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28 May 2014

Ms Anne Scott
Principal Adviser
Small Business Ombudsman & Procurement Unit
Small Business, Competition and Consumer Policy Division
The Treasury
Langton Crescent PARKES ACT 2600

By email: Anne.scott@treasury.gov.au
small.business@treasury.gov.au

Dear Ms Scott,

SMALL BUSINESS & FAMILY ENTERPRISE OMBUDSMAN – DISCUSSION PAPER

The Australian Finance Conference (AFC) appreciates the opportunity to provide feedback for the Government's consideration in taking forward the proposal to transform the Australian Small Business Commissioner into a Small Business & Family Enterprise Ombudsman [SBFEO]. We understand input is particularly sought on the nature and scope of four key responsibilities for the role; namely:

- Concierge for dispute resolution;
- Commonwealth-wide advocate for small business and family enterprises;
- Contributor to the development of small business friendly Commonwealth laws and regulations; and
- Single entry-point agency through which Commonwealth assistance and information regarding small business can be accessed.

Feedback is intended to assist shape the development of the SBFEO role by the Government.

Background

The AFC membership includes a range of credit providers, financiers, receivables managers and service providers to the finance industry including the three principal Australian credit reporting agencies. AFC member companies are involved in the full range of lending financial services in both the consumer and commercial markets. For those that provide commercial finance, a significant component of their customer-base is "small business". Small business finance is also of particular interest for Members of our associated bodies that focus on providing finance in the commercial market; the Australian Equipment Lessors Association (AELA), Debtor and Invoice Finance Association (DIFA), Australian Fleet Leasing Association (AFLA) and the AFC-affiliated Insurance Premium Financiers. Depending on how "small business" is understood, some of our Members (in addition to the AFC) may also fall into this category in their own right. As a consequence, in framing our comments we have attempted to consider the Government's proposal for the SBFEO from the perspective both of a small business customer of one of our Members and as a Member that is a small business.

Context of Inquiry

We agree with the view expressed by the Minister for Small Business on behalf of the Government that "*small businesses and family enterprises are a vital part of the economy.*" They are certainly a vital and important part of the customer-base of our Members.

We also support the Government's red-tape reduction agenda given the flow-on benefits for small business and equally for the economy generally. A fundamental of this agenda is best practice regulatory reform that is designed to target evidence-based areas of market failure or consumer protection risk. While this has been espoused by previous Governments in recent times, we remain significantly concerned that our industry and others have been challenged with implementing change to be compliant with regulatory reform designed to protect small business but for which the underlying policy or rationale remains less than clear.

With almost 2 million small businesses in Australia, employing close to 5 million people, representing approximately 96% of all operating businesses in the country, with 50% of all employees and comprising 40% of GDP¹; we believe the small business sector deserves a thorough and rigorous identification of existing policy conflicts or gaps prior to implementation of any new regulation.

We are therefore encouraged by the moves of this Government to engage in open and meaningful consultation as a pre-cursor to reacting to address what are perceived rather than actual concerns of small business.

It is with this background that we make some general observations for the Government's consideration in preference to commenting on the specific issues raised in the Paper. In our view these more general matters are key to setting a foundation from which the Government could pursue the SBFEO role and are relevant to each of the focus questions posed.

What is a small business?

We appreciate this may appear trite. But, a key element of the Government's proposal is:

- Whether there is a need to set parameters to provide a class of entities that the SBFEO has the role to service; and
- If so, what those parameters are, and when are they to be tested.

For example, at its simplest, we understand that the role of the Australian Small Business Commissioner and the state equivalents, is to provide an avenue for an individual that is in business, in contrast to the individual in his/her personal life, to obtain information relevant to running that business and, where required, to provide a means of independent mediation or conciliation to endeavour to resolve issues between that business and another business (ie B-2-B complaints).

The Commissioners recognise that a business may have a range of legal forms, including sole traders, partnerships, unincorporated associations or companies. What is interesting, however, is that while the Commissioners' roles are labelled "small business", in our discussions with the State Commissioners, in particular, we understand that they see any B-2-B issue that falls within their broad remit of "*unfair market practices or commercial dealings*" potentially within their dispute resolution jurisdiction regardless of whether the business is able to establish that it meets a particular "small business" test or not. In effect, the role is one of dealing with B-2-B issues. Provided the complainant is able to establish that the issue is one relating to a business in which he / she is involved, no further interrogation or filtering is required before the Commissioner's Office focuses its resources on working to resolve the issue.

As a consequence, in our view it is therefore able to achieve its aim of being a simple, cost effective and otherwise accessible means for a business, through the engagement of an

¹ [Australian Small Business Key Statistics Report](http://www.innovation.gov.au/SmallBusiness/KeyFacts/Documents/SmallBusinessPublication.pdf) produced by the (Cwllth) Department of Innovation Industry, Science and Research published October 2011. Available through:
<http://www.innovation.gov.au/SmallBusiness/KeyFacts/Documents/SmallBusinessPublication.pdf>.

independent entity, to work to resolve a complaint with another business. Critical to this is that the mediators of the independent entity are appropriately trained and bring to the table business skills and acumen to be able to work with the complainant business and respondent business(es) to arrive at an resolution that works for all.

This therefore means that if, for example, one of our Members was of the view that another Member had engaged in unfair commercial dealings it could in theory take up its concern through a "Small Business" Commissioner and have the issue taken forward through that dispute resolution process. However, by removing "small" from the role this approach sees the potential remit of the SBFEO covering all entities (and therefore potentially all complaints from these entities) other than those of an individual(s) relating to his/her consumer or personal issues (ie true consumers). In such context, the additional \$6m allocated to the role may need revision.

Acknowledging the current budgetary constraints that may make this difficult for the Government at this time, it may be appropriate for the SBFEO to identify the non-true consumer entities that have been identified as warranting the "small business" protections (including advice / education) of the role. For example, is it the small single director proprietary company that warrants protection as opposed to a large publicly listed company? Do all small proprietary companies and similar entities (eg sole traders) warrant protection or should it only be those that are starting up, or that generate modest levels of revenue in a financial year, that are able to engage through the SBFEO?

If it is determined appropriate to set some parameters around who the SBFEO is designed to service, this then leads to difficulties around what key attributes should be used to set those parameters.

A further layer for consideration by the Government is that even if an entity may meet those attributes to be able to approach the SBFEO, that the availability of complaint-handling jurisdiction may require it to meet a different set of attributes before the "small business" is able to substantiate the "small business" complaint.

By way of illustration, a fundamental difficulty that we have encountered in moves by the former Government to provide protection for small business is having a clear understanding of the constituents or population at which the regulation is targeted. The challenge has also been that attributes have been used to set parameters in attempts to clearly define that regulated class of entities, but only to find that the attributes may change from one context of regulation to the next.

For example, under the Australian Consumer Law and ASIC Act, small business is defined according to the number of full time employees [FTEs]. This has also been the case in setting jurisdictional limits for External Dispute Resolution Services (EDRS) relevant to our Members, namely the Financial Services Ombudsman (FOS) and the Credit Ombudsman Service (COSL). Whether a business fits within this definition is relevant to determining whether it has a right to pursue consumer protection measures (including external dispute resolution) in relation to the acquisition of goods or services, including financial services. We submit that the number of FTEs is a test that, based on ABS data, potentially captures 96% of business entities in Australia. It may include a joint venture between BHP Billiton and RIO Tinto for example where the joint venture company employs less than 20 FTEs.

In contrast, APRA has a different measure of small business lending based around the quantum of amount of borrowing (ie \$1m) by the business.

Further, under the Privacy Act a small business is defined according to a monetary threshold (of \$3m) based on the annual turnover in a financial year. Again, it is critical for a business to know whether it meets this definition to determine whether it is required to comply with the APPs and other requirements (eg credit reporting provisions) under that Act to minimise risk of breach and significant sanction. This is equally relevant for an individual to know to determine whether they can pursue their rights of access and correction of personal information handled by that business, for example.

The Privacy Act attempts to provide facility for compliance to be tested at a point after commencement of a financial year.

This highlights a further issue for any test of whether an entity is a “small business” and that is questions around the point in time at which a business, or in our case our Member when providing finance to the entity, needs to consider whether the entity has those attributes and is a “small business”. For example, on start up an entity may employ less than 20, but a few years later, its ability to run at profit and grow, has enabled it to take on an additional 5 FTEs. Our Member may have had first contact with the entity at start up and at that time it would have met the test of a “small business” as it had FTEs of 20 or less. However, at the point that the entity may seek to complain about our Member’s lending activities to a relevant regulator or even an EDRS, the additional FTEs sees it fall outside a definition based on FTEs, if the entity’s attributes were assessed against the test at that time.

There are further complications that may depend on other attributes. For example, if the business was a farmer or the issue related to farming equipment or the issue related to a truck driver and his/her commercial vehicle, there are particular business protection mechanisms available to an entity that is of that particular type or the equipment involved is of that particular type (eg under the Australian Consumer Law or the Farm Debt Mediation laws).

The other challenge is the paradigm of a hierarchical system which may see any business as small when compared with another slightly less small business, again depending on the metrics used to establish that “smallness”. This becomes critical to regulatory design including the SBFEO role if the underlying assumption is that a business that is “smaller” than another is potentially in an unequal bargaining position when dealing with the other and consequently warranting protection. Equally this is relevant to another policy reform under consideration by the Government relating to the extension of the unfair contract provision protections to B-2-B standard form contracts.

In summary, therefore, we recommend a key area for the Government in progressing this proposal is to have a clear understanding of the constituent who is designed to benefit from the creation and role to be fulfilled by the SBFEO. We submit this is a pre-requisite and critical to more detailed questions around the design of the role including its functions, operation and appointment.

What is the cause of a B-2-B Dispute?

In considering the Paper, a principal reason for pursuing the SBFEO appears to be concerns around the amount of time that a small business may be distracted from its primary goal of running a successful and profitable business by disputes with other businesses. Again, we submit that this is a concern shared regardless of the size of the business or the industry in which it operates; not unique to the “small business” segment.

We also note the consideration of a range of work that has been conducted in recent years in relation to small business dispute resolution experience, including the statistical outcomes of the surveys conducted as part of the project conducted by the (then) Department of

Innovation, Industry, Science and Research. In our view, the Summary Report (June 2012) of the Orima Research, that shaped the findings of the Government's Australian Small Business Key Statistics Report, provides valuable information. We acknowledge that this work is referred to in the paper and is to be taken into account as the Government progresses this SBFEO proposal.

We nevertheless think it worthy to note a few key areas from this research. Of the approximately 2000 interviews conducted with small business:

- 80% of respondents (1 600 business or 4 out of 5 surveyed) noted that they had **not** experienced a dispute or disagreement in the last 5 years;
- Of those that had experienced a dispute (400 businesses), only 9% (36 businesses) indicated that the dispute was serious enough to result in third party involvement or legal action being taken by either business involved in the dispute. A significant proportion of the balance were either regarded as routine or minor – not something to worry about, or potentially serious but easily resolved without escalation. Those that required some form of intervention of a third party had available a broad range of third parties to utilise (detailed in some 20 pages in the Appendix to the report). We acknowledge in the Paper there is a suggestion that small businesses may not have been aware of this plethora of external dispute resolution facilities, which for us again highlights the issue of lack or awareness or education of small business of what protection and avenues to pursue it are available rather than a lack of protection or a need for further assistance providers. What is also very interesting is that only 0.9% of all businesses surveyed (ie 18 businesses) indicated that there was a perceived gap in the dispute resolution mechanisms available to small business at that time.

In relation to those that identified that they had a serious dispute that required escalation, the findings relating to the size of the business, the industry, the geographic location all provide interesting metrics.

But the key matters that appeared to be the reason for the dispute were a disagreement over:

- payment for goods or services (65% of the 36 businesses – 23 disputes);
- other contractual obligations (30% of the 36 businesses – 13 disputes).

And further, of those complaints:

- 45% were that a client was not able to pay the bill;
- 9% were that a client was unable to pay their bill due to bankruptcy or liquidation;
- 10% were that a respondent's client had been unhappy with their product or service (which we presume may have resulted in the respondent not meeting the contractual obligations with the complainant who provided the goods or services).

We question what if any assistance a SBFEO or any other third party may have been able to provide to assist resolve the issue on behalf of the complainant business in those cases.

The balance of matters relating to:

- Disagreements with suppliers over quality of the goods or services provided (27%);
- Breach of the terms of the agreement (20%);
- Erroneous charging by supplier (14%),

appear to be matters that the SBFEO might have a role in relation to. In the second category in particular, a critical means of addressing the issue and, we submit in preventing it and the balance of other issues, is a clear understanding of all contracting parties of the terms and conditions of their bargain or agreement.

We also highlight the statistics produced in annual reports of the EDRS – FOS and COSL – which consistently show that complaints by small business make up a minor portion of their total case management workload. In looking at the types of complaints, again, the majority appear to be matters where there has been a break-down in communication or a lack of understanding rather than any deliberate act or wrong-doing on the part of the respondent.

In fact, we submit that in the majority of cases a dispute between businesses arises from these few key issues:

- Economic conditions;
- Communication between the businesses - whether it is open and effective;
- Level of financial, business and legal literacy of the businesses.

In the experience of our Members, while economic conditions are strong, they are less likely to have concerns or complaints raised by small business customers.

Also, provided communication between the small business customer and our Member is able to remain open and effective, that generally escalation of a complaint is avoided with both parties working to achieve effectively the same outcome of remaining in business by being able to run a successful and profitable enterprise. Our Members acknowledge that small business customers, like any customer, may face challenges arising from a change of circumstances which may require some latitude to be shown in the short-term to facilitate the eventual repayment of the total finance provided. Provided the customer is willing and able to work with our Member to assist identify the cause of the problem, identify a reasonable means of resolving the problem without creating greater financial difficulty for the customer down the track, and then implement the agreed resolution, all parties benefit. Key to this is open and effective communication nonetheless.

A critical component of communication is a clear understanding of the terms of the bargain by both parties. And, this is where we submit, Government through the SBFEO can play a key role.

In our view, the key cause of small business complaints is lack of awareness or understanding of information and regulatory protections available, rather than gaps or inadequacies in the format of the regulation or information. Current regulation, coupled with additional resources being allocated to ASIC (eg for their MoneySmart website) and providing the SBFEO with responsibility of enhancing awareness and understanding of both business customers and businesses with whom they deal (including our Members), would provide better protection for the small business market and minimise the cause of B-2-B disputes.

Conclusion

In conclusion, while the global financial crisis towards the end of 2007 and through 2008 heightened the need for Government intervention to enhance market stability and ensure appropriate protection of traditional consumers, other Government initiatives (eg small business capital investment allowance stimulus package, ADI deposit guarantee) and the general stabilisation of the global markets has lessened the need for Government intervention to protect small business entities unless an evidence-based, regulatory / market failure has been established. Clearly, in the absence of such evidence, we are opposed to further regulation of lending to “small business” as a matter of policy principle.

The key area of focus for a SBFEO is that of educator and information-provision facilitator for business – regardless of whether it is a “small business” or otherwise. Through educating and informing business of their regulatory and contractual responsibilities, the SBFEO can play a key role in preventing or minimising escalation of B-2-B queries. Education including

a means for B-2-B communications to be open and effective including increasing awareness of internal dispute resolution mechanisms that are readily available in each of our Members' organisations and encouraging use of that facility as the primary means of resolving concerns.

Educating business to enhance understanding of the obligations that a contractual commitment brings with it together with the financial skills necessary to ensure on-going success and profitability of a business so that it is able to trade through varying economic conditions is equally paramount for the SBFEO. In this way, other components of the role become far less relevant. In particular, in our view by educating and informing both potential complainant businesses and respondent businesses, the SBFEO is able to minimise the risk of a customer query dealt with inappropriately at first interface with the other contractual business party to escalate into a dispute between two parties that become entrenched in positions largely based on lack of understanding often inflamed by lack of communication and requiring an independent third party to intervene to remove the intransigence and re-open communication flows.

We would be happy to explore this further with the Government through the Minister for Small Business or your Department. Please feel free to contact me via email through ron@afc.asn.au or our Corporate Lawyer, Helen Gordon, helen@afc.asn.au or both by phone through the AFC Office 02 9231 5877.

We also look forward to continuing to work with the Government to provide input on steps to take forward decisions it makes in relation to the SBFEO role.

Kind regards.

Yours truly,

A handwritten signature in black ink, appearing to read 'Ron Hardaker', written in a cursive style.

Ron Hardaker
Executive Director

Attachments:

List of AFC Members; AELA Members; DIFA Members; AFLA Members



AFC MEMBER COMPANIES

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AlliedCredit
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ANZ t/as Esanda
Automotive Financial Services
Bank of Melbourne
Bank of Queensland
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180 Group

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Polczynski Lawyers
Trace Personnel
Gregory Clayton, Barrister & Solicitor**

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Australian Fleet Lessors Association

Incorporated - ABN 78 059 998 533

AFLA MEMBER COMPANIES

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