the state of COMPETITION

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Australia's small business sector : "Not for the faint of heart"

The great raconteur, Anonymous, observed that "Small business isn't for the faint of heart. It's for the brave, the patient & the persistent. It's for the overcomer". While this may be true, the law should not be amongst the hurdles that small business needs to overcome. But a close look at Australia's competition law regime suggests that there is plenty of room to improve the way it engages with the "backbone" of the Australian economy. In this issue, we identify some shortcomings before floating ideas as to how they may be overcome.

A lot has been written about 2014 Australian Open winner Stanislas Wawrinka. Wawrinka, an Australian crowd favourite and confirmed underdog, has inscribed on his arm a quote from Samuel Beckett:

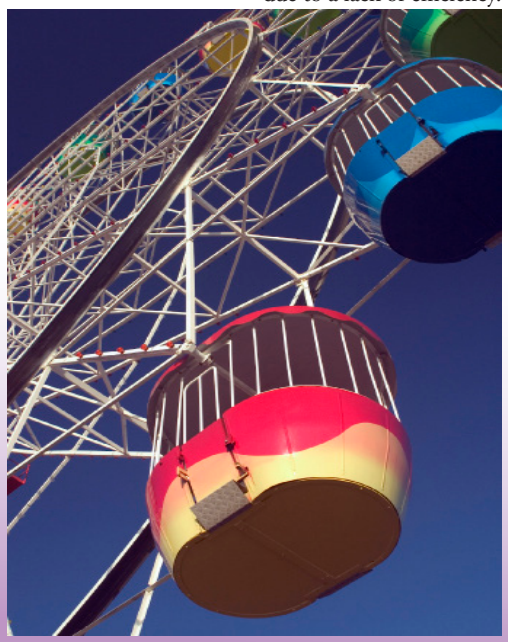
Ever tried. Ever failed. No matter. Try Again. Fail again. Fail better.

Fail again, fail better… If only that were possible for the many Australian small businesses who face their own daily battles to stay in the game. Most of them will get only one shot at failure.

From the perspective of competition law/economics, should we care about the stories of small business owners who passionately believe in what they do but have reached the point where they have to sell up or shut up? After all, we're taught that it's about competition, not competitors with markets being ruthless places where we expect to see less efficient players fall by the wayside. And surely, unless it's a market known to have barriers to entry, can't we just assume there'll always be someone else prepared to come in and take their place?

Well maybe it's not that simple. There are valid reasons why even hardcore fans of competition theory should care. But to appreciate these, we need to allow the shiny theory to become tarnished by the oxygen of practical reality.

Let's start with the observation that, often, the failure of a small business is not due to a lack of efficiency. Frequently, it's the result of having less cash flow, less ability to cope with unexpected external conditions or to bear losses while problems not of their own doing are fixed, or simply due to increased vulnerability eg following investments in innovations that will deliver lower unit costs if accompanied by increased volume. In other words, it could be that a business's very "smallness" is preventing market forces from playing out as they should, such that there is an implicit requirement to be "this big to ride" at the amusement park.



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Is the Australian economy increasingly imposing a "this big to ride" requirement on business?

Further, as we discussed in Issue 14, small firms are often an important source of innovation, with owners willing to bear the risk of trying out new and better ways of doing things, backing their own belief until their ideas are proven enough for others to support them. Indeed, think of the findings of market power in *Melway* and *Cabcharge*: these were players who came to dominate the market due to their innovation and preparedness to explore new territory. Before they "qualified" for section 46 scrutiny, they too were small businesses. Continually developing "work arounds" on tight budgets, small businesses frequently play an important role – individually and collectively – in keeping large

Does small business have the luxury of being able to fail better? If not, are our competition laws helping or hindering?

businesses "on their toes" and preventing them from freezing market forces that would otherwise drive change.

But there's nothing more likely to chill a potential innovator waiting in the wings than watching the failure of good initiatives – not because customers didn't like them but because no matter how hard you try and how much better your innovation, it's just too hard.

When failures of this sort happen, efficiency is actually harmed with market power frequently being "gifted" to incumbents. Indeed, this analysis provides the theoretical underpinning of the need for mavericks or, in the language of our merger law, "vigorous and effective competitors". Similarly, whether such players have been deliberately targeted is a key way to distinguish fiercely competitive conduct from predation.

So sometimes the best way to protect competition may well be to look after the small innovative players in the market, at least until customers can decide whether they are worth supporting or not. Ultimately, that's where competition law and competition regulators should get involved – not deciding *how* the market should operate, but rather ensuring that customers have the opportunity to decide which products/suppliers best meet their needs and who should stay or go.

What then are the practical problems facing small business? Often they are not to do with the scope of our competition law (ie what it does and does not catch); rather, they relate to how small businesses can access the law and how they engage with regulators and policy makers.

Engaging with the law *and* the ACCC

There are three basic capacities in which small business engages with the law (and the ACCC):

• in a compliance sense

• as a complainant (ie, as a "victim" of anti-competitive conduct or as someone concerned by a merger) and

• as the target of investigations.

Each of these facets could be improved.

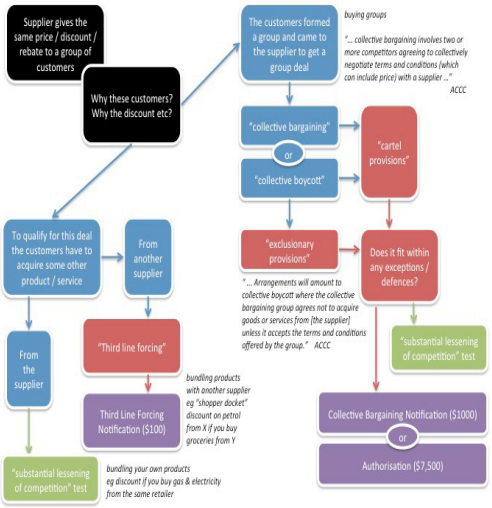
Trying to ensure compliance can be expensive

When asked by an appreciative client "how can I ever thank you?", famous American lawyer Clarence Darrow is said to have responded: "My dear woman, ever since the Phoenicians invented money there has been only one answer to that question".

Australia's competition laws are extremely complex, and as discussed in Issue 11, with every iteration, they seem to become more complicated. The result, as a former High Court judge said, is a maze of statutory provisions that "requires the negotiation of too many cross-references, qualifications and statutory interrelationships" with the "danger of losing one's way in the encircling gloom".

Meanwhile, access to quality information about the law is very difficult – free materials provided by the ACCC (or others) are hard to access and tend to be excessively simplified. If one acts on this advice, one will be colouring so far within the lines that better-advised competitors will likely have a competitive advantage. It is those competitors who understand how they can legally bundle their products, enter into efficient joint ventures or simply partner with a business up the road to make their offerings more attractive. Simplified statements of the law are dangerous because they constrain the capacity of small business to compete effectively and engage in the rough and tumble of tough (but fair) competition.

Complexity creates disadvantage



The above illustration (taken from Issue 11) is a "simplified" flowchart of how our filing system works. While freely available information tends to advise that "*competitors can't fix prices*", nuanced (expensive) advice will add "*unless they fall within an exemption or an anti-overlap provision or have obtained authorisation*" before explaining the ins & outs of the above diagram

The secret to navigating the maze is, of course, to have an expert guide. However, it is hard to find expertise in competition law outside the big law firms where, at around $700 per partner hour, the rates are prohibitive for most small businesses.

Put another way, with a limited pool of experienced competition lawyers, small businesses are competing against big businesses for these services. It's not just a question of whether they can afford one-off engagement with an expert either: work from the small end of town is not all that enticing to many firms when compared with the portfolio of work that may be offered over many years by the big players. In the case of "commercial" conflicts, it's generally the smaller guys who are asked to look elsewhere for assistance.

If small businesses can't access expert legal advice, then they tend to be left with well meaning but misguided (or, even worse, potentially incorrect) informal advice. This could come from other businesses, Government departments or even regulators.

Small business as a complainant

What about when small business perceives that it is the target of anti-competitive conduct? Complainants should be able to bring their concerns to the ACCC without having to engage a lawyer. In reality, though, this is not the best approach to ensure a legitimate complaint gets the attention it deserves. DIY complainants who cannot clearly articulate their problem within the legal framework may have their issue summarily dismissed by someone with little or no legal training.

As a further issue, problems have to be sufficiently "big" to attract ACCC attention. Where complaints *are* taken up, their legal resolution can take so long that a commercial resolution will beat any final decision of a Court (even if, in a worse case scenario, that means the victim goes out of business).

Does $1 million matter?

As a complainant, it's hard to get the attention of the ACCC if your loss is "small bikies". But what is small bikkies? $1m is way too much for a small business to bear but is unlikely to be enough to capture the ACCC's interest.

Similarly, when trying to comply with the law or to engage with an investigation, a small business acting properly & trying to provide a comprehensive response can easily burn $1 million in legal fees and lost management time. Even complying with a "friendly" section 155 notice can incur significant cost.

Small business as a target of ACCC investigations

Finally, make no mistake, small business frequently falls foul of the law. There is a disproportionate number of cases taken against small business, as opposed to cases against larger, well-resourced and well-advised businesses. (While recent statistics don't tend to bear this out, such statistics are distorted by the air cargo litigation and in general the very small number of competition cases over the last few years.) But this does not suggest that small business has more than its fair share of rogues. Indeed, many successful ACCC prosecutions are for breaches that are inadvertent and/or do not affect competition.

Small business is more likely to be poorly advised when engaging in specific conduct (see above); will have greater difficulty in obtaining appropriate advice during the course of an investigation; and will be more likely to settle with the ACCC rather than fight due to the sheer expense of litigation. Even responding to a "simple" section 155 notice can impose a crippling cost burden on small business, leading to inadequate answers which can prolong an investigation or make things appear worse than they really are.

These factors combine to make cases against small business "low hanging fruit".

Should the *per se* prohibitions apply to small business?

When considering practical solutions to the problems outlined above, we pondered the point made in Issue 11 about filings: there is a significant strategic advantage in knowing not only what you can't do but, more significantly, what you *can* do.

Generally speaking, it is unlikely that the day-to-day activities of a small business are going to impact on competition in a market. But the *per se* prohibitions apply equally, regardless of size or impact on the market as a whole. So, two small fish & chip shops who agree not to compete are no different in the eyes of the law from two major banks reaching the same agreement – even if the former did not lessen competition but the latter did.

The rationale for *per se* contraventions is that – generally speaking – the particular conduct in question will inevitably have an adverse impact on competition and that undertaking a detailed competition analysis every time it occurs is not worth the time and money (either for the parties involved or for the enforcing agency). This assumption, however, simply does not hold for small business.

Further to the points made earlier, perhaps another reason why small businesses appear to be disproportionately prosecuted for *per se* breaches is that they see larger players engaging in conduct that is clearly attractive to customers and want to do the same thing. Without a bevy of lawyers at their beck and call, however, the small business in question may not understand that the conduct was supported by a notification or had been structured in a particular way to avoid attracting provisions that favour form over substance. (To this end, we again note how difficult it is to search the public registers, especially if you don't already know what you're looking for.)

Given the scope of *per se* prohibitions in our Act, there is a huge burden on small businesses to get it right. Fear of breaching the law typically results in self-censorship of commercial options that might actually be possible if structured the right way or covered by an appropriate filing. So, assuming there was a legitimate public benefit justification for the non-compete in the example above, the reality is that the major banks would be receiving expert advice and obtain protection via authorisation while the two small fish & chip shops would end up being prosecuted.

Once again, this comes back to money and resources. Authorisation is a powerful tool but an expensive one. It's not unusual to hear businesses talking of $100,000 or more for the work involved in getting an authorisation in place. With merger authorisations now going straight to the Tribunal, one can only imagine those costs are higher again. Even the simple collective bargaining notification comes with significant red tape (and accompanying expense), having to be renewed every 3 years.

Thoughts on small business

"Entrepreneurs & their small enterprises are responsible for almost all the economic growth in the United States."

"Be faithful in small things because it is in them that your strength lies."

Who knew Ronald Reagan & Mother Teresa had so much in common? (We assume you can guess who said what!)

More thoughts on regulator engagement

Clearly the ACCC is a world class regulator and does many things very well. However, there's also no denying that much of the way it operates has been shaped by two regular dance partners: consumers and what is often referred to as the "big end of town". The latter tend to comprise regulated monopolies and the behemoths who have market power or the potential to influence competition, usually represented by the familiar faces of what the press calls the "trade practices mafia".

That makes sense given the theoretical reasons why we need to have a "competition" and "consumer" commission. However, as our Act becomes increasingly prescriptive and given the scope of *per se* prohibitions, smaller businesses are increasingly likely to come into contact with the ACCC and need to add competition law compliance to their cost of doing business.

The Productivity Commission summed it up in its report on *Regulator Engagement with Small Business* in October 2013:

> *Small businesses feel the burden of regulation more strongly than other businesses. Almost universally, their lack of staff, time and resources present challenges in understanding and fulfilling compliance obligations.*

It's a challenge too for regulators. As the NSW Small Business Commissioner observed to the Productivity Commission, "a small business is not just a big business on a smaller scale", but one that operates in a fundamentally different way. Further, the small business sector is "notoriously hard to engage", covering a diverse range of industries, each with different priority issues and all being time poor.

An important lesson that comes out of the Productivity Commission's review is that how small businesses "experience" regulation "has as much to do with the engagement approaches of regulators as it does with the regulations". Whilst our regulators are generally recognised as being committed to effective engagement and to minimising unnecessary burdens, they fall short in trying to translate that into "good practices on the ground".

The Productivity Commission emphasised the fundamental importance of "regulator culture", which must include embracing continuous improvement "including critical evaluation of existing practices". It noted that if a regulator adopts an "us and them" mentality, then it is "highly likely that this will manifest itself as poor regulatory engagement strategies".

The ACCC stands out in comparison to many other regulatory bodies in relation to some aspects of engagement, especially education – adopting the multiple channels and multi-pronged approach preferred by small business commissioners in their input to the Productivity Commission.

In other respects, however, the ACCC can all too easily fall into an adversarial mindset that may well be understandable dealing with the corporate machinery of big players (where differences are resolved by drawing writs at 50 paces). For small business owners, however, this can appear extremely insensitive as, for them, business is intensely personal (after all, it might be the owner's house on the line).

The Productivity Commission suggested that regulators should have processes for dealing with small business complaints (and learning from them) including low cost mediation services to resolve disputes and misunderstandings between small businesses and regulators. It suggested this could involve mediation by existing small business commissioners, and that such services should complement existing statutory and administrative review rights.

Such a suggestion really tests the commitment of a regulator to small business engagement. However, the reality is that sometimes regulators do make mistakes and get things wrong. But, as the NSW Small Business Commissioner noted "there is no remedy or compensation available to small business when a regulator makes errors causing inconvenience and in some instances financial loss to a small business".

The Department of Industry, Innovation, Science, Research and Tertiary Education in its submission to the Productivity Commission provided data about the calls made to its Small Business Support Line from 3 September 2009 to 15 February 2013.

Typically the concerns centred on "licensing information (fee structures), conflicting advice from agencies/regulators, unclear advice from agencies/regulators, and insufficient information available". The most frequent calls were about the ACCC (31%) with the next most frequent calls being about ASIC, Standards Australia and General (14% each).

Thinking small business first

The NSW Small Business Commissioner advocated the adoption of a "think small business first" mindset for regulators. In the context of the ACCC, we consider such a mindset would mean that it's all about the *process* of engagement, not about whether the regulator should "take sides" with small business or treat small business as a protected species.

So focusing on the process of engagement, how might a "think small business first" mindset manifest itself?

One of the key things would be an added sense of urgency for matters involving small business, recognising the disproportionate ability of small business to bear the cost of unresolved issues. Small businesses complainants need to know quickly whether or not the ACCC can do anything and, if so, the timeframes for what the ACCC will do (because sometimes, as the saying goes, justice delayed is justice denied). Small businesses can find that even if their complaint is taken seriously, once an investigation starts they have no idea how long it may be before there is any outcome and in the meantime they are bearing losses they cannot sustain.

If the ACCC cannot do anything, then there needs to be a very clear explanation of exactly why this is so. Sometimes the public disappointment of small businesses about a lack of action by the ACCC is due to unrealistic expectations. On the other hand, sometimes explanations are inconsistent or misleading, which makes it hard for small businesses to take up their issues elsewhere. This can result in a merry-go-round between the ACCC and Government or some other regulator, each telling the small business to go back to see the other because what they have been told cannot possibly be right.

For investigations involving small businesses, a "think small business first" mindset would manifest itself in going beyond being a "model litigant", appreciating that when dealing with businesses who cannot afford to fight, the ACCC effectively becomes "judge and jury". Whilst it may be great to see a competition regulator willing to test the boundaries of the law, the ACCC needs to be wary about using small businesses as test cases; a "think small business first" culture would suggest test cases are more appropriately run against businesses who can afford litigation (so there is actually a true "testing" of the point concerned).

It's not only small business who has to count their pennies

Getting the culture right is one thing, having the funds to translate that into practice is another. The Productivity Commission made the point that regulators should be assured of "sufficient resourcing to enable them to administer and enforce regulation effectively and efficiently" including ensuring that they have "the capacity to make appropriate use of educative and facilitative engagement practices."

In that regard, should small business be concerned about the impact of budget constraints on the ACCC? The ACCC Chairman assured the Senate Estimates Committee on 26 February 2014 that the ACCC would adjust to whatever level of funding was given in the future, which might mean having to write smaller reports or running fewer enforcement cases. But prudent fiscal management may not be compatible with improved small business engagement.

The Productivity Commission also had another message for Government if it wants to take small business engagement seriously, namely the importance of proper regulatory impact

analysis, including "intended approaches to regulation implementation, monitoring and enforcement; and the likely impacts on business". In that regard, the quality of regulatory impact analysis involving changes to the Act has been somewhat inconsistent or superficial, as mentioned in Issue 14 regarding amendments to section 46.

Finally, the Productivity Commission suggested that regulators should facilitate opportunities for staff to "enhance their understanding of business practices and the nature and magnitude of the compliance costs their engagement approaches impose on small businesses". In its submission to the Productivity Commission, the ACCC noted that it is required to have at least one Commissioner who has knowledge of or experience in small business matters and observed that this Commissioner (currently Dr Michael Schaper) "participates in all of the meetings and decisions of the ACCC". As a Commissioner, that is of course to be expected. However, a more interesting cultural question to explore would be the extent to which that Commissioner is given the "access all areas" pass to get involved in any matter or process involving small businesses and if needs be to critically evaluate or change how that matter or process is being handled.

Some practical ideas to help

One thing we could do is simplify the law a little. For example, the historical reasons for distinguishing section 45 conduct from section 47 conduct have largely disappeared. Recently, Rhonda - in concert with the Melbourne Law School's Arlen Duke - has been looking into how we could devise a single provision that prohibited commercial arrangements involving 2 or more parties which substantially lessen competition. You'd be surprised at how much unproductive legal analysis would be stripped away by such an approach, with limited (if any) increase in the potential for anti-competitive conduct.

We could also get rid of some of the red tape. As flagged above, the *per se* prohibitions seem a good place to start. In Issue 11, we concluded that filings are working fairly well in terms of allowing firms to deal with *per se* prohibitions. However, the issues raised above affect the ability of smaller businesses to access this solution. There is a case for carving small businesses out of the *per se* prohibitions so that they will only breach the law (and only need to consider filings) if their conduct impacts on competition.

It would be necessary to establish an appropriate threshold for when *per se* prohibitions don't apply. There is no uniform definition for "small business", as noted by the Office of the Australian Small Business Commissioner (**ASBC**) in its submission to the Productivity Commission. However, the standard ABS definition favoured by the ASBC (being a business that employs less than 20 employees) could be the starting point for debate on an appropriate threshold.

Another thing we could do is to expand the role of the ASBC to encompass an advocacy role in dealing with the ACCC and providing affordable assistance – whether through internal expertise to help businesses prepare and file authorisations or notifications, or by acting as a clearing house for competition lawyers and economists willing to act pro bono or at reduced rates to help small businesses facing genuine competition problems.

The Root and Branch review is not the first attempt to improve Australia's competition law framework, particularly as regards its engagement with small business. Hopefuly a focus on practical solutions will deliver more effective outcomes than we've seen in the past. If nothing else, it's an opportunity to try again, perhaps fail again but at least fail better.

If you're a small business, we'd love to hear your experiences. Please email us if you have any observations you'd like to share.

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Rachel and Alexandra are both Australian Legal Practitioners within the meaning of the Legal Profession Act 2004 (Vic), with liability limited by a scheme approved under Professional Standards Legislation.

The Cement Australia decision (late last year) has prompted some interesting musings on market definition. Read all about them in our next edition by subscribing via the "Newsletter Sign-up" button on our website.

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