts for approximately one-third of Australia's GDP.

1.8 Indeed, the Australian economy is sometimes described as a 'small business economy' because the small business share of private sector employment (outside agriculture and mining) is larger than in most industrialised countries apart from Italy, Spain and Denmark.²

1.9 For many Australians, owning their own business is a cherished dream, providing a rare opportunity for independence and self-fulfilment. Australia has one of

1 Australian Bureau of Statistics (ABS), *Small Business in Australia 2001*, 16 October 2002, 1321.0, 2001, p. 9

2 Productivity Commission, *Small Business Employment*, August 1997, pp. 11–12

the highest rates of business start-up in the world.³ With many traditional and 'standard' jobs disappearing in recent years, and a growing demand from men and women for more flexible ways of balancing work and family, an increasing number of Australians, including women and Indigenous people, see self-employment, particularly in home-based business, as their most promising career path.

1.10 Small business also contributes to the quality of life and sense of community for many of those Australians who do not work in the sector. Small businesses provide many of the daily goods and services for the local neighbourhood; compared with larger businesses and chains, they are more likely to use local suppliers and thus re-invest in the local community; the proprietors often contribute financially, and in other ways, to support community projects; and they are more likely to provide flexible, personalised services to meet the needs of local customers. At least one in ten homes across Australia now hosts a home-based business. As a Western Australian businesswoman explained:

Small businesspeople underpin our communities...They're the people who provide the soft drinks for the tee-ball wind-up, the people who operate the pharmacy up the road. They're the people who live and work and play next to you and I think they have a really big impact on our lives but we tend not to look at them in that way. We often see big businesses as heroes, but I think some small to medium businesses are the real unsung heroes.⁴

1.11 In regional areas, small businesses play an even more significant role because, along with agriculture, they are often the main drivers of economic activity. A recent policy options paper on regional development concluded that:

At the end of the day, most regional communities will only survive through the efforts of entrepreneurial businesspeople continuously making successful investment decisions so that the local economy constantly reinvents itself.⁵

1.12 There is increasing recognition of the potential for small business to contribute to economic development, innovation and export growth. Information and communications technology are opening new opportunities for small business to market its goods and services outside the local area including in international markets. Small business is lifting its export performance at a faster rate than medium or larger businesses.⁶ There is a growing interdependence between small and larger businesses as larger firms and public sector agencies outsource non-core functions to small,

3 K. Hindle, and S. Rushworth, *Global Entrepreneurship Monitor Australia 2001*, Yellow Pages, p. 7

4 'From Pressure and Success, the Western Australian 1998', article on Joanna Ballantyne reproduced at: www.secondskin.com.au/

5 T. Sorensen, 'Regional Development: Some Issues for Policy Makers', *Parliamentary Library Research Paper No. 26, 1999–2000*, 27 June 2002, p. 18

6 Submission No. 58, Austrade, p. 3

specialised firms. The OECD has identified the role of small and medium enterprises in promoting innovation and economic growth and development as an important area of policy interest for member governments.⁷ This includes small business' role as the seedbed for entrepreneurial talent.

1.13 Small business is also of increasing interest to policy makers because it accounts for almost half all private sector employment nation-wide, and often more in regional areas or less urbanized states. Employment growth in small business began to outstrip that in medium and larger size firms from the 1980s to late 1990s, but the pace of growth subsequently slowed,⁸ prompting interest in employment determinants and the role of government interventions or policy settings. The Productivity Commission study of small business employment in 1997 set out, in part, to address this question. It concluded that the factors that determine small business employment are complex and not well enough understood and cautioned against unrealistic expectations that selective assistance to small business will translate into increased employment.⁹ Evidence to this inquiry reinforced this finding. The OECD, while recognising the difficulties in framing effective policies and programs for small business, supports the need for encouragement of entrepreneurial activity and for governments to address areas of small business disadvantage, including in relation to information, new technology and innovation. A key aim of this inquiry is to develop a better understanding of the factors that determine employment growth in small business as the basis for more informed debate and policy development.

1.14 The relationship between regulation and employment in small business is a particular area of interest because of small business complaints that an increasing burden of regulation and government 'red tape' is stifling its capacity to employ more people. At the same time, some segments of the small business community, particularly those in highly competitive, price-driven markets dominated by large corporations, see the regulation of anti-competitive practices as the key to their survival.

1.15 The complaint of excessive red tape and the burden of government regulation is not new. The Small Business Deregulation Task Force was established in 1996 to recommend measures aimed at halving the regulatory burden on small business. Many of the recommendations have been implemented but the pace of regulation continues: in 1999–2000, the Commonwealth government alone made around 2,000 regulations, of which 207 had an impact on business.¹⁰

7 See for example, *SMEs: Employment, Innovation and Growth—the Washington Workshop*, OECD, 1996, p. 7

8 ABS, *Small Business in Australia 2001*, 1321.0, 2001 p. 13

9 Productivity Commission, *Small Business Employment*, 1997, p. 69

10 Productivity Commission, *Regulation and its Review, 1999–2000*, Commonwealth of Australia, 2000, p. 3

1.16 A CPA Australia survey in July 2002 identified compliance costs as among the major risks to small business profitability. These include: the compliance costs associated with the GST/BAS (29 per cent); too much paperwork (14 per cent); government bureaucracy (10 per cent); and, legislation changes (10 per cent).¹¹ To put this in perspective, other major risk factors are big business and other competition (21 per cent); other matters related to the GST, such as impact on cash flow (21 per cent); slowing economy (15 per cent); and cash flow (10 per cent).

1.17 The problem of an increasing regulatory burden is not unique to Australia. In its recent review of small business views on red tape, the OECD acknowledged the continuing need for regulation to protect the public interest but urged governments to find better ways of minimising the adverse effects on business and entrepreneurship.¹² This inquiry provides a useful opportunity to draw together the findings of that review and to assess what has been achieved following the implementation of the Government's response to the Small Business Deregulation Task Force report, and what remains to be done.

Overview of submissions and key issues

1.18 Submissions were received from the following groupings:

- Commonwealth and state government agencies and local councils;
- regional development bodies or organisations, including Area Consultative Committees and regional development boards;
- national, and in some cases state-based, industry associations;
- organisations representing segments of the small business community or broader business interests;
- professional associations and unions; and
- organisations and associations providing services to small business, general interest groups, academics, and individual small business people or advisers.

1.19 Issues raised in submissions often reflected the particular interest or focus of the submitter. Industry associations such as the Australian Retailers Association and the National Association of Retail Grocers of Australia raised predominantly industry-specific issues such market concentration in the supermarket sector and the need for reform of competition laws and retail tenancy issues; the Pharmacy Guild raised concerns about the compliance burden of current arrangements for GST collection in the pharmacy industry; and the Housing Industry Association identified problems with the planning and development approval processes. Several submissions also expressed concerns with the personal services income taxation legislation.

11 CPA Australia, *Small Business Survey Program: Perceptions of Risk*, August 2002

12 *Businesses' Views on Red Tape—Administrative and Regulatory Burdens on Small and Medium-Sized Enterprises*, OECD, Paris, 2001

1.20 Submissions from regional organisations understandably highlighted the problems facing small business in regional areas but also provided many useful insights into ways to reduce the burden of regulation on small business and suggested initiatives to assist small businesses to grow, prosper and employ more people. Small business associations raised a broad range of issues, including the need for governments to reduce the compliance burden and improve their assistance to small business. Two of the issues that were raised in a large number of submissions, the need for stronger competition laws to protect small business from anti-competitive practices and the high cost and limited availability of public liability insurance, are not dealt with in any detail in this report as they are subject of separate government or parliamentary inquiries.

1.21 The key issues that emerged in the inquiry are:

- the enormous diversity within the small business sector and its relatively fragmented, isolated and unorganised nature, which complicates the tasks of consultation, information dissemination, and policy formulation and implementation;
- the changing nature of small business and the environment in which it operates, including the rise of home-based business, the growing number of small business exporters, the increasing participation of women and Indigenous people in small business and the challenges, opportunities and potential arising from more open, globally oriented markets, the knowledge economy and technological change;
- the determinants of employment in the small business sector are complex and not well enough understood so developing a better information base is an important precondition for more effective policy development. Business growth is clearly a precondition and an area where a range of government interventions could be effective;
- the critical role that business management skills play in the survival and growth of small business and the need for many small business operators to upgrade their skills in this area, including their people management skills;
- the difficulties and disadvantage that small business faces in obtaining the key inputs of capital and skilled labour, and the less favourable treatment that it receives from big business in many areas including settling of accounts, terms of trade, and bank fees and charges;
- the *ad hoc* and disparate range of Commonwealth, state and local government assistance programs for small business, the large number of agencies and organisations involved and the lack of formal coordination arrangements is confusing for small business and limits the effectiveness of the total investment; and
- the compliance burden associated with government regulation is a major and growing concern for small business (although this varies with the business size and industry sector), with many small business operators unaware of the full

extent and nature of their obligations and many others struggling to come to terms with identifying, understanding and meeting those obligations. Regulatory requirements associated with taxation (particularly the new taxation system and the Goods and Services Tax or GST), employment and the environment are particular areas of concern along with the pace of change and growing complexity of requirements.

1.22 This report deals with these main themes in the following five chapters:

- Chapter 2 provides an overview of the small business sector, highlighting areas of common ground and points of diversity;
- Chapter 3 assesses the evidence on the nature of employment in small business and the factors that affect employment potential and trends;
- Chapter 4 provides an overview of current government programs and policies and identifies areas where improvements are needed;
- Chapter 5 discusses the business management skills of small business operators and the broader skills of the small business workforce; and
- Chapter 6 discusses how regulation affects small business and considers ways in which further progress could be made in reducing the burden of regulation.

1.23 The committee has chosen to focus its discussion on these issues at the level of broad or general principle. In the time available it would not have been able to do justice to the very diverse and specific matters of concern to small business. It also considers that the most constructive contribution that it can make is to focus on the issues that were identified as of greatest importance and relevance to the sector as a whole. Inevitably this means that some of the issues of concern to specific industries or segments of the small business community are not addressed in any detail. The committee considers that those industry specific issues are best dealt with in other contexts.

