

THE IMPACT OF THE DIGITAL ECONOMY ON SMALL BUSINESS

Speech to Digital Technology Convention, Melbourne, 28 November 2012 by
Geoff Browne, Victorian Small Business Commissioner

Thank you for the opportunity to speak with you at this important conference.

You have already heard this morning, and will continue to hear over the course of this conference, expert commentary on the digital economy, technology, convergence, and the NBN rollout.

Let me say that I am not an expert in any of these technical areas. However, the fundamental structural changes that the digital revolution is having and will continue to have on the way business is conducted, and how businesses respond to the risks and opportunities presented, is something I can make some observations about.

My comments today will therefore be geared towards the implications of the emerging digital economy on you as small and medium businesses – not the immediate contracting opportunities arising from the NBN rollout, but the implications for businesses of all types, whether technicians, retailers, contractors, trainers, etc. of these significant changes to the way in which business is, and will be conducted.

Markets continuously change, and businesses have always had to adapt to these changes to remain successful. In this regard, the digital economy emergence is no different from any other changes to market structures and dynamics over the years – new customer demands, new channels of information and communications, new payment systems, new product opportunities continuously emerge.

There are certainly characteristics of the digital economy that are unique to it, and businesses need to adapt to these.

However, there are also some pretty basic requirements of running a successful business which apply regardless of any market transformation.

Today I plan to look at three areas:

Firstly, I will provide an overview of the role of the Victorian Small Business Commissioner.

Secondly, I want to consider the opportunities and risks to small and medium businesses presented by the emergence of the digital economy;

And thirdly, I want to note some of things that don't change with the digital economy – your legal rights and obligations, and trying to run a successful business. In particular I want to share with you some research undertaken by my Office into some key characteristics critical to business success – regardless of market changes occurring from time to time.

The Role of the Victorian Small Business Commissioner

The role of Commissioner was established by its own legislation in 2003. It is a statutory role, providing independence to the activities undertaken.

The objective of the *Small Business Commissioner Act 2003* is
*‘to enhance a competitive and fair operating
environment for small business in Victoria’.*

It’s interesting that the legislation does not define ‘small business’, nor does it define what constitutes ‘a competitive and fair’ operating environment.

Accordingly, previous Commissioners, and I, have taken an expansive view of the scope of the role.

Under the Act, the Commissioner has some 13 functions. Three of these are:

‘to facilitate and encourage the fair treatment of small businesses in their commercial dealings with other businesses;

To promote informed decision-making by small businesses in order to minimise disputes with other businesses; and

To receive and investigate complaints by small businesses regarding unfair market practices, and mediate between the parties in the dispute’.

Over the past 9 years, our role has increasingly focused on dispute resolution – assisting businesses to resolve disputes with other businesses, or government, without recourse to litigation. A large part of the reason for this increased focus has been the introduction of three additional pieces of legislation which statutorily require disputes to come to me for attempted resolution before they can be progressed through the Tribunal or the Courts.

These additional laws cover Retail Leases, Owner Driver disputes, and Farm Debts where the farmer is in default.

While at first glance these areas may not appear of any relevance to you, I would suggest that our role under the Retail Leases Act is relevant to any of you who lease business premises and sell goods or services to the end users of those goods and services. Retail premises are very broadly defined, and chances are that any dispute between you as a business tenant and your landlord falls under that Act. The good news is that we have a high level of success in resolving those disputes without the matter escalating to litigation, and we do it quickly, and at no cost or low cost.

In each of the past two years, my Office has received formal applications for assistance in resolving over 1500 business disputes. Since 2003, we have received over 10,000 applications for assistance with business disputes. These include general commercial disputes covering:

- Franchise disputes
- Supply chain disputes
- Agency or distribution agreement disputes
- Lease disputes (retail and non-retail)
- Even partnership and shareholder disputes.

The claimed amounts in dispute total over \$1 billion since 2003.

The main method we use to resolve business disputes is mediation, although we are quite successful in resolving many disputes prior to mediation through shuttle negotiation. Around 30% of applications are resolved through such early engagement, at not cost to either party. Of those matters that progress to mediation, around 80% have reached settlement. We charge just \$195 per party for a 3-4 hour mediation, conducted by an independent, expert mediator. Parties can bring along legal representation, or represent themselves.

We generally schedule mediations within 4-6 weeks of receipt of an application for assistance, but can also accommodate urgent matters if the parties are agreeable. Compare this with a typical 6-8 month delay for matters at VCAT or the Courts.

Resolving disputes quickly, and at no cost or low cost, makes business sense. It enables you to get back to doing business, and avoid the uncertainty, emotion and distraction of drawn out litigation processes, as well as the likely escalated costs of that litigation. It is also more likely to enable the parties to reach win-win terms of settlement, and continue their business relationship, rather than the usual win-lose outcome of litigation.

So if there is one message I'd like you to take away from this session, it is that we offer a quick, effective and low cost dispute resolution service for any commercial dispute between businesses.

The Digital Economy and Small Business – opportunities and risks

I'd now like to turn to my second key theme – opportunities and risks arising from the digital economy. Firstly, let's look at the opportunities.

Opportunities for small businesses

I'm not talking about the primary reason you are here today – to win some of the business associated with the rollout of the NBN. My focus is not on the opportunities arising from the development of the digital infrastructure, but the opportunities arising once the infrastructure is in place.

More generally, I want to look at how you as small and medium businesses can take advantage of the digital age – whether at speeds we've had access to in recent years, or greater speeds we will have access to after the NBN rollout.

There are some in this audience keen to provide training and services to small and medium businesses on the use of the internet. How many of you, here to capture some of the business from the rollout of the NBN, are also putting your names down to attend training in how to utilise the internet more effectively, or to understand your

customers and your markets better in the digital age? Have you considered how your business can take advantage of the infrastructure you are looking to roll out?

Opportunity is often the 'other side' of risk. If you don't take the opportunities emerging, I can guarantee that others will. And those taking the opportunity will leave the laggards behind.

You may have seen the old cartoon depicting two men running from a bear, and one stops to put on his running shoes. The other says 'you can't outrun the bear, even with running shoes'. The response is 'I don't need to outrun the bear; I need to outrun you!'

Imagine you and your competitors as the two men, running away from market changes imposing major challenges to the way you've always done your business, and the running shoes as the embrace of the digital economy. You need to move faster than your competitors to stay ahead of, and take advantage of, the dynamic marketplace that is emerging.

So what are the opportunities?

As a supplier of goods and services, you need to make sure your offering is known to potential customers. While some businesses have embraced an 'on-line only' model, many have adopted a multi-channel communications and distribution strategy. Increasingly the internet is being used as a search tool to find and compare offerings. If you are not on the list, you will not stand a chance.

In a recent presentation for the Westfield group, Jon Stine from CISCO stated that:
"In a growing number of industry segments, internet search is influencing 50% or more of revenue. The internet is the front door of your brand."

ABS 2010-11 statistics¹ show that nearly all large businesses had a web presence, compared with just one-third of micro-businesses (0-4 employees). In Victoria, where there are some 465,000 micro businesses, that means that a lot of small businesses are simply not on the list when buyers are searching online.

And while only a small percentage of transactions currently occur online, if you are not part of the online search, you are far less likely to be involved in the transaction.

There is an increase in the proportion of transactions being undertaken online.

The ABS data also shows that Australian businesses received online orders worth \$189 billion in 2010-11, up 32% from the year before. Twenty eight percent of businesses reported receiving orders via the internet, up 13% from 2009-10. Perhaps surprisingly, around half of the businesses in the wholesale and manufacturing sectors received online orders, while the retail sector was in sixth place at 35%.

¹ ABS 8166.0 Summary of IT Use and innovation in Australian Business, 2010-11

Further, fifty one percent of Australian businesses reported placing orders via the internet in 2010-11, a 9% annual increase.

And that data is now over 18 months old.

The underlying trends and the behaviours of internet users must inevitably affect all forms of business.

Your customers – whether consumers or businesses - will be embracing the digital economy, and will expect suppliers to be digitally capable. The emerging cohort of ‘digital natives’ – those who have never known life before the internet, google, amazon, apps, and so on – will be entering the workforce in the next few years, profoundly influencing markets as consumers, but also as employees and managers in businesses purchasing all manner of goods and services. Generation Ys (born 1980 – 1994) will be one third of the Australian workforce by 2020. They expect access to and use of the internet in their daily life – from social media to smart phones and clever apps – and expect information instantly.

The ABS reported earlier this year that 90% of Australian children aged 5 to 14 accessed the internet in the preceding 12 months. It was 65% in 2006.

So the opportunities are to understand what your current and emerging customers want, and outrun your competitors through well implemented channel strategies.

A recent report from American Express and Galaxy Research² found that small businesses engaged in e-commerce activities were 33% more likely to be profitable in 2011-12 than those that weren't, and one in five businesses stated that social media helped grow their business in that financial year - further compelling reasons to embrace the digital economy.

Increasingly, businesses will be looking at greater efficiencies in procurement and contract management. If the client expects the head contractor to implement online solutions to make contract management and project management more efficient, guess what the head contractor will expect of its sub-contractors, and so on down the contract chain.

This recent article from The Age highlights this point. It says that Minter Ellison is planning to roll out an Australian version of a contractor claims processing system in January next year. The web-based system aims to replace paper invoicing from individual contractors with electronic management of payments. It is claimed that about one third of the commercial construction sector in North America use this particular system.

You can embrace these opportunities, or they become risks to your business success. As stated³ by the Commonwealth Government earlier this year:

² Cited at dnbsmallbusiness.com.au/News/Online_strategies_drive_small_business_profits, downloaded 7 November 2012.

³ As stated at digitalbusiness.gov.au on 2 August 2012, downloaded 7 Nov 12.

“a lot of businesses that don’t harness the opportunities offered online could fail to reach their full potential.”

As a purchaser, your business can also benefit from the digital age. As the customer, you can search for products and services more efficiently and across a wider pool of suppliers. How are you going to respond to the current or potential supplier who does not offer the online service levels you expect?

While putting yourself in the customer’s shoes is helpful in considering how you as a supplier need to respond, don’t forget that you may not be the best judge of the new ‘digital consumer’s’ expectations. Are you going to close your mind to the new consumer’s requirements (and their business), or embrace the opportunity, even though it may not be the way you have traditionally done business?

The previously mentioned American Express survey noted that a significant proportion of firms – mostly in the construction, finance, insurance and health industries – found that selling their products and services online is irrelevant. Issues raised included customer privacy concerns and problems setting up on-line payments. However, it is interesting to question whether these dismissals of the relevance of the internet to these businesses was based on informed and strategic judgement of customers and markets, or based on a level of comfort with the past ways of doing things.

The changes emerging from the digital economy are, in one sense, no different from any other market shifts over past years. Consumer preferences change, technology changes, different generations bring and expect different ways of doing things. What is different is the magnitude and speed of the changes accompanying the digital revolution.

The first internet browser was created only in 1993 – less than 20 years ago. I recall working for one of the major banks in the late 1990s, leading the implementation of this new thing called on-line banking. The first business case proposed two connection channel options – via the internet, and via a dial-up telephone connection. In the space of twelve months, the dial-up option was discarded, and the focus put on this new internet channel. It was new, unknown, risky, and cutting edge. And that was barely 12 years ago. The pace of change of internet and computer speeds, new applications and access to a global market in the past decade has been phenomenal. Put on the running shoes or get left behind.

Risks

Let’s turn now to business risks arising from the digital age. I’ve argued that there is little alternative but to embrace the digital economy. However, just like any market shift, there are new or modified risks to be aware of.

The competition risk is clear. Purchasers can search via the internet for goods and services traditionally sourced locally, or from known suppliers. You need to consider ways in which you can run ahead of your competitors, and present your offering to your customers to enhance their value and better meet customer needs and expectations.

There is a changed business risk, arising from a broader potential market of customers and suppliers. Will you be paid for the goods and services provided to unknown or distant customers? Will the goods and services you order be fit-for-purpose? Will your payment and identity details be held securely? What after sales service is offered?

The use of social media has also amplified the implications of good and bad customer service. The old adage was that one customer experiencing poor customer service told five others. These days, poor customer service is broadcast over social media channels to thousands of potential customers. Somewhat ironically, the digital economy is making good customer service even more important to a business' success.

These are not new risks for businesses dealing online, but they are likely to increase as businesses enter the online space for the first time, and will become increasingly important for all businesses to manage effectively.

There are costs of utilising the online channel. You will need a modern and maintained web presence and probably a payments system. You will need to ensure your customers' details are secure. There are costs inherent in building and maintaining new capability to embrace new opportunities.

Online scams are a particular example of business risk. Usually these are digital versions of tried and proven 'physical world' rip-offs. Unfortunately, the low costs of scamming online make it a very easy thing for scammers to start.

The best protection against scams is to be alert to their possibility, and avoid engaging. Scammers are often based overseas, making any follow up and enforcement extremely difficult, although the ACCC in particular leverages links with similar international organisations to try to stop these scams.

I thought I'd mention some of the more common online scams to watch out for.

Phishing (with a p-h) refers to emails allegedly from a trusted source (often a bank, government agency, or the like) asking you to log onto 'their' website via an email link to verify your details. These are high quality fake websites which look remarkably like the websites of the alleged source organisation. They will typically have a slightly different URL - possibly just one letter different from the real thing - which can easily trick the user. These scams aim to capture your login details, credit card details and passwords. If you click on the links, they may also cause some code to be down loaded to your computer, such as key loggers to record the key strokes of bank account details, or otherwise interfere with your computer and data.

Reputable companies do not ask for information from you via email in this way. If in doubt contact the alleged source organisation to confirm whether the email is genuine. Generally, just delete these emails and notify the source organisation.

A related scam is the Computer Repair scam. The phone caller will say they are from Microsoft or another reputable IT company, and they've discovered that your computer has been infected by a virus. All of your data will be lost unless you log

onto a website (allegedly the Microsoft website, but it will be another similar looking site that downloads code onto your computer). Alternatively, they may ask for money for software to download to fix the problem, which may in fact cause a problem where none existed.

Another common scam is the Advertising Scam. While not solely online, it involves an outstanding invoice sent via email, fax or letter for advertising in a publication. The publication may not exist, and no order requesting advertising has been placed, yet often these bills can be inadvertently paid

Other scams include the URL registration scam, where the invoice to renew your URL is fraudulent. Businesses can pay these quickly to avoid their website being deregistered (or so they believe).

These scams are somewhat more sophisticated than the Nigerian Lotteries scam, and have the added problem of extremely low operating costs. Each letter offering you a million dollars from the Nigerian Lottery at least costs a stamp to send. In contrast, the close-to-zero cost of an online scam means that many people can be affected at virtually no cost to the scammer.

Faster internet connections can only be a boon for online scammers. Again, the best defence is to be aware of the risks, and not engage.

There is a website – scamwatch.gov.au - operated by the ACCC and other government agencies which provides updates on the latest scams circulating.

While it's not an online scam, I thought I'd bring to your attention a new scam, called the Fee Fishing Scam (that's fishing with an 'f'), only recently brought to my attention by ASIC.

The scam relates to accessing finance by small businesses. The lender produces a Letter of Offer without regard to the strength of the application. The Letter of Offer includes an array of fees and charges and the applicant is obliged to pay as part of the terms in the Letter of Offer. The fees and charges are often out of proportion to any work reasonably undertaken in assessing the application, and more importantly, there is no actual assessment of the likely success of the application, despite assurances to the contrary. The applicant is therefore surprised when the application is rejected, and the lender puts a caveat on the business' property to chase its fees and charges. The lenders involved are usually private mortgage lenders or 3rd or 4th tier lenders introduced via brokers. So watch out for these Fee Fishing scams, and notify ASIC if you come across any such offers.

Returning to the online world, faster online connections can also be expected to boost business opportunities for developers of websites and applications. While most such businesses will be genuine, there is potential for online scams to emerge in this area.

My Office has dealt with a number of disputes between businesses and web designers, where both businesses are genuine. You should take reasonable precautions such as making sure your requirements are clearly defined and agreed in writing, cost and time are agreed with payments based on work completed, and where possible seek

word of mouth referrals – which sounds very old fashioned in the digital age, so maybe the contemporary version of word of mouth is to check online blogs and other online sources. Of course, you still face the challenge of determining if the online source is reputable and reliable.

Business rights and obligations under the Australian Consumer Law

I'd now like to turn to my third theme – there are things that don't change for businesses in the digital economy.

Firstly, your legal rights and obligations.

Just because you use the digital economy for information, communication or transactions does not affect your obligations under the law. What was the Trade Practices Act was changed in January 2011 to the Australian Competition and Consumer Act. This provides, amongst other things, obligations on you when dealing with consumer customers, but also provides rights to businesses as consumers in certain circumstances.

Some of the key obligations you have to your consumer customers (which may be individuals or businesses) to be aware of include:

Guarantees

Under the Act, your business automatically provides your customer with a basic set of statutory consumer guarantees when they purchase your goods or services. These guarantees cannot be excluded or limited, and apply regardless of any express or manufacturer's guarantee or warranty.

Consumers with a problem with goods or services provided are free to approach the seller, the manufacturer or the importer to seek a remedy, and businesses cannot tell them otherwise.

The remedy will depend on the circumstances but may include a repair, replacement or a refund, or having the service performed again.

'Consumers' may be a person or a business, provided that:

- The goods or services costs up to \$40,000; or
- The cost was more than \$40,000 and the goods and services are normally used for personal, domestic or household purposes; or
- The good is a vehicle or trailer used mainly to transport goods.

The guarantees do not cover goods purchased for resale or to be transformed into other products.

These statutory rights apply to you as a business when you sell, and in many cases to you as a business when you buy – whether online or not.

There are a range of obligations under the Act relating to guarantees including

- Goods must be of acceptable quality, fit for any disclosed purpose, must match their description, must match any sample provided or demonstrated. A manufacturer or importer must also guarantee that repairs or spare parts will be provided for a reasonable time.
- Services must be provided with due care and skill, be fit for any disclosed purpose, and must be provided within a reasonable time of purchase (unless otherwise agreed).

Further, if you offer an express or manufacturer's warranty, it must by law include prescribed wording saying, in effect, that it does not exclude the operation of statutory guarantees under the Competition and Consumer Act.

Some other requirements of the Act include:

Proof of transaction

Businesses must provide proof of transaction for goods or services valued at \$75 or more, or for lower amounts on request.

Unsolicited sales

It is illegal to request payment for goods or services that the customer has not agreed to buy.

False or misleading statements

It is illegal to make incorrect statements to customers, or statements that are likely to create a false impression. It does not matter if a false or misleading statement was intentional or not.

The ACCC has an excellent brochure titled 'Small Businesses and the Competition and Consumer Act – Your rights and responsibilities' which is available from their website.

Characteristics of Successful Business Relationships

I'd now like to highlight another aspect of your business which is important whether you are dealing online or not – forming and maintaining successful business relationships.

In 2007 my Office commissioned Deloitte to undertake an Improving Business Conduct Study. The aim was to identify those behaviours that underpin successful business-to-business relationships, and to consider the arguments for adopting such behaviours.

Desk based research was complemented by interviews with Australian business leaders and other stakeholders.

Many well known, successful businesses and organisations were involved in the research.

Business leaders were unanimous in the assertion that:

‘successful business-to-business relationships improve commercial outcomes for all parties, by decreasing costs and increasing competitive advantage’

Successful business relationships do not just happen. Rather they require a commitment to some key behaviours as you form and maintain relationships.

A clear consensus emerged that there are seven main characteristics of successful business-to-business relationships. Each is integral to long-term, mutually beneficial and sustainable relationships.

The seven key characteristics identified were:

1. The **ALIGNMENT** of the values and ethics of a business internally with the day to day behaviour of its employees, and externally with its chosen business partners
2. A **COMMITMENT** wherever possible to a long-term relationship rather than a one-off transaction.
3. The recognition that working towards a common goal based on **MUTUAL INTERESTS** is the best way to achieve a profitable and sustainable outcome for all parties.
4. The need for clear, transparent and frequent **COMMUNICATION** to ensure that all parties fully understand the other’s position, that obligations are met, and that any issues or problems are raised early.
5. All parties recognising that they are **ACCOUNTABLE AND RESPONSIBLE** to the other for the success of the relationship.
6. That **PROFESSIONAL CONDUCT** occurs in all interactions between all parties.
7. And there is rapid and satisfactory resolution of disputes or issues through **PRE-AGREED DISPUTE RESOLUTION PROCEDURES**.

The pre-agreed dispute resolution procedures are of particular interest and importance to me. I would encourage any business entering into a contract with another business, in Victoria, to include reference to mediation in any dispute resolution escalation process, as a low cost, quick and effective means of resolving disputes without having to incur the cost and formality of arbitration, or litigation. I would further encourage specific reference to my Office as the independent provider of that mediation service. On that point, earlier this year I wrote to NBNCo alerting them to the services provided by my Office and encouraging them to incorporate our services into contracts relating to the rollout of the NBN in Victoria. With Small Business

Commissioners also in NSW, WA and SA, an equivalent arrangement could apply in those States.

It is pleasing that I recently received a response from NBNC Co, including details of their primary contractors involved in the rollout. I have written to all of these primary contractors alerting them to the services of my Office, and encouraging them to include mediation through my Office in any contracts relating to the rollout in Victoria.

The seven best practice behaviours support successful business-to-business relationships, which lead to improved commercial outcomes through competitive advantage and decreased costs.

Competitive advantage derives from the enhanced reputation of parties pursuing, and known to pursue, good and ethical business practices.

Lower costs arise through more efficient interactions and transactions, reduced switching costs, and early identification and resolution of disputes when they arise.

The full report can be downloaded from our website at sbc.vic.gov.au/publications

Conclusion

To conclude, I encourage you to embrace the opportunities of the emerging digital economy in your own businesses, watch out for the online scams, understand your legal rights and obligations, assess your behaviours against the seven key characteristics of successful business relationships, and decide how best you can stay ahead of your competitors.

And if disputes arise with another business, remember that my Office provides quick, successful and low cost dispute resolution services for any commercial dispute.

Thank you.