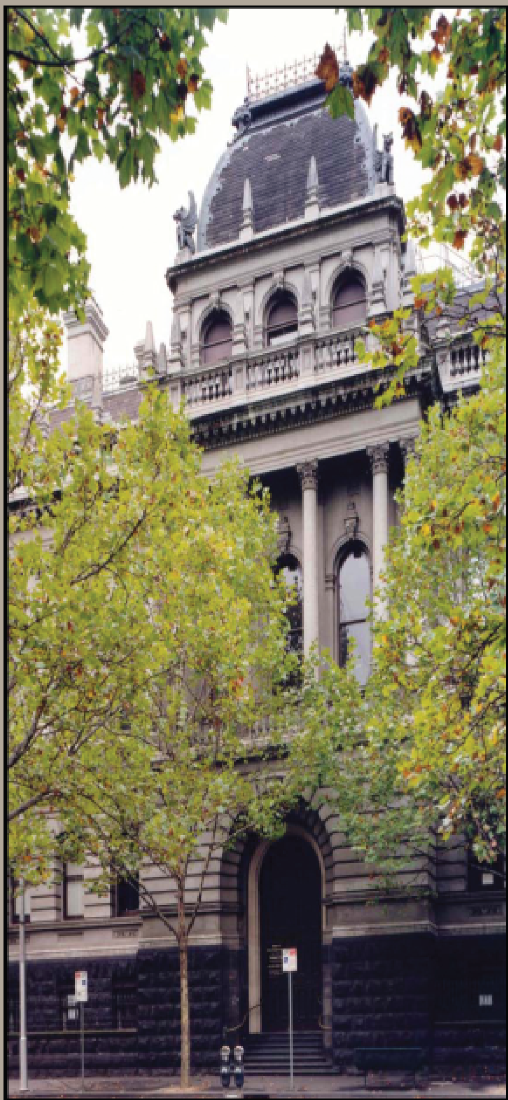

Developing a Responsive Regulatory System for Australia's Small Corporations: Governance for Small Business

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Melbourne

Australian Government Department of the Treasury
Council of Small Business of Australia
Australian Research Council

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- The Australian Federal Government Department of the Treasury
- The Council of Small Business Organisations of Australia (COSBOA)

Project Partners:

- University of Western Sydney
- Corporate Governance Group, School of Law, Victoria University
- School of Law, Centre for Labour Market Research and Faculty of Information Sciences and Engineering, University of Canberra
- University of Technology, Sydney
- School of Commerce and Management, Faculty of Business and Law, Southern Cross University

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Australian Research Council Linkage Grant

Abbreviations

ACCC	Australian Competition and Consumer Commission
ACCI	Australian Chamber of Commerce and Industry
APRA	Australian Prudential Regulation Authority
ASIC	Australian Securities and Investment Commission
ASX	Australian Stock Exchange
ATO	Australian Taxation Office
BRTF	Better regulation Task Force
CEO	Chief Executive Officer
CGT	Capital Gains Tax
COAG	Council of Australian Governments
COSBOA	Council of Small Businesses Organisations of Australia
GDP	Gross Domestic Products
GST	Goods and Services Tax
NIA	National Institute of Accountants
OECD	Organization for Economic Co-operation and Development
PAYE	Pay As You Earn
SBRT	Small Business Research Trust
SME	Small Medium Enterprises
STS	Simplified Tax systemsVAT Value Added Tax
VACC	Victorian Chamber of Commerce and Industry

Australian Research Council Linkage Grant

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Executive Summary

1. The project was made possible though the support of:

ARC Linkage partners:

Australian Research Council

The Australian Federal Government Department of the Treasury

The Council of Small Business Organisations of Australia (COSBOA)

2. The significance of the project

Australia's small corporations play a vital role in national economic and social wellbeing. They comprise more than 99% of all firms, employing more than 5 million people. In the past, their regulatory needs are largely ignored because regulation is aimed at large listed firms. This is particularly true in respect to the Corporations Act. However, the sequence of disasters affecting businesses in Australia, natural disasters such as droughts and floods and economic flow-on from the impacts of the GFC, have drawn attention to the role of small business in stimulating the national economy. One consequence is that governments are increasingly seeking ways of both reducing the burden of regulation on small corporations and using regulation to enhance their efficiency and contribution to the national economy.

No previous study has investigated the impact of corporate regulation directed at regulating the governance of Australia's small corporations by the Corporations Law.

3. The purpose of the project

This purpose of this project is to develop a responsive regulatory model for small corporations drawing together the experiences of small corporation owners/mangers, CEOs of industry associations, regulators, the Federal Treasury, industry leaders and academic experts.

The scope of this study was restricted to compliance with the governance requirements of the Corporations Law and to corporations defined as ‘small’ under the Corporations Act and that are not public or listed companies.

The analytical framework of the study (Refer to Chapter 5) suggests that Government regulation promulgated in the Corporations Law impacts on the small business sector. The response to the regulation, evident in internal governance mechanisms, is mediated by the context in which a business operates. The aim of the regulation is to facilitate small business performance which, in turn, has implications for the performance of the economy.

The aims of this study, stage two of the project, were to determine what are the factors which inhibit or promote good governance in small corporations and what kinds of regulation, or some other approach, will best achieve the desired outcomes.

The research questions were:

What were the key governance issues that were a problem for the operation and growth of small business?

What is the aim of corporate governance regulation of small corporations?

What could the regulators do to improve regulation of small corporations?

What are the real issues that inhibit efficiency and effectiveness in small businesses?

4. Methodology

The research was conducted in four stages. The first stage was designed to identify the theoretical stances found in previous research that would support the appropriate design and direction of the regulation of small business. To this end, a literature search and a bibliography of related studies was compiled. The third stage of the project is a major survey of small business owners and the final stage will be to determine the response of the regulators to the proposals emerging from the research.

This second stage study was a detailed analysis of the small business sector and interviews with the CEOs of small business associations and owner/mangers of small corporations (Details of the sample are in Chapter 6). The study was designed to determine what the small business sector contributed to the national economy and what were the key issues related to regulation that are emerging for small business in Australia today. The results of this study, the second stage of the project, are the subject of this report. They provided a basis for the further investigation of the issues through a survey of small business corporations and interviews with the relevant regulators.

5. What is a small corporation?

Corporations in Australia are regulated by the Australian Securities and Investment Commission (ASIC). Section 112, Corporations Act 2001 (Cth). Several amendments to regulations to meet the needs of small businesses can be found in Part 1.5, a Small Business Guide.

The definition of small companies adopted in this study is that of s45A(2) Corporations Act 2001 (Cth): corporations with less than 50 shareholders which meet at least two of the following criteria: consolidated revenue of less than $25 million per year; gross assets of less than $12.5 million; fewer than 50 full-time employees.

6. Profile of small business in Australia (Chapter 2)

Chapter two of this report describes the small business sector and its importance to the Australian economy. Nearly 1.4 million companies employ more than five million members of the Australian workforce. They represent over 98% of all corporations and of these approximately half are sole proprietors and partnerships. Ninety four percent of small businesses have a turnover of less than $2M but together small and medium contribute over half of the value added by business to the Australian economy.

The major employers are in retail trade, manufacturing and construction. The most profitable small businesses are professional services, manufacturing and construction.

The characteristics of many individual entities are: a small market share; owner owned and managed; often family owned; and closely associated with independence and entrepreneurship. Their weaknesses are succession; dependence on external expertise for advice; very susceptible to major economic fluctuations.

7. Regulation of small business (Chapter 3)

Chapter three discusses what is meant by regulation, the recent reforms to regulation in Australia, the major theories of regulation, the burden of regulation for small business, and some example that illustrate some of the difficulties associated with regulation.

Regulation can be categorised by their regulatory content as social, economic and administrative. Primary regulation is enacted through acts of Parliament and endorsed by legal sanctions. Quasi or co-regulation is promulgated through statutes and other regulations and often involves those who are being regulated. Implementation is related to the type of regulation. For example Acts of Parliament such as the Corporations Law are prescriptive, and apply to all. Performance based regulation offers some flexibility related to the ability of a corporation to comply.

The main theories that determine the design and purpose of regulation are public interest, private interest and institutional theories. Governments are increasingly engaging in institutional theories to support the involvement of industry in self-regulation. The argument is that it reduces administration costs for government and the rise of unintended consequences for business.

8. Governance (Chapter 4)

Governance and regulation are intimately related. Corporate governance is concerned with the internal structures and processes for decision-making, accountability, control and behaviour at the top of organisations and external mechanisms for accountability. The purpose of regulation of corporate governance is to reduce risk and maintain order and confidence in the corporate capital market and to safeguard the investments of shareholders. Regulation of the governance of corporations in Australia is largely captured in the Corporations Law. All companies in Australia are registered under the Corporations Act 2001 which is administered by the Australian Securities and Investment Commission (ASIC).

Small corporations act in isolation and often in ignorance of their governance obligations. The demands of the business are constant and a first priority of owners/managers who regard regulatory compliance as a distraction from their core business.

The main difference in the Corporations Law between the regulation of large and small companies relates to the level of disclosure by the companies and the requirement for large companies to produce formal audited accounts. Governance also differs significantly in small corporations from that found in larger corporations in respect to size, resources, level of employment, directors' perceptions of their role, decision making authority, family business structures, independence of board chair and CEO/manager, use of independent directors, diversity and accountability.

9. Assessment of corporate governance practices in small corporations (Chapter 7.1)

Corporate governance in the context of this study referred to the provisions of the Corporations Act, particularly the Replaceable Rules and aspects of the Law which had been simplified for the regulation of small businesses, plus some aspects of best practice governance as recommended by the ASX guidelines. The Laws referred to are the formation and structure of a board, the appointment and independence of directors and the direction and accountability exerted by those in control. Best practice guidelines recommend boards with independent directors, the separation of ownership and control, appropriate skills and diversity of directors, succession plans, a code of conduct and record keeping and information disclosure.

The first section in this chapter describes the incidence of best practice governance in place in small corporations. The second section describes the perceptions of difficulties that small businesses encountered with the governance regulations.

Constitutions and Replaceable rules

Two thirds of the small businesses had their own constitution while three stated that they used the Replaceable Rules. In general, respondents were not familiar with the Rules and left all governance matters to their accountants.

Board Structure

The research found that few of the small businesses operated with a board, and sub-committees were rare .There were almost no independent directors and little separation of the management and board. Where boards were formed they met two to four times a year.

For many small businesses, a board was reported as 'not applicable' or not necessary. A board became necessary when a company had more than one shareholder or grew to the stage of appointing a separate manager. Shareholders usually took a seat on the board due to the need to exercise control over their investments.

Directors

In response to questions to the small business owners about "Directors" many did not appear to recognise that as the single 'owner/manager' they were also the 'Director' responsible under the Corporations Law.

Qualifications of directors

The qualifications of those were CEOs of their small business associations and small business owner/managers varied. Several of the Association CEOs had tertiary qualifications. Among the small business respondents, two had professional qualifications but most relied upon business or commercial experience. There were no female respondents and only one respondent saw any value in ethnic or gender diversity on boards.

Succession plans

Less than 25% of small business members have a succession plan. Where there was one, the plan was most likely to be directed towards the senior management or the owner manager position.

Monitoring performance

Two areas that could (a) promote good governance and (b) monitor results are a code of conduct and independent auditing. Half of the small businesses were reported to have a code of conduct, only two of the twenty one respondents reported that their entities were audited.

Disclosure

Small corporations keep disclosure of their financial performance private and provide information to their accountants to meet taxation and financial requirements.

Less than 25% of their small business members have a succession plan.

10. Governance related difficulties experienced by small corporations (Chapter 7.2)

This section examines the extent to which the regulations meet the needs of small business and where there are difficulties, how the respondents suggested that these could be improved. It also describes the sources of advice to small businesses and the use of information and communication technologies (ICT), as these have a bearing on future communication between government and small businesses.

Corporate registration

Compliance with the corporate regulations was in many cases left to accountants. The difficulties encountered were:

time frames for reporting are “too short”

the penalties disproportionate compared with an offence.

ASIC is too inflexible for small business management

ASIC should send out notices confirming charges applied by a bank

ASIC and ACCC language is confused and convoluted.

ASIC provided poor phone advice and

ASIC was not tune with modern IT.

Directors Duties

Major difficulties for small business members with regards to **directors’ duties** include:

- Rules for the directors are so difficult to understand;
- lack of awareness of owner/managers’ directors duties;
- A good deal of concern about the level of liability/criminal sanctions regarding directors, ASIC assumes that directors understand their responsibilities;
- Too much accountability requirements, and
- A limited ability to fund directors can hardly attract high quality directors.

Proposed Solutions:

The government should clarify and simplify their rules with regards to the directors’ duties and educate the directors. Funding the industry associations could provide training to directors.

Regulation

The major problems with governance regulation were:

Small business:

- lack of knowledge of the regulations by small business;
- lack of understanding of the regulations by small business;
- lack of appreciation of the difference between the owner/manager and the company as a separate entity;
- lack of understanding of what it means not to comply with directors duties and governance regulations;
- lack of skills in dealing with regulators;
- reliance on accountants or lawyers and the costs involved.

Regulators:

- Inappropriateness of regulation to small business.
- Lack of understanding by ASIC of small business points of view resulting from poor communication, resulting in poor compliance
- Government has failed to communicate efficiently with small corporations about orporate governance;
- The regulation and corporate governance requirements are intertwined; businesses find it is difficult to capture the latest requirements.

<u>Proposed Solutions:</u>

a) Government should streamline registrations and regime to assist small business. Previous processes for change have never resulted in improvement. Government efforts are misplaced.

b) ABR Blog looks good- lots of money thrown at it- but take up seems to be very low. Government should develop programs suitable for small businesses.

c) The regulation requirements, in particular the law, needs to be stabilised and consistent. For example, labour law and health & safety regulations are changing so frequently that it is very difficult for industry associations to follow.

d) Second is unified requirements between the States: i.e. adoption of unified definitions in legislation; adoption of standard business reporting; and adoption of uniform hours among the states.

e) Third is streamlining the requirements of tax administration and other reporting requirements.

f) Governments should improve communication with the industry and small businesses.

Record Keeping

Major difficulties small businesses face with regards to record keeping include:

- Rules for record keeping are complex to understand and follow;
- Keeping records is time consuming;
- Lack of the skill set to prepare financial documents requires small businesses to use accountants.

Proposed Solutions:

a) Simplify the requirements of record keeping for small businesses and facilitate training of small businesses with techniques suitable for them to use for compliance purposes.

b) The government should fund small business industry associations or professional associations to communicate the changes of regulations rather than letting small businesses bear the cost of keeping up to date or of non-compliance.

c) Greater flexibility should be given to small businesses when it comes to auditing issues, because reporting is not their core business.

11. Difficulties incurred with different regulatory regimes (Chapter 7.6)

The major difficulties were:

- access to finance;
- tax administration
- interest rates;
- anticompetitive practices.

Also rated as difficult for the respondents

- labour relations and
- crime

Government was reported to be slow and difficult about paying small business for work undertaken, and did not adhere appropriately to agreed contracts.

Confusion regarding labour relations and awards was destabilizing for small business.

The new Foreign Investment Review board policy requiring employers to report on their own staff would be inappropriate and destabilizing for small business.

Proposed Solutions:

a) Federal government – provide more supportive export grants;

b) State government- ease the paper work;

c) Employee superannuation and parental leave management could be handled through the tax office.

12. The burden of compliance (Chapter 8)

The burden of compliance refers to the costs incurred by small business in meeting the demands of regulation. The cost of compliance to the small business sector is estimated to be $17billion.

The CEO respondents indicated that up to a month of their time costing at least $20,000 is spent each year on compliance. Over half the small businesses did the same.

The answers given by the respondents reflect the difficulties and the perceptions that regulation duplication should be reduced, that the imposition of similar regulation on small and large business was inappropriate and unfair. Some respondents identified problems specific to their industry, such as the costs of auction regulation to estate agents.

A Chi Square test of significance showed that there was no statistical significance between the answers of the two groups of respondents.

13. Factors which inhibit or promote the performance of small business (Chapter 9).

The performance of small business is impacted by various externalities that include taxation, the direction of regulation of utilities, and access to finance. Government response to the sector depends on the ability of small business to influence government, on the level of access to government., the relationship of government with industry, the latter most often represented by industry associations.

Internal factors which can promote performance are high levels of skills and knowledge by owner/manager/directors, their expertise in the use of information and communications technology (ICT), and ability to obtain information and advice. This is to some extent dependent on their relationship with and the quality of their sources of advice and information, professionals such as accountants and lawyers and their industry associations.

Emerging issues that will be important in the future are the environment, social networking and social responsibility.

14. Conclusion (Chapter 10).

This chapter identifies the limitation of the study, the issues that emerged for further exploration, and the next steps in the research.

The study is limited by the number of respondents. Nevertheless, those CEOs who participated were selected for their expertise and the positions that they hold as leaders of the various associations which are members of the Council of Small Business Associations. Similarly, the small business respondents were selected for their expertise and in-depth knowledge of small business.

The next steps in this research are a Small Business Forum to confirm with the Small Business sector the important issues that should be addressed by regulators and how they should be addressed. At the same time the research team will be seeking a larger sample with randomly selected respondents so that the results can be analysed with greater reliability. Following the Small Business Forum, the conclusions will be put forward for the regulators to assess.

Some of the options for policy makers that emerged from the study and that are expanded upon are:

- Actions by Government
- Changes to inappropriate regulations for the small business sector
- Improve government communication with the small business sector
- Improve ASIC inflexibility
- Address small business lack of knowledge and understanding of governance

Some of the issues that emerged in relation to the Corporations Law were:

Should the regulators reduce the ‘staying incorporated’ time and costs for small corporations? How could this be done? Should the small business definitions be expanded? How can the corporations Act be made more ‘user friendly’ for small businesses”

Should entry to business be made more difficult? Should there be character or competency requirements for directors? Should the $2 capital threshold be raised to something more meaningful?

How can we obtain better information about small businesses? Can definitions be made consistent across all governments and regulatory authorities? Should ABS conduct a regular census of small businesses?

"Small business was the engine room of the economy and that was a truth based on the quantifiable contribution of small business to our country". — Kevin Rudd[1]

Chapter 1

Introduction

1.1 Introduction

This research is one of a number of studies into the small business sector conducted by a consortium of researchers from five universities. The research in this project was stimulated by the interest of the Australian Department of the Treasury in addressing concerns observed by the Australian Productivity Commission (2006) in regard to the difficulties of compliance with regulation expressed by the small business sector.

This research was supported by an Australian Research Council Linkage Grant and the Industry Linkage Partners, the Australian Treasury and the Council of Small Business of Australia (COSBOA). The Victorian Chamber of Commerce and Industry (VECCI), The Victorian Automotive Chamber of Commerce (VACC), The Australian Institute of Company Directors (AICD), and the MICRO supported the project by encouraging the participation of their Members.

"Small corporations" make up the vast majority of the Australian market, some 1.38 million companies, and are vitally important in economic, social and cultural contexts. They employ more than five million members of the Australian workforce (National Office for the Information Economy, 2007). They are referred to as the 'engine room of the Australian economy' (Clarke, A., 2007, Emerson 2007). Regulators and scholars are yet to agree upon a simple definition of a small corporation, however, they do agree that small corporations can include: one person firms, family firms/ businesses (Romano and Smyrnios 1996; Spender

[1] The ex-Prime Minister Kevin Rudd addressed in the 2009 Virgin Blue National Small Business Summit, http://www.mybusiness.com.au/administration/resources/files/pdf/NSBS09_report.pdf.

1997; Fehlberg 1997), SMEs (small and medium enterprises), and small proprietary companies (Cassidy, 2005, 33). The range of small corporations is therefore numerous and complex.

For the purposes of this research, small companies are those with less than 50 shareholders which meet at least two of the following criteria: consolidated revenue of less than $25 million per year; gross assets of less than $12.5 million; fewer than 50 full-time employees. This definition derives from s 45A(2) *Corporations Act 2001* (Cth).

Small businesses are more severely affected by red tape than large companies because they are less proficient in dealing with regulation because of its complexities and are unable to spread the costs of compliance across large-scale operations (Chittenden, Kauser et al. 2003). Regulation is considered the essential component of governing. It is one of the main instruments that lawmakers use to implement national policy outside of taxing and spending, and it is through regulations that society can minimize environmental damage, produce quality products, and help maintain a safe workplace (Green 2002).

As the complexity of regulations increases, the financial impact of the regulations increases. The fixed-cost nature of the regulation creates an environment, where the regulatory costs are disproportionately borne by small businesses (Green 2002). However, it can be argued that small businesses generate benefits for the whole of the economy and should be promoted by government policies (Freedman 2003).

This research examined the corporate regulation of this vast and vital group of companies. It explored the current governance frameworks, assessing if they are responsive and indicative of world 'best practice.'

Its aims were to determine how to simplify the regulation of the governance of small business corporations in ways that will enhance the efficiency of both government regulation and small business. In particular the purpose of the research was to:

1. Identify and document the organising principles adopted by the regulators of Australian corporations in order to control, govern and regulate small corporations.
2. Identify and distil the particular Federal regulatory requirements relevant to the growth and expansion of small corporations.
3. Develop a map of the most effective regulatory framework to assist and enable optimum performance by small corporations.

4. Link item 3 to a law and policy reform agenda.

1.2 Design of the study

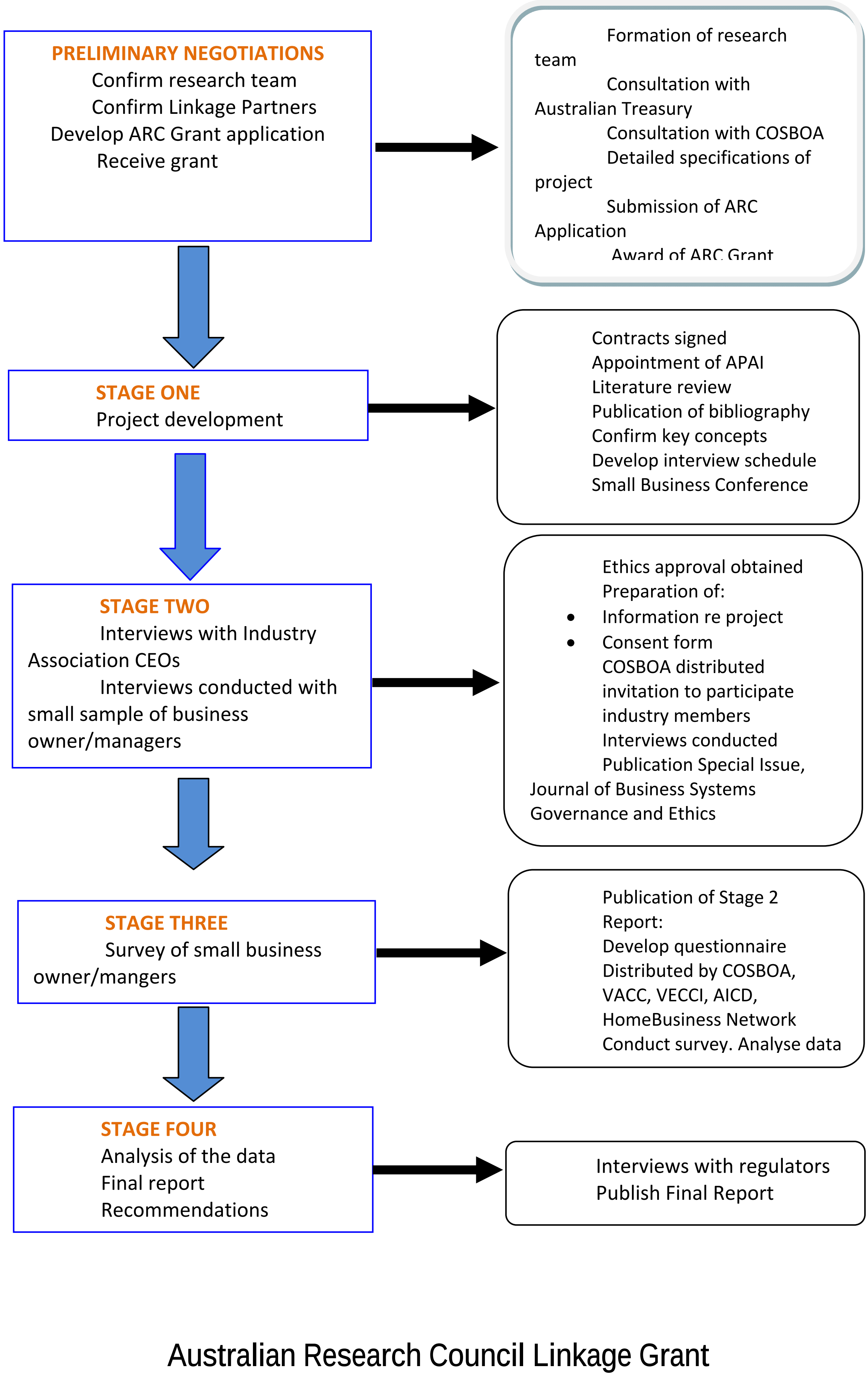
The research was conducted in four stages Figure 1). The first stage was designed to identify the theoretical stances found in previous research that would support the appropriate design and direction of the regulation of small business. To this end, a literature search and a bibliography of related studies was compiled. The third stage of the project is a major survey of small business owners and the final stage will be to determine the response of the regulators to the proposals emerging from the research and make recommendations that can promote not only less but new or ‘other’ ways of regulating small business.

The second stage study was designed to determine what the small business sector identified as the key issues related to regulation that are emerging for small business in Australia today. The results of this study are the subject of this report. To avoid confusion, this report will refer to the research titled , *Developing a responsive regulatory system for Australia’s small corporations*, as the ‘project’ and to this part of the research as the ‘study’.

Interviews were held with the Chief Executive Officers of twelve associations that are members of COSBOA and nine of their constituent small business members. The CEOs of the associations volunteered to take part and nominated the small business owner/mangers participants who were their members known for their expertise in their businesses and interest in the issues that affect small business. It should be pointed out that not only are the industry associations knowledgeable about the issues confronting their small business members, they are small businesses themselves and their CEOs are well able to identify with the problems faced by the small business sector.

Despite the fact that over 90% of businesses in Australia are small, big business is exciting and dominates the attention of government. A search of the Australian Government’s web sites illustrate how little government interest is invested in small business. However, the global financial crisis has renewed interest in promoting small business because of its potential to drive economic growth.

Figure 1. 1 Design of the study.



It is possible that the election of members of parliament who are independent of the major parties, and who now hold the balance of power in the Australian Government, is due in some measure to the previous lack of attention by both major political parties to the needs of the small business operators in both the urban and rural sectors. Indeed, the current attention by political parties and the media to the small business sector is an indicator of its importance to economic recovery from the global financial crisis (GFC). Small businesses are frequently described as the “engine of growth in the economy” (Rudd, 2009) and the Australian Treasury recognises this by its support for this project into the future direction of regulation of the sector.

While previous studies of small business have addressed various issues of concern, a primary aim of this study was to investigate how the Corporations Law affected the governance of small business and their operations, and whether changes to regulations in this area could assist the small business sector.

1.3 Significance of the Project

This project has arisen out of the interest and involvement demonstrated by the Federal Department of Treasury, in terms of investigating the key issue of the regulation of the governance of small corporations. Several studies of the burden of regulation (see for example, Industry Commission 1997, Productivity Commission 2006) have been conducted in response to Federal and State government policies to reduce the burden of regulation. Most of these studies have surveyed a large sample of corporations from all sectors of the economy. None have specifically targeted small corporations nor investigated the impact of the Corporations Law on small business.

Small business not only accounts for 96% of all Australian businesses but also 13-18 per cent of any electorate (Australian Broadcasting Corporation, 2010).

In addition to political influence, there is also the clear potential for this study to contribute to national economic benefit: nearly 1.4 million companies employ more than five million members of the Australian workforce (National Office for the Information Economy, 2007). The aims of this project therefore deal with matters of political, economic and social importance that effect the working lives of many millions of Australian employees, and their families (Patmore 2003).

The practical benefits of the study are to free small corporations of unnecessary regulatory burdens in relation to Corporate Laws. This will assist in making them more productive, more efficient and more mobile in terms of their growth and development strategies.

In terms of the Government's Research Priority 4: Safeguarding Australia and Understanding our region and the world, this project has the potential to enhance Australia's capacity to interpret and engage with its regional and global environment through a greater understanding of languages, societies, politics and cultures, in the context of the critically important small corporation economic sector. The research approach enhances Australia's capacity to engage with the ASEAN region and beyond by adopting a leading edge approach to research and by formulating a new set of regulatory practices that can be used for training in developing economies, and for comparative analysis in developed economies.

The results of the research will inform the Australian Treasury policy decisions that affect small business.

1.4 Theoretical significance

Factors determining the performance of large corporations are well researched and documented in the existing literature in disciplines such as Law, Economics, Human Resource Management, Organisational Design and Public Policy. However, the fact that small corporations are always exceptions in mainstream research, establishes the gap in the theoretical research into the performance of small businesses. Equally, rigorous theoretical foundations for corporate governance and government regulation of small corporations are also rare in the prior research. Thus, the development of theories for small business productivity, government intervention and growth is a real need (Productivity Council 1997). The ground breaking research from this project is attempting to fill in this gap.

Due to lack of application of a theoretical basis and the measurement difficulties of small business performance, empirical research into small corporations has been constrained Specifically, the logical relationships between corporate governance, government regulation and performance of small corporations have yet to be adequately explored. This study draws on theories of governance (chapter 3) and regulation (chapter 4) to develop a theoretical framework (chapter 4) to guide the direction of its research.

1.5 The purpose of this study

Previous studies of small business have addressed numerous issues of concern to small business in both developed and developing countries: governance (Francis and Armstrong 2003; Clarke and Klettner, 2009), information technology and reporting (Heenetigala and Armstrong 2010), family businesses, (Craig, Moores et al 2009), leadership (Muenjohn, Armstrong et al 2010), succession (Ip and Jacobs, 2006), access to finance (Abor and Adjasi 2007), entrepreneurship (Taylor 2007)), more recently, corporate social responsibility (Banerjee and Duarte, 2010) and various aspects of regulation (Bradford, 2004; Chittenden et al 2002). However, research into the implications of the regulation of corporate governance through corporations laws has been scarce. The primary aim of this research was to address this gap by determining how the Corporations Law affected the governance of small business and their operations, and whether changes to regulations in this area could assist small corporations.

The purpose of this exploratory study was, therefore, to determine the critical regulation issues that were important to the small business sector in relation to the corporations law and their governance. In particular, the study was designed to answer the research questions:

- What were the key governance issues that were a problem for the operation and growth of small business?
- Was the Corporations Law, as it now stood, appropriate for small business?
- How does it affect the governance of small business?
- What were the factors that promoted or inhibited compliance with the Corporations Law?
- Were there were changes to corporate regulation that would facilitate the growth and success of small corporations?

A second purpose of the study was to ensure that the next stage of the Reducing Regulation project addressed the issues that were of primary concern to the small business sector, and to build these into the questionnaire that was used in the third stage of the project, a large survey of small business owner/managers.

1.6 Methodology

This report describes the research undertaken in the second stage of the ARC project to investigate the regulation of the governance of small businesses in Australia. The following describes the selection of the procedure in the study, the sample, data coding and data analyses.

1.6.1 Procedure

Approval for the project was obtained from the Victoria University Human Ethics Committee. Information about the project and participation consent forms was sent to respondents.

Two semi-structured questionnaires were developed and used in telephone interviews to collect data from both industry associations and small businesses. Demographic data were collected about two sample groups. However, the industry associations were asked to provide their views about the governance in their members, the small business associations provided data about their own businesses.

Approximately one hour interviews were conducted with the respondents in person or by telephone. As small business owner/managers are noted for being ‘time poor’ personal interviews were deemed the best approach. Two interview experts were recruited to undertake the interviews. Both of them are native English speakers and experienced in communicating with senior executives in organisations.

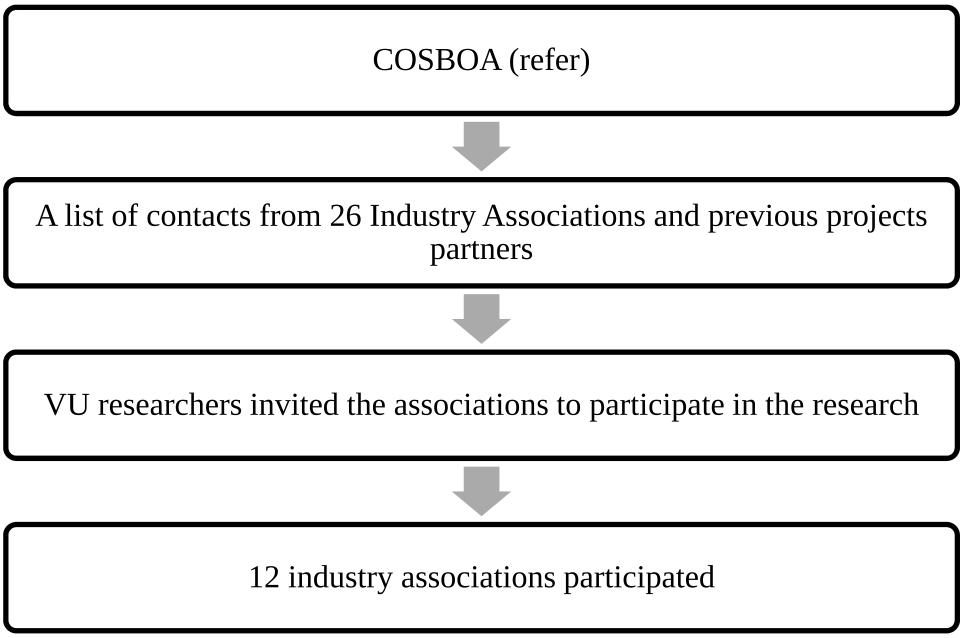
1.6.2 The Sample

A realistic challenge for this type of research is to generate an effective sample in terms of the extent of representativeness and participation. The collaboration of this research group with Federal Department of Treasury and COSBOA and the support of several organisations enabled this research to obtain a representative sample and achieve the comprehensive participation of the representatives of small corporations.

Two samples were selected for the study, an industry association sample and a sample of small business leaders. In the industry association sample, COSBOA introduced the project to its 26 member associations. The research group contacted the industry associations as well as three other small business associations that the research group invited to participate in the study. The sample of 12 business associations responded were interviewed. The sample selection process is shown in Figure 2a.

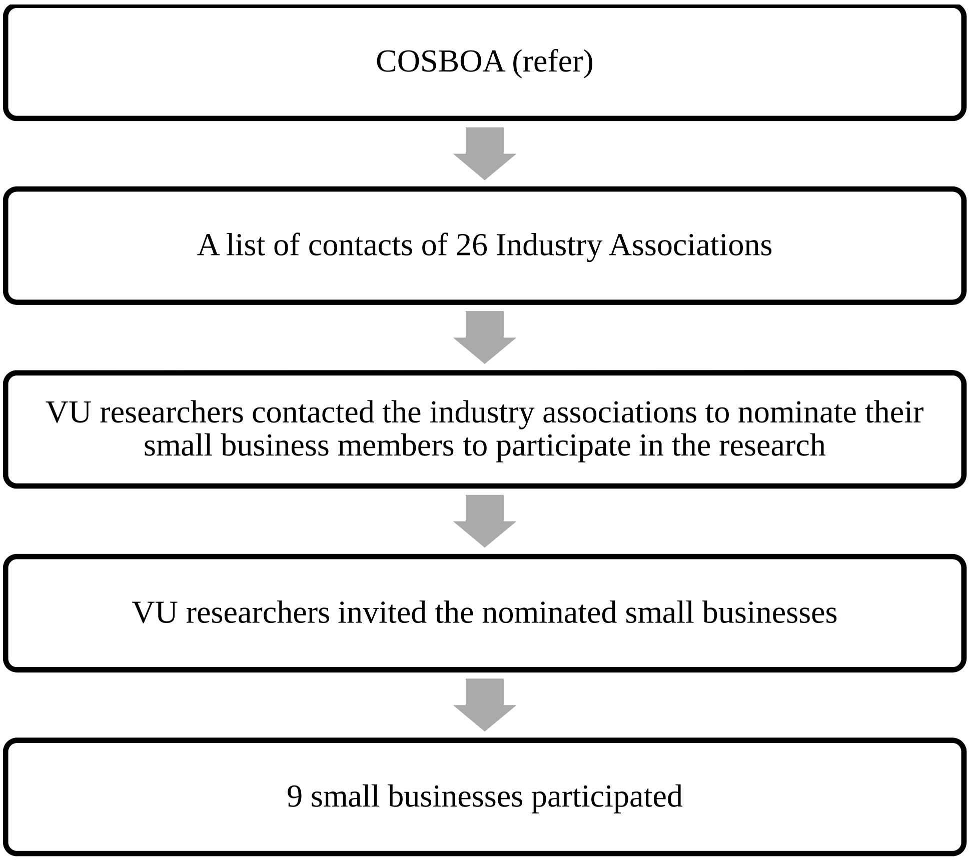
Eight associations out of the twelve associations interviewed were national level organisations. Three respresented businesses operating at both the state level and the federal level, three were Victorian based and each of other three associations represented businesses in Queensland, Western Australia and Tasmania.

Figure 1. 2 Selection of the Industry Sample



A two-step approach was adopted to generate a sample of small businesses: the first step was to contact the industry associations which were members of COSBOA and ask them to nominate a small business member whose mangers had confirmed that they were interested in participating the research; and the second step was to contact the nominated small businesses and invite them to participate

Figure 1. 3 Selection of Small Business Sample



The purpose of selecting a convenience sample was to focus on those who would have in-depth knowledge of the issues that affect small business. Although the samples were small they were representative of small business and well able to identify the issues being targeted by this study. The two samples included in the study provided an opportunity to determine whether the views of the owner/mangers of small businesses differed from those put forward by their Associations.

1.6.3 Quantitative and qualitative data coding

All the interview records were manually entered into SPSS database as a master dataset. The maintenance, decoding and other transformation of the variables are all based on the master dataset.

1.6.4 Data analysis

SPSS was used to analyse the quantitative data. The analysis required descriptive statistics and comparison of statistics between the two sample groups. The qualitative data were content analysed to allow the major issues and themes to be identified. Comments indicative of the views of respondents are reported below[2]. While the structure and purpose of the association CEOs and the small business owner/managers, where their responses were similar they were combined. No significant differences were found in their views of the costs of regulation, as indicated in chapter 9.

1.7 The structure of this report

The focus of this report is small business in Australia. Chapter two describes the small business sector and its importance to the Australian economy. Chapter three defines what is meant by regulation and the regulation that impacts on small businesses. A conceptual framework for the study is presented in chapter five. Chapters six presents descriptive statistics from the study. Chapter seven directly addresses the major research question: What is the impact of current regulation on small business. The major regulatory issues raised by small business are answered in Chapter eight together with a comparative analysis of the views of the two samples on the research question of the costs incurred by governance regulation. Here, the report compares and contrasts the interview results between these two groups, identifying similarities and discrepancies which merit further investigation.

Chapter nine turns to the core of the study by identifying the difficulties small businesses face dn the factors which promote or inhibit the delivery of appropriate regulation.

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[2] Given that the sample size is small, an explorative analysis approach was used to summarise the key finding in the qualitative data. For the second stage of the research when the sample size is large, a standardise software package, i.e. Nvivo, can be used for the analysis.

The final chapter draws together the conclusions from this study. It identifies the major issues on regulation, both difficulties and solutions, emerging from the study. In response, it presents some policy options and initiatives in relation to the actions of government, changes to inappropriate regulations, ASIC flexibility, and addressing the lack of knowledge and understanding in the small business sector.

These pose questions for further investigation that will be addressed in the next stages of the project. A Small Business Forum will present the results of this study to the respondents and representatives of the sector. A larger survey of small business corporations and interviews with regulators will confirm that these are the real difficulties faced by the sector as a whole and whether the proposed policy 'solutions' are ones which will meet the objectives of both regulation of the sector and reducing the burden for small business.

Chapter 2
Small Corporations in Australia

2.1 What is a small corporation?

This chapter reviews the small business sector in Australia and its role in promoting economic growth.

Businesses vary in size from the small corner store to large multinationals with turnovers exceeding the national income of some small countries. The focus of this study is small business, but small corporations are not large businesses scaled down or even, necessarily, small in size before they become big. They have their own economic and management characteristics.

Small Business can be a sole proprietorship, a partnership or a company. Academics and policy makers have looked for objective definitions of small business. Among the variety of criteria used to define small business are total net worth, relative size within the industry, number of employees, value of products, annual sales or receipts and net worth (Cochran 1981) have been employed. Because of the range of definitions that have been used, it is extremely difficult for researchers to matchup different small business studies (Burgess 2002).Micro businesses are a special type, of very small businesses. SMEs are a combination of small and medium sized businesses. Therefore what is classed as small in one study may be medium in another and large in yet another study (Burgess 2002).

Often the issues that face small businesses are dealt with under the heading of small and medium sized enterprises (SMEs). But issues that arise in relation to small business are different to medium sized businesses. Therefore Freedman (2009) refers to small business as an "owner-managed business with ten employees, whatever its legal form".

Among the major studies of small business in Australia, the first was conducted by the Small Firms Research Group at the University of Newcastle between 1973 and 1975 (Johns et al 1978). For the purpose of their surveys the criteria for inclusion in the study was the size of a business. A manufacturing business was considered small if it employed fewer than 100 persons; a non-manufacturing business was considered small if it employed fewer than 30 persons.

There were a host of different definitions used in studies in Europe. The term ‘SME’ was coined by the European Commission (EC). SMEs have since been divided into very small micro-enterprises (0 to 9 employees), small enterprises (10 to 99 employees) and medium enterprises (100 to 400 employees). The EC definitions were based on some research results. British research indicates that the operations in SMES change with a growth in the size of their workforces. For example, the introduction of non-owner managers tends to occur when firms have between 10 and 20 employees, and that sub-contracting firms with less than 10 employees tend not to have formal contracts with their customers (Storey 1994).

In several Asian countries, (for example Thailand, Indonesia, Malaysia) small enterprises were defined by their number of workers and the level of assets. In contrast, definitions of SMEs in the US varied from industry to industry. The UK and Australian definitions took into account the number of employees, turnover and assets.

The Australian Bureau of Statistics (ABS 2005) defines a small business as one that employs less than 20 people and a medium business as one that employs between 20 and 200. It also considers a smaller category of business as a ‘micro’ business if it employs less than 5 employees. As the ABS is the source of most statistics about small business, the ABS statistics quoted in this report relate to small companies which employ less than 20 people.

The stimulus for the present study was the interest first expressed by COAG in 1995 into reducing regulation in Australia. No previous study has investigated the impact of the regulation directed at regulating the governance of small corporations by the Corporations Law.

Corporations in Australia are regulated by the Australian Securities and Institutions Commission (ASIC). Section 112 *Corporations Act* 2001 (Cth) provides for the registration of public or proprietary companies. Small businesses are largely proprietary companies i.e. privately owned. Unlike public companies proprietary companies cannot seek capital from the public and are limited in their number of shareholders to 50.

A company, as a ‘registrable body’ under Australian law, can be inexpensively and quickly established under s117 Corporations Act 2001. There are no credit or character tests of key personnel or requirements for positive proof of honesty or business acumen. The asset test at $2 is nominal. The first set of information recorded as part of the entry price includes the firm's name, registered address, first directors, secretary, constitutional documents and so forth. Small proprietary limited companies need to have a registered office; it does not need to be open to the public. Under the small business guide they need to notify changes in these to ASIC. They are also required to keep financial records under sections 286-291 but auditing of these by small corporations is not required. Both small and large companies need to keep minute books which comply with Pt 2G.3 and company registers which comply with 2C, s271. Neither small nor large companies need to hold AGMs or to make continuous disclosure (these requirements are applied by the ASX to listed companies).

The incorporation documentation is lodged with ASIC and the fee is paid. The company comes into existence at the beginning of the day on which it is registered as per s119. The company then exists as an entity separate to its members.

In 1995, as part of the *First Corporate Law Simplification Act*, it was first proposed that proprietary companies would be divided into small and large. Several amendments to regulations contained in the Act can be found in Part 1.5, a Small Business Guide that summarises the main rules that apply to small businesses. The major differences between the main provisions of the Act and the Guide are that if there is a single shareholder/director, Replaceable Rules and meeting rules do not apply, annual reports do not have to be submitted to ASIC, and a resolution can be passed by the single director recording and signing the resolution.

By 2007 the definition of small proprietary companies was based on satisfying two-out-of-three criteria in a financial year. These were:

- consolidated gross revenue of less than $25 million;
- value of consolidated gross assets less than $12.5 million; and
- fewer than 50 full-time equivalent employees.

This is the definition of a small corporation adopted in this study. Under this definition, around 98 per cent of Australia's 1.6 million proprietary companies are classified as small and, with some exceptions, do not have to prepare annual financial statements and lodge them with ASIC. However, there are over 30,000 small and medium companies which must meet the full regulatory requirements (Miller, 2009).

2.2 The characteristics of small corporations

The characteristics that are identified with small business (Francis and Armstrong, 2006) are:

- They have a relatively small share of their marketplace. They often operate in only one location servicing local customers but may have operate in a niche market or be part of a franchise.
- They are usually owned by one person, or a small number of individuals, often linked by family ties. Because of this, although many are registered as companies, ownership is often restricted and takes the corporate form of sole proprietorships or partnerships. These latter forms leave the small corporate without the protection of limited liability.
- They are privately, often family owned. In the USA family businesses represent 35% of all businesses, in Europe over 50% (Faccio and Lang, 2002) and in Asia over two-thirds of businesses (Claussens et al 2002).
- They are managed by owners, often owner/managers who make all the critical management decisions and undertake many of the management functions such as financial management, personnel, marketing and production that might be distributed in a larger corporation.
- Succession in ownership and management is often a problem (Reference Hartel, Bozer and Levin 2009)
- They may have resources constraints. Access to financial and other resources is often a major constraint (CPA, 2008).
- Because an owner/manager undertakes most management roles without the support of internal specialists, the small business is often dependent on other professionals such their accountant or lawyer for advice (Heenetigala and Armstrong, 2010)
- Small business is closely associated with entrepreneurship and innovation (Muenjohn et al 2010).
- They are independent, in the sense that they are not part of a larger enterprise. In fact, some are deliberately kept small because their owners value the life style associated

with “less hassles, less politics, more flexibility and better work-life balance (Rudd, 2008).

Small business, is very susceptible to major economic fluctuations. In difficult times, such as the Global Financial Crisis (GFC) they are the suppliers, the creditors and customers at the end of the corporate value chain. As a consequence they suffer the most from credit crunches, the loss of revenue, the loss of skilled staff and uncertainty in customer production and service demands.

2.3 Small business in Australia

There are approximately 1.99 million active small businesses in Australia (Table 2.1, ABS 2010). They represent ninety six percent of all businesses, employ over 5 million people, and account for around fifty one percent of private sector employment. Small businesses contribute over one third of Australia's total GDP.

Table 2. 1 Small business in Australia

Industry	Number of Small corporations in each industry(000,000)	Percentage of Number of Small corporations to Total number of Enterprises	Number employed in each industry	Percentage of employment in Small Corporations
Agriculture, Forestry and Fishing	202,341	10.19%	60,608	7.67%
Mining	7,558	0.38%	3,219	0.41%
Manufacturing	87,842	4.42%	49,006	6.20%
Electricity, Gas, Water and Waste Services	5,362	0.27%	2,569	0.33%
Construction	339,469	17.10%	128,372	16.25%
Wholesale Trade	74,106	3.73%	39,734	5.03%
Retail Trade	136,234	6.86%	78,323	9.92%
Accommodation and Food Services	72,275	3.64%	50,414	6.38%
Transport, Postal and Warehousing	141,982	7.15%	50,509	6.40%
Information Media and Telecommunications	17,486	0.88%	7,130	0.90%
Financial and Insurance Services	148,556	7.48%	35,319	4.47%
Rental, Hiring and Real Estate Services	216,611	10.91%	31,453	3.98%
Professional, Scientific and Technical Services	229,157	11.54%	105,707	13.38%
Administrative and Support Services	73,580	3.71%	33,033	4.18%
Public Administration and Safety	7,666	0.39%	3,721	0.47%
Education and Training	22,684	1.14%	10,298	1.30%
Health Care and Social Assistance	90,725	4.57%	45,405	5.75%
Arts and Recreation Services	26,938	1.36%	8,703	1.10%
Other Services	84,987	4.28%	46,290	5.86%
Total	1,985,559	100.00%	789,813	100.00%

Source: ABS (2010)

In Australia, not only is small business a source of economic activity but the sector is expanding rapidly. The past two decades saw a four-fold increase in the number of small and medium enterprises (SMEs) from 577,100 in the financial year of 1983-84 to more than two million in 2007. One can equally say that one person out of ten in Australia owns his/her own business[i]. SMEs accounts for about 99.71% of all private sector entities, while large firms never exceeded 1% of aggregate firm numbers during 1983-2007 (Australia Bureau of Statistics 2007).

2.4 Employment of Australia businesses

Given that the ABS definition of small business is inconsistent with the definition of small businesses in the Corporations Act and only data under the ABS definition is available, here the employment situation of small, medium and large businesses are summarised by industry (ABS 208-9).

In total, small and medium businesses employ approximately 71% of the workforce in Australia. In particular, small businesses who employ less than 20 employees, account for more than 47% of the whole labour force.

Table 2. 2 Employment of Australia businesses

Number of employees ('000)	Agriculture, Forestry and Fishing	Mining	Manufacturing	Electricity, Gas, Water and Waste Services	Construction	Wholesale Trade	Retail Trade	Accommodation and Food Services	Transport, Postal and Warehousing	Information Media and Telecommunications
Small	431	21	326	15	743	210	490	399	269	35
Medium	71	26	309	19	150	196	215	191	98	32
Large	13	89	373	73	136	149	562	166	217	108
Total	515	135	1,008	108	1,030	555	1,266	756	584	175
Percentage	5.15%	1.35%	10.08%	1.08%	10.30%	5.55%	12.66%	7.56%	5.84%	1.75%

Table 2.2 Employment of Australia (Continued)

Number of employees ('000)	Rental, Hiring and Real Estate Services	Professional, Scientific and Technical Services	Administrative and Support Services	Public Administration and Safety	Education and Training	Health Care and Social Assistance	Arts and Recreation Services	Other Services	Total	Percentage
Small	286	530	275	17	79	283	72	286	4,764	47.65%
Medium	52	213	199	23	143	241	46	106	2,331	23.32%
Large	33	178	258	25	76	344	53	48	2,901	29.02%
Total	371	922	732	66	298	867	172	439	9,997	100.00%
Percentage	3.71%	9.22%	7.32%	0.66%	2.98%	8.67%	1.72%	4.39%	100.00%	

Source: ABS (2008-9).

Table 2. 3 Legal status of businesses in Australia 2007-2009

	2007	**2008**	**2009**
Companies	662,183	670,956	670,951
Sole Proprietor	641,633	620,492	605,015
Total Partnerships	394,389	378,798	360,228
Trusts	375,130	400,677	414,020
Total	**2,075,342**	**2,072,931**	**2,052,223**

Source: ABS (2008-9)

2.5 Legal status of businesses in Australia

Legal registration requirements do not require businesses to report the number of employees that they hire. Thus the cross tabulation between number of employees and the legal status of business registration is unavailable. To get an estimate of the legal status of small businesses, Table 2.3 provides the distribution of all Australian businesses by legal type. Among various legal forms, small businesses include the entire sole proprietor, partnership firms, and a large proportion of companies and trusts. Of the over 2 million small entities, 32% are registered companies, 29% are sole operators and 17% are partnerships. Eighty percent of these are micro-businesses that include self-employed persons and 0-4 employees. There is a high level of ‘chrrn’ within the SME sector. In Australia, 334,000 new businesses started trading in the 2006-7 financial year and 286,000 enterprises ceased operating. From 2007 to 2009, the number of companies and trusts slightly increased, while the number of sole proprietors and partnerships declined.

2.6 The profitability of small corporations

In a study of the determinants of profitability, Feeney (2000) analysed the characteristics of the entities in the Australian Taxation data base. The operating profit before tax for each industry is reported in Table 2.4.

Feeney (2000) found that of over three hundred thousand entities analysed, thirty percent did not make a profit and only 69% reported a positive profit margin. Furthermore, 60% of the entities had revenue of less than $250, 000. These entities, many of which could be considered small businesses, were concentrated in the category Communication, Finance, Insurance, Property and Business Services (Table 2.4). This was also the category of industry in which the highest number made a profit (74%). This seems to suggest that despite the concentration of research on big business, it is in the small business sector where return on investment may be highest.

2.7 Annual Turnover of small corporations.

ABS data on Australian industry (ABS 2010) collated the number of businesses located in statistical local areas by annual turnover. The data is aggregated in Table 2.5.

Overall, nearly 94% of businesses among all Australian businesses were generating an annual turnover of less than 2 million dollars. Literally more than 99% of businesses have an annual turnover of less than 25 million, which are classified as “small” by the definition of the Corporations’ Act.

2.8 Value added to the GDP of the Australian Economy.

In terms of industry value-added to the GDP of the Australian economy, Table 2.6 shows that both mining and manufacturing industries are contributing more than 10% each, followed by the industry of Professional, Scientific and Technical Services, which is adding approximately 10% . The value added to the national economy by small and medium businesses is 56%.

Table 2. 4 Percentage of all and small businesses reporting profit: Operating Profit before Tax

Operating profit before tax ($million)	Agriculture, Forestry and Fishing	Mining	Manufacturing	Electricity, Gas, Water and Waste Services	Construction	Wholesale Trade	Retail Trade	Accommodation and Food Services	Transport, Postal and Warehousing	Information Media and Telecommunications
Small	5,585	2,769	9,885	1,235	19,215	6,023	2,703	1,365	6,021	1,465
Medium	285	8,027	6,031	1,599	5,921	7,556	3,236	2,536	763	651
Large	-103	52,840	11,341	8,604	2,480	5,899	6,867	1,310	4,401	4,333
Total	5,767	63,636	27,256	11,438	27,616	19,477	12,806	5,210	11,185	6,449
Percentage	2.12%	23.39%	10.02%	4.20%	10.15%	7.16%	4.71%	1.92%	4.11%	2.37%

Note: estimate has a relative standard error of 10% to less than 25% and should be used with caution.

Table 2.4 Percentage of all and small businesses reporting profit: Operating Profit before Tax (Continued)

Operating profit before tax ($million)	Rental, Hiring and Real Estate Services	Professional, Scientific and Technical Services	Administrative and Support Services	Public Administration and Safety	Education and Training	Health Care and Social Assistance	Arts and Recreation Services	Other Services	Total	Percentage
Small	17,632	13,796	4,839	300	-200	10,002	966	5,665	109,264	12.97%
Medium	-1,923	6,556	-1,609	181	1,220	1,158	1,530	1,116	44,833	5.32%
Large	-1,512	17,559	1,245	173	235	903	1,533	-195	117,912	13.99%
Total	14,196	37,910	4,475	654	1,255	12,064	4,029	6,585	272,010	100.00%
Percentage	5.22%	13.94%	1.65%	0.24%	0.46%	4.44%	1.48%	2.42%	100.00%	

Note: estimate has a relative standard error of 10% to less than 25% and should be used with caution.

Source: ABS (2008-09)

Table 2. 5 Annual turnover of Australian businesses by industry

Industry	Sum of Zero to less than $25k	Sum of $25k to less than $50k	Sum of $50k to less than $75K	Sum of $75k to less than $100k	Sum of $100k to less than $150k	Sum of $150k to less than $200k	Sum of $200k to less than $500k	Sum of $500k to less than $1m	Sum of $1m to less than $2m	Sum of $2m to less than $5m	Sum of $5m to less than $10m	Sum of $10m to less than $20m	Sum of $20m to less than $50m	Sum of $50m to less than $200m	Sum of $200 m or more	Sum of Total
A Agriculture, Forestry and Fishing	50459	32709	16208	13176	16734	12166	32799	16344	8164	3794	754	300	135	72	12	203826
B Mining	1872	792	414	326	642	427	1298	557	406	441	216	143	156	141	119	7950
C Manufacturing	11620	7793	6050	5718	7820	4975	16818	10451	7590	6583	2824	1599	1131	616	252	91840
D Electricity, Gas, Water and Waste Services	685	450	400	408	456	470	1156	496	322	318	138	84	69	57	60	5569
E Construction	37999	28717	46026	38039	40428	27272	63050	25559	16218	11173	3945	1772	892	403	129	341622
F Wholesale Trade	10303	5954	4004	4186	4987	4031	11040	10237	6664	6929	3392	2193	1353	744	285	76302
G Retail Trade	15100	10964	7196	7310	10285	7692	28543	18315	15377	11625	3891	1772	869	572	98	139609
H Accommodation and Food Services	5505	4480	4155	4361	7710	6028	22657	10883	5553	3642	1409	481	171	68	6	77109
I Transport, Postal and Warehousing	29056	20448	16660	12200	14001	8030	17751	6216	3625	2653	1163	768	369	234	114	133288
J Information Media and Telecommunicatio ns	3971	2269	1743	1308	1720	1303	2465	1132	797	650	267	153	72	81	57	17988
K Financial and Insurance Services	53622	17988	12332	9574	11534	7558	18257	7139	4405	2872	1340	932	838	712	558	149661
L Rental, Hiring and Real Estate Services	40048	33349	23081	21598	22878	13419	33937	13843	8044	4708	1413	638	279	187	51	217473
M Prof.Scientific and Technical	41663	28597	17596	18926	25276	17656	44970	16966	9678	6132	1926	983	658	345	93	231465

Services															
N Administrative and Support Services	11886	12254	7337	6625	7336	4524	12888	5552	3260	2731	1178	572	236	148	43	76570
Not Classified 1	8010	11443	2444	6063	4162	4885	4218	1490	592	478	171	67	45	61	6	44135
O Public Administration and Safety	1275	1095	581	597	697	463	1515	822	520	318	114	33	6	15	6	8057
P Education and Training	4271	3476	1979	2025	2538	1562	4246	1361	840	621	273	188	135	36	0	23551
Q Health Care and Social Assistance	10864	7128	7137	4890	8851	6029	25421	13528	5378	2167	482	213	205	90	18	92401
R Arts and Recreation Services	6279	4267	2826	2155	2870	1870	4162	1596	756	444	135	51	54	30	21	27516
S Other Services	8772	9020	8688	7529	10555	8108	18795	7763	3745	1811	393	150	108	36	6	85479
Grand Total	353260	243193	186857	167014	201480	138468	365986	170250	101934	70090	25424	13092	7781	4648	1934	2051411
Proportion of businesses in the category	17.22%	11.85%	9.11%	8.14%	9.82%	6.75%	17.84%	8.30%	4.97%	3.42%	1.24%	0.64%	0.38%	0.23%	0.09%	100.00 %

Source: ABS 2010

Table 2. 6 Industry value-added by business size

Value-added ($million)	Agriculture, Forestry and Fishing	Mining	Manufacturing	Electricity, Gas, Water and Waste Services	Construction	Wholesale Trade	Retail Trade	Accommodation and Food Services	Transport, Postal and Warehousing	Information Media and Telecommu nications
Small	17,085	12,557	23,327	3,256	44,080	15,522	17,216	11,377	15,799	3,038
Medium	2,952	17,694	28,281	2,905	20,315	23,114	12,203	9,769	10,451	3,270
Large	628	76,809	53,547	23,219	18,816	20,259	25,940	6,687	25,132	28,633
Total	20,665	107,059	105,154	29,380	83,210	58,895	55,359	27,833	51,381	34,940
Percentage	2.45%	12.71%	12.48%	3.49%	9.88%	6.99%	6.57%	3.30%	6.10%	4.15%

Table 2.6 Industry value-added by business size (Continued)

Value-added ($million)	Rental, Hiring and Real Estate Services	Professional, Scientific and Technical Services	Administrative and Support Services	Public Administration and Safety	Education and Training	Health Care and Social Assistance	Arts and Recreation Services	Other Services	Total	Percentage
Small	36,791	39,479	12,476	874	776	20,524	2,467	13,704	290,348	34.46%
Medium	5,630	22,526	10,281	1,198	8,944	10,251	2,882	6,190	198,853	23.60%
Large	6,915	21,824	15,863	1,534	4,572	16,558	4,075	2,373	353,382	41.94%
Total	49,336	83,829	38,620	3,606	14,292	47,332	9,424	22,267	842,582	100.00%
Percentage	5.86%	9.95%	4.58%	0.43%	1.70%	5.62%	1.12%	2.64%	100.00%	

2.9 Summary

This chapter provided an overview of the small business characteristics from various perspectives, including the number of small businesses by industry; the number of small businesses employing people; total amount of people employed by small businesses; number of businesses by legal status; operating profit before tax by industry; annual turnover by industry; and industry value-added.

Despite the inconsistencies in their definitions of small corporations/business by ABS and the Corporations' Act, it is undisputable that small businesses are playing a vital role in the growth and development of the Australian economy**.** They represent over 98% of all corporations and of these approximately half are sole proprietors and partnerships. Ninety four percent of small businesses have a turnover of less than $2M but together small and medium contribute over half of the value added by business to the Australian economy.

Chapter 3

Regulation

The purpose of this project is to examine the regulation of small businesses by the Corporations Law. This chapter discusses what is meant by regulation, the recent reforms to regulation in Australia, the major theories of regulation, the burden of regulation for small business, and some example that illustrate some of the difficulties associated with regulation.

3.1 What is regulation?

Banks (2006, p.3) defined regulation as a principle, rule or law designed to control or govern conduct. The OECD (1997) defines regulation more broadly as "the diverse instruments by which governments set requirements on enterprises and citizens". Regulations include laws, formal and informal orders and subordinate rules issued by all levels of government, and rules issued by non-governmental or self-regulatory bodies to which governments have delegated regulatory powers.

Regulations fall into three categories:

- Economic regulations intervene directly in market decisions such as pricing, competition, market entry or exit.
- Social regulations protect public interests such as health, safety, the environment, and social cohesion.
- Administrative regulations are paperwork and administrative formalities — so-called "red tape" — through which governments collect information and intervene in individual economic decisions. Administrative regulations are important tools to support public policies in many areas such as taxation, safety and environmental protection.

The common types of regulation (Productivity Commission 2009, p.13) are:

- Primary legislation – Acts of parliament, including those that underpin treaties signed by Australia, regulation that is high risk, for example health and safety, or where universal application is required.

- Subordinate legislation – rules or instruments which have the force of law, but which have been made by an authority to which parliament has delegated part of its legislative power. These include statutory rules, ordinances, and by-laws.
- Quasi-regulation – rules or instruments and standards by which government influences business to comply but which do not form part of explicit government regulation. Examples include government-endorsed industry codes of practice or standards, government- issued guidance notes, industry government agreements and national accreditation schemes.
- Co-regulation or self-regulation – a hybrid, in that industry typically develops and administers particular codes, standards or rules, but the government provides formal legislative backing to enable arrangements to be enforced.

Regulation design consists of standard setting, information gathering and behaviour modification. Implementation takes two forms, prescriptive or performance based. Under prescriptive regulation each entity is required to act in the same way. Performance based regulation, by contrast, sets out the regulatory performance standard to be achieved and gives regulated entities freedom to decide how to achieve the set standard. In this case a corporation can conduct a risk identification, assessment and impose the level of control that meets an enterprise's stage of development. This is the approach taken by the Australian Securities Exchange in its "if not, why not" approach to compliance with governance guidelines.

It is no surprise that, in general, regulators support prescriptive regulation while those who support persuasion and values based regulation favour a performance based approach. However, rising costs to government of regulation and shrinking budgets relative to the demands continuing to follow the GST, has stimulated actions to move the costs of regulation to business. The latest example is the responsibility for payments for parental leave which Centrelink, the Government's social services arm, wishes to hand over to the business sector.

3.2 Theories of Regulation

Theories of regulation try to explain how and why regulations emerge, why regulatory processes take a particular form and how they affect businesses. The main theories on origin, design and implementation of regulations, which have evolved over time, are public interest, private interest and institutional theories (Morgan and Yeung 2007).

Public interest theory implies that regulators are responsible for the design and implementing of regulation aimed at pursuing common goals that promote the general welfare of the community. To achieve its aim the regulation, based on protecting the public, should aim at providing the relevant information for necessary decision making and correction of market failures. Regulation must therefore strive to protect the public from monopolies and industries that generate substantial external costs or benefits.

Private interest theories are concerned with explaining how and why regulation emerge and why regulatory processes take a particular form and whether the processes are efficient. Regulation is modelled on game theory and based on the economic premise that regulation emerges from the actions of individuals or groups motivated to maximize their own self interests.

Morgan and Yeung (2007) identified the third body of regulatory theory as institutional theory which gives prominence to the role of formal organisations (e.g. rule based regulatory agencies, corporations, states) embedded norms and routines (e.g. risk analysis, cost-benefit accounting , precedent, advocacy norms) or systems as understood by system theory (e.g. legal systems, economic systems or political systems). They claim that institutional theories tends to analyse regulatory interactions from a higher level of abstraction using a system approach to explore the dynamics between the legal, economic, and political systems. An offshoot of this is network theory which uses a similar approach but focuses on a specific policy sector.

An example of institutional theory is the theory of responsive (Ayres and Braithwaite, 1992) and networked (Braithwaite, 2008) regulation . Although Ayres and Braithwaite do not take a systems approach Morgan and Yeung concluded that they blend the public and private interest approaches in a manner that highlights institutional dynamics.

3.2.1 What is a Responsive and Networked Regulation?

A responsive regulation is considered “a process that confidently and openly engages taxpayers in thinking about their obligations and accepting responsibility for regulating themselves in a manner that is consistent with the law” (Braithwaite,V. 2007). According to

Ayers and Braithwaite (1992), the regulators need to be responsive to the conduct of those whom they seek to regulate and to decide if a more or less interventionist response is required.

A regulatory pyramid shows a series of options that a tax authority might use to win compliance. It is sequenced from the least intrusive at the bottom of the pyramid to the most intrusive at the top. In most cases authority that is legitimate and engages seriously with the democratic will of the people does not need coercion from the top to win compliance. Taxpayers are generally aware of the coercive power that exists and can be used. They generally comply with persuasion and education, but if more encouragement is required, the level of intrusiveness may be escalated until intervention elicits the desired response. Once co-operation is forthcoming de-escalation is desirable.

Associated with responsive regulation is “Tripartism”. This is defined as a regulatory policy that fosters participation with relevant private interest groups in which the groups operate as private sector regulators, with access to same information and the same standing to sue or prosecute under the regulatory statute as the regulator.

Braithwaite, J. (2008) expands on responsive regulation to suggest that due to communications and technological developments, businesses, and particularly small and medium businesses, operate across borders linked to large corporations to form networks rather than to operate as individual companies or groups of companies. He suggests (p,2) that “states that fail to adapt to the possibilities for network governance fail to dominate global governance”. In place of the traditional confrontational relationships between regulators and the regulated, regulation should take the form of strategic alliances by which expectations, agreements, codes and norms of compliance can be agreed co-operatively. These would be implemented through self-evaluation. Successful governance would require top—down planning, metagovernance with the State steering, establishing the measures aimed at legitimising and accountability for the arrangements, helping to resource arrangements, and the use of coercive power in the face of breeches or failure.

The success of networked governance is grounded in collaboration, detection of poor performance as every business is benchmarking for continuous improvement, and the resulting competition. Bell (2008, p. 499) criticises the theory saying that “if the state remains a central player it is not clear why at this point we should step past the concept of the ‘regulatory state”.

The theory is also criticised on the basis of the opportunity for interest groups to capture legislation for their own interests. According to capture theory, regulation is ‘acquired’ by an industry and is designed and operated primarily for its benefit. That is, regulatory agencies are captured by the industry they are supposed to be regulating (Uche 2001). To date there is little empirical support to support or discount the theory.

However, the theory appears to support the use of ‘performance based’ regulation such as that of the Replaceable Rules of the Corporations Laws, and ASX governance standards in which companies can choose their form or level of compliance. This form of regulation might be the most appropriate to meeting the needs of the diversity of forms and level of development of small business and relieve them of some of the burdens associated with inappropriate regulation. Inappropriate, here, refers to legislation introduced with good intentions but which may have undesirable and unexpected consequences such as the imposition on small corporations of high costs associated with compliance.

3.3 Regulation reform in Australia

Regulatory reform has been an issue for governments worldwide from the 1990s. Concerns about the growth of regulation in volume and complexity in other countries were confirmed by corporations in Australia (ACCI, 2005). The Small Business Deregulation Task force (1996) had also identified numerous areas of regulation where recording and reporting obligations on small business were judged to be excessive. Not only the costs and the ways in which regulation was implemented but there was also uncertainty about what was required, and the additional costs of dealing with a variety of jurisdictions. Furthermore, there were concerns that many government regulations dampened investment and job creation, resulting in higher prices and reduced choice for consumers (Rimmer, 2006)

The response in Australia was regulatory reform (Table 3.1). This had its beginnings in the perceptions that the multi-government imposed regulations, and multiple sources of regulation and regulators operating across the “tyranny of distance’, were a constraint on competition, not only within Australia but with overseas markets.

Table 3. 1 Key events in regulatory reform in Australia

Year	Regulation	Comment
1995	National Competition Policy	State and Commonwealth Governments (COAG) agreed that new legislation should not restrict competition
1995	Regulatory Impact Statements	Introduced following the collapse of HIH
1996	Small Business Deregulation Taskforce	Survey by Australian Bureau of Statistics and Yellow pages. Report Reducing Redtape
1998	Regulatory Impact Statements strengthened	
2001	Corporations Act 2001	Commonwealth regulation of corporate law established
1998-2004	Corporate Law Economic Reform Commission (CLERP)	Regulation; fundraising, takeovers, executive remuneration, financial reporting, reporting, shareholder participation
2003	OECD	Report: From Red Tape to Smart Tape
2003	Australian Securities Exchange	ASX introduced Principles of Good Governance and Best Practice Recommendations
2003	Standards Australia International	Corporate Governance Standards announced
2005	COAG further regulatory reforms	COAG introduced new wave of reforms
2005	Victorian Office of Regulation Reform; Victorian Competition and Efficiency Commission	Allocated $42m to programs: Reducing the Regulatory Burden (est. $42b.)
2006	Competitions and Markets Advisory Committee	Corporate Social Responsibility Report
2006	OECD	Report: Cutting Red Tape: National Strategies for Administrative Simplification
2006	Australian Government	Taskforce on Reducing the Regulatory Burden on Business
2007-2010	Productivity Commission	Research Reports of Annual Review of Regulatory Burdens on Business:
2009	National Consumer Protection Bill	Introduced licensing and responsible lending obligations for financial lenders, brokers
2009	Henry Review of Taxation	
2010	Cooper Review	Review of superannuation system.

The interest in governance reform was stimulated by several corporate disasters and especially the collapse of HIH, the biggest insurance company in Australia, in 2004. This made the inadequacy of corporate governance regulation a national issue that gained added prominence when addressed by Justice Own during the Royal Commission into the collapse.

By 2003 governments in OECD countries had been seriously addressing how to reduce regulation. All Governments in Australia initiated programs to review and reduce regulation. In Victoria, for example, the State government allocated $42 million to a number of initiatives taken under the Regulation Reform program managed by the Office of Regulation Reform. These included instigating a 'whole of government' approach, and adopting Regulatory Impact Statements. "Whole of government" denotes public services agencies working across portfolio boundaries to achieve a shared goal and an integrated government response to particular issues. Approaches can be formal or informal. They can focus on policy development, program management, and service delivery.(Australian Management Advisory Committee 2004).

Figure 3. 1 Regulation Impact Statements

Regulation Impact Statements

comprise:

- identification of the *problem* requiring action and the desired *objective* or outcome;
- setting out the *options* (regulatory and non-regulatory) and their respective *costs and benefits* across the economy and community;
- *consultation* with those potentially affected; and
- a strategy to *implement* and *review* the preferred option.

A critical feature of this process is that RISs are required to be presented to political decision-makers in time to inform their decisions.

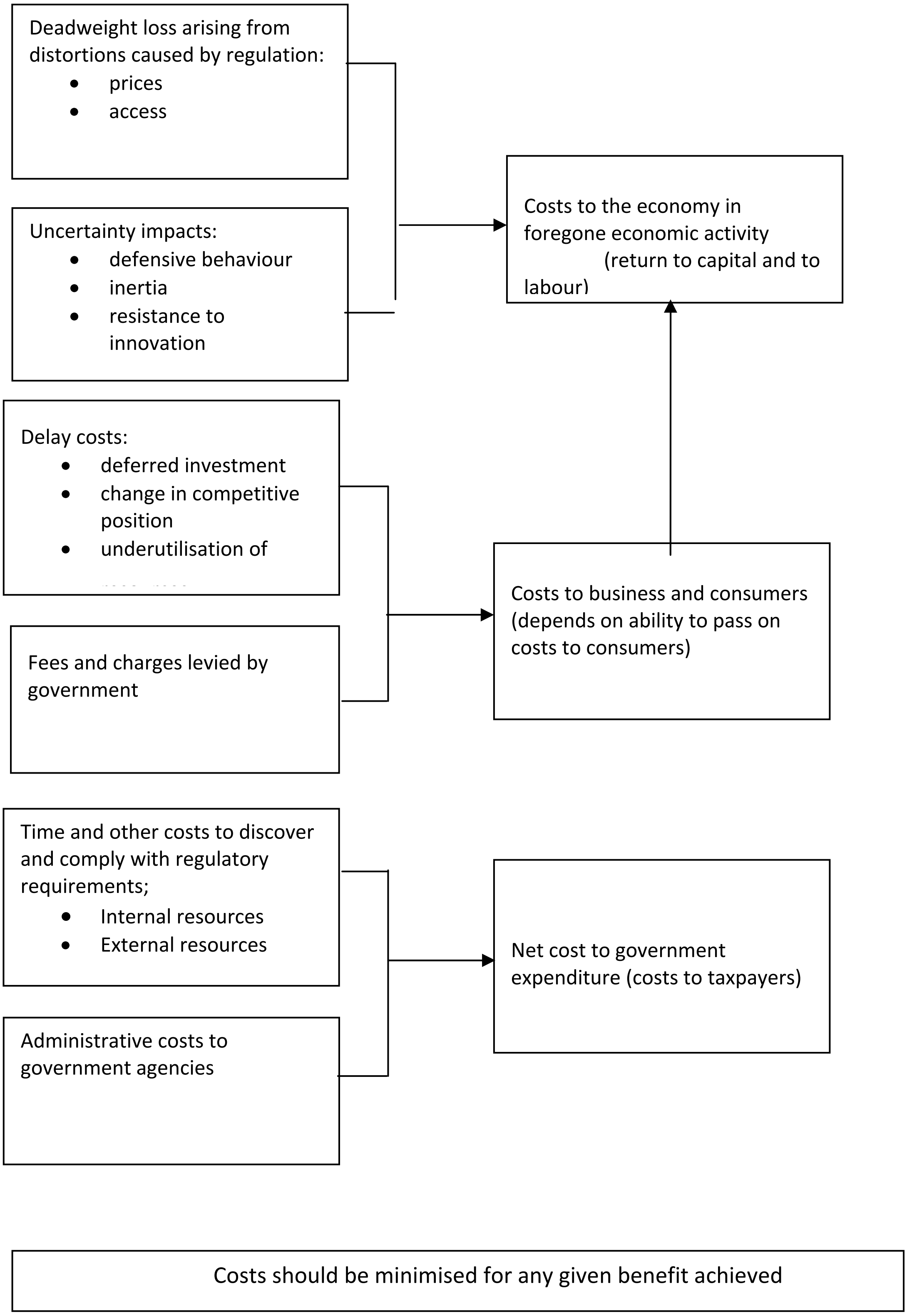
The RIS must also accompany bills and subordinate legislation into Parliament, enhancing the scope for a well-informed political debate, and providing transparent accountability to the community.

Regulatory Impact Statements (Figure 3.1) required a process including risk assessment and quantification of the costs and benefits of regulation. A key element of modern regulation is the requirement for consultation with those affected by the regulation. This is an equity issue for the regulated but an opportunity for the regulators to assess if there are any unintended consequences that would result from the design of a regulation or how it was implemented.

By 2006 the Members of the Council of Australian Governments (COAG) had agreed that the costs of regulation were unnecessarily high. The Productivity Commission, an independent research entity, was requested to investigate the issues. Following on from its first Report in 2007, the Commission has conducted six major reviews that have targeted a different industry sector each year. In response to the Reviews, the Australian Government has undertaken a continuous and active reform of regulation through a variety of means. These have included the development of quantitative and qualitative performance indicators and reporting frameworks for ongoing assessment and comparison of regulatory regimes across all jurisdictions. A major focus was procedures for estimating the costs of regulation.

Following *the Rethinking Regulation* report of the Banks Regulation Taskforce, the Government introduced *The Simpler Regulatory System Bill* in 2007. The Bill was directed to increasing access by companies to the financial sector, and greater efficiency through reduced reporting requirements and use of electronic media. The aim of this Bill was to reduce the regulatory burden. It included initiatives relating to: the use of the internet for financial reporting; financial reporting thresholds for proprietary companies, reporting requirements for executive remuneration, and fund raising requirements for employee share schemes. A *Small Business and General Business Tax Break* was announced on 3 February 2009 as part of the Government's *Nation Building and Jobs Plan*. The Tax Break gave businesses a temporary bonus of a tax deduction as an incentive to business to bring forward investment in new capital equipment one of the measures being implemented by the Government to support economic growth and employment in Australia in the face of a deteriorating global economic environment.

Figure 3. 2 Multiple costs of regulation. Source: Productivity Commission 2006



As these initiatives cover regulation across all levels of government they have major impacts on areas such as finance, taxation and the environment that affect the governance and performance of business.

3.4 Regulatory Burdens

While regulation necessarily imposes costs on those being regulated, an unnecessary burden arises (Productivity Commission, 2009, p. 14) 'when the policy objective of the regulation could be achieved with a lower cost to affected parties'.

Commonly used terms for regulatory burdens are "compliance costs", "administrative costs", and regulatory costs which are used interchangeably to describe regulatory burdens.

Compliance costs are defined as

> "*the costs incurred by taxpayers, or by third parties (such as businesses), in meeting the requirements of the tax system, over and above the tax liability itself and over and above any harmful distortions of consumption or production to which the tax may give rise*" (Sandford, Godwin et al. 1981).

In a later study Sandford et al (1989) define compliance costs to include:

> "*…… for individuals, the cost of acquiring sufficient knowledge to meet their legal requirements; of compiling the necessary receipts and other data and of completing tax returns; payments to professional advisors for tax advice; and incidental costs of postage, telephone and travel in order to communicate with tax advisors or the tax office. For a business, the compliance costs include the cost of collecting, remitting and accounting for tax on the products or profits of the business and on the wages and salaries of its employees together with the costs of acquiring the knowledge to enable this work to be done including knowledge of their legal obligations and penalties….*"

Several studies have confirmed that small firms bear a disproportionately larger share of the regulatory burdens than large firms. Banks (2006, p.xiv) reported that the Industry Commission found that in Australia:

- Disproportionate costs of new regulations or compliance requirements can lower the returns of owners and managers of small businesses;

- entrepreneurs must typically work longer hours in complying with the regulations: and
- compliance cost can be considered “unfair’ in the sense that smaller businesses face higher proportionate costs 9measued against turnover) than larger firms.

The introduction of the business activity statement (BAS) was an example of the burden of compliance on small businesses. (Lateline Business 17/08/2010). The Australian Government’s Regulatory Taskforce’s report *Rethinking Regulation* (2006, p.ii) also identified the drag on entrepreneurial drive (p5) that regulation can place on this sector:

The costs of regulation to business involve not just extra time, paperwork and capital outlays, but also deflect management from the core activities of the business. Submissions indicated that compliance matters can consume up to 25% of the time of senior management and boards of large companies. The impact is even greater for small businesses, which generally do not have the in-house capacity to deal with and keep abreast of the regulatory morass. Regulation can thus stifle innovation and crowd out productive activity in the ‘engine room’ of Australia’s economy.

Banks (2006) reported research by the OECD and the Australian Chamber of Commerce and Industry that estimated $17 billion indirect costs were imposed on Australian SMEs as a result of Australian taxations, employment and environmental legislation.

Similar results have been found in other countries. According to Chittenden et al (2002) the majority of compliance costs borne by small businesses are related to paperwork. Due to the size of the small businesses, the number of staff employed is small and the number available to respond to regulations is small. Hence, in the UK the cost of administering VAT falls heavily on small businesses, which restrains their growth and development. Crain and Hopkins (2001) report that in the ninety nine percent of all firms in US employing fewer than 20 employees (in comparison to the 500 or more employees in 0.3 percent of large firms) the cost disadvantages facing small businesses are mainly driven by environmental and tax-related paper work.

A number of factors have added to the costs of regulation in Australia. Rivalry between levels of government in Australia has inhibited the development of a common legislative framework for SMEs in Australia (Buffini 2007). For example, many licensed tradespeople operating in accordance with apprenticeship regulation in one state needs to comply with different regulations in another state (Leung, Raar et al. 2008).

Small businesses are also unable to look in a single place for regulatory requirements, but must rather look to several bodies within at least three political jurisdictions such as federal, state and local. Another problem for small businesses is to locate from where the regulation is generated. They also considered tax-related regulations most often as the type of regulation providing them the greatest headaches (Clarke, 2002).

But not all regulations fall heavily on small businesses. The cost per employees of economic regulation falls more heavily on large firms, cost per employee of workplace regulation falls more heavily on medium-sized firms and small firms are explicitly exempt from many work place regulations (Crain and Hopkins, 2001). Furthermore, results from a study in the UK the Small Business Research Centre confirmed that regulation was (2008, p.iii) 'enabling and motivating for small business owners as well as constraining. They reported that many business owners were aware that regulation offers opportunities to develop more efficient ways of working and/or increasing income and that (2008, p.40) "37% of the sample reported being able to adapt more quickly to regulations than competitors, 33 per cent reported that regulation encouraged them to take action to ensure the business remains competitive, and 29% reported that regulation increased customer confidence in their business and its products and services".

In regard to Corporate Laws, Dibbs et al (2007) investigated directors' views of the burden of corporate governance regulation imposed on listed companies. Unlike the US, where compliance with the governance provisions of the Sarbanes Oxley Act was seen as a major cost, they found that in Australia (p.74) "very few expressed negative views about Australian corporate governance regulation". Companies felt that they should do all they could to demonstrate good governance because it assisted in ratings from research houses and the difference that made to the firm value justified the cost.

Although this benefit does not apply to small businesses, research shows that without regulation, public perceptions tend to regard businesses as lacking trust and credibility and therefore business activities and access to finance are constrained (Levy and Spiller 1994).

Governments have taken several initiatives directed towards reducing the burden for small businesses in several regulatory areas, particularly in regard to tax and environmental regulations as these are perceived to be among the most onerous of the regulations.

Table 3. 2 Initiatives to reduce the burden of regulation

Government initiatives to improve regulation
Better quality regulation design Clear objectives and frameworks Minimum necessary to achieve objectives Ensure regulations are transparent and non-discriminatory Minimum incentives needed for compliance Able to be monitored and policed effectively Regular reviews and sunset clauses Substitution by removal or off-set of a previous regulation for each new measure introduced **Communication** Written in 'plain' language Open to appeal and review **Simplification** Regulation impact assessments Whole of government access points Use of e-government: the use of ITC and web-based platforms **In regard to small businesses**: Adopting risk-based approaches to identifying inspections or data requirements Modifying thresholds at which regulations apply Quantifications and cost-benefit analysis

Source: Adapted from OECD 2008.

3.5 The challenges that regulation imposes on small business.

Despite the major reforms that have taken place, the cost of regulations in Australia has become particularly burdensome for small business, particularly start-up companies, because they are a major source of innovation and job growth in the Australian economy (Leung, Raar et al, 2008). The Regulatory Task force (2006) cited research conducted by OECD and ACCI which estimated that $17 billion indirect costs were imposed on Australian SMEs as a result of Australian taxation employment and environmental legislation.

Regulation impacts on business in a number of ways. Small businesses find red tape burdensome and hence discourage new business start-ups. These effects can be costly in the global market, because the efficiency of small business can be influenced by domestic regulations and administration cost which reduce competitiveness (OECD 2006).

The increase in the complexity and number of regulations can result in a financial impact on businesses. The economic burden described above is particularly felt by small businesses because of the fixed-cost nature of regulations which creates an environment where regulatory costs are disproportionately borne by small entities. These regulatory costs can act as a "hidden tax" that impede the growth and sustainability of small enterprises (Green 2002).

The time required to deal with existing regulatory requirements for SMEs was an important issues for the Regulatory Taskforce. In a survey of SMEs in 2006 Leung, Raar et al (2008) found that businesses were concerned with the volume and complexity of government legislation, unable to keep up with new legislation and also the apparent duplication of legislation. They also concluded that recognition of the importance of lowering compliance cost was the result of the impact of changes to taxation reporting which were aimed at aligning taxation reporting with accounting standards.

Doern (2009) considered that some of the challenges for SMEs were changing and confusing legislation, unfair inspection by regulatory bodies, lack of finance and access to finance, inability to recruit qualified staff and difficulties encountered in managing employees. They also found understanding legal regulation and obtaining access to credit were challenges. Barriers to growth are expressed along internal and external issues. Internal issues may include cash flow management. Hashi (2001) found among the barriers that had a negative effect on SME growth were financial barriers and tax regulation. Other research (Andrew 2002) confirmed that paper work associated with preparation of tax was considered the biggest regulatory headache for small corporations.

According to Chittenden et al (2002), an initiative by the Better Regulation Task Force (BRTF 1999) in the UK acknowledges both the contribution of small business to the economy, and the competitive disadvantage they suffer in relation to compliance costs. The BRTF looked at the regulatory barriers to the start-up, success and growth of small businesses and found that small firms are often at a competitive disadvantage compared with larger firms because of the cost and time involved in regulatory compliance. BRTF (2000) proposed a number of recommendations to the government to help ease the regulatory burden on small firms. These included greater financial and administrative assistance, better quality and timeliness of information, better consultation and transparent cost assessments.

3.6 Government initiatives to reduce the burden of regulation in small business.

The OECD's 2006 Report "cutting Red Tape" reviews the initiatives taken in many OECD countries to reduce the burden of regulation. All of these (Table 3.1) have been taken at various times by governments in Australia to better design, simplify and communicate regulation. In addition, major initiatives have been taken in the use of information and communications technology.

Armstrong et al (2010) found that for most small businesses their main regulatory concern was taxation and for this they relied on their accountants. Most SMEs used some form of information technology to communicate and provide data to their accountants.

Clearly web based and computer technologies will have a major impact on the ways in which governments interact with their citizens. The Australian Government aims to use information technology to improve the efficiency and reduce the cost of doing business with governments. An example is the VANguard project designed to reduce the costs of compliance for businesses and administration for government in terms of time and money (DITR 2006). The VANguard project provides online validation, authentication and notary services for Federal, State and Local government agencies via a single entry point (Australin e-government 2006), Substantial investment in developing systems using XBRI will offer new ways of informing and managing small business clients and monitoring and analysing data. In the future these offer opportunities to small corporations to lower costs, reduce time and simplify access to governments.

However, whether they will reduce, or indeed increase, regulation and compliance is yet to be determined. The following discussion examines various measures put forward to relieve the burden on small business in regard to taxation, the environment and opportunities to exempt small corporations from legislation.

3.6.1 Tax Regulation

Research by McKerchar, Ingraham et al. (2005) into achieving simplification of tax regulation suggests that it is clear, both in the US and Australia, that a progressive tax rate does not add significantly to complexity in the tax system. Yet simplification is a commonly used political rationale for a flat tax system for the US. The authors state that policy makers need to give consideration to rate change and its effect on taxpayers as a whole and also to provide uniform definitions both within a tax system and between different tax systems. They also state that simplification cannot be achieved by cutting the tax rates or rewriting the existing legislation.

According to Grain and Hopkins (2001) the compliance burden for small businesses may be reduced by a tiered approach which will provide special rules for target groups. In respect to Capital Gains Tax (CGT) and Simplified Tax Systems (STS), tax agents did not perceive them as simple, because they may not be targeted effectively.

Losses impact heavily on small businesses, because tax is paid immediately on a taxable profit. To claim any relief for losses, businesses have to wait until profits are generated.

Tax incentives may result in economic inefficiency if they interfere with the market and result in allocation of resources to less efficient firms rather than to larger and more efficient firms. The incentives may relate to objectives other than pure economic efficiency, such as `encouraging economic growth or income distribution which may justify special tax and other provisions. Where market failures are suspected but their effects are not clear or where the effects of a particular tax policy are uncertain then it is advisable to introduce them on a pilot basis and evaluate their efforts before implementation nation wide (Freedman 2003).

For SMEs which often make losses in their initial years, higher depreciation rates, other tax allowances and reduction in tax rates, are valuable initially (Freedman 2003).

Freedman (2003) suggests the introduction of a definition for tax legislation in regard to small business as the “owner/managed company”. In the UK, sole traders and partnerships are taxed similarly and are both unincorporated business forms which are subject to income tax. An essential feature of the unincorporated business taxation is that both business and personal taxation is fully integrated. This means a company pays the corporation tax rate on profits, which includes capital gains, but net of salary. Income tax is paid on the salaries by the directors and employees.

Tax reliefs are provided in the UK for unincorporated businesses that become incorporated but no tax relief is provided for disincorporation. Despite the tax benefits of incorporation, SMEs may find themselves subject to anti-avoidance legislation. The initial capital expenditure allowance of 40% and 100% write off for information and communication technology is allowed for corporate and unincorporated SMEs. These allowances will be of value only to the level of corporation tax payable.

In the UK corporate SMEs must pay tax on owner/mangers earnings through PAYE systems and pay tax nine months after the end of the accounting period. But unincorporated SMEs pay tax by two instalments on 31st January in the current year of assessment and on 31st July following the end of the current year.

Freedman (2003) states that the European Commission Recommendation emphasises the importance of working towards greater tax neutrality between enterprises with different legal forms so as to avoid distortion of competition. Reduction of compliance costs for small businesses is a strong factor behind most of the tax and non tax special measures for small business in UK, especially in the areas of VAT. Even though governments have indicated a strong desire to reduce the compliance burdens of small businesses, the expansion of tax credits, delivering social security via the tax systems and the introduction of student loans have added considerably to the burdens on small business employers. In 2002 the UK government introduced a flat tax rate for businesses with a turnover of less than £150,000 which is also intended to reduce the accounting work for separate transactions, but they still need to keep proper accounting records for tax purposes. The Finance Act 2003 introduced a new incentive scheme to encourage small businesses to comply with the VAT system and included reduced penalties for late notifications. It also introduced cash accounting for businesses with turnover of up to £600,000 to avoid bad debt problems.

Freedman (2003) suggested three tax policy considerations, each with their own difficulties:

- First, there are significant tax differences between the main legal forms in which SMEs may conduct their activities. This begs two questions: whether such differences are at all desirable and, if not, whether they are necessary?
- Second, as a matter of personal taxation, (despite a preference normally for a tax system that achieved a degree of equity between taxpayers), horizontal equity so that those with like means bear similar tax burdens; and vertical equity so that those with greater means bear greater tax burdens than those with lesser means. The difficulty with this suggestion is to what extent do the differences in tax outcomes according to whether a person is classified as employed, self-employed, or an entrepreneur, compromise those aims?
- Finally, there is a prevailing belief in the need for special measures to benefit SMEs but, as discussed above these measures need to be measured in terms of cost effectiveness, targeting and the distortions they create. How do the UK SME relief measures look, measured against these benchmarks?

The Australian Government introduced a number of mechanisms to reduce the cost burdens to small businesses of GST. These include immediate write-offs of GST related software for businesses with less than 10 million turnover. In addition, a free software package was produced by the Australian Taxation office for small businesses and a further strategy was to give small businesses assistance with transition (Breen, Sciulli et al. 2003).

There are significant differences between the main forms in which business activities are conducted by small business. Therefore, the question is whether such differences are desirable or necessary. Secondly, the tax system should be designed to achieve a degree of equity between taxpayers; that is, those with like means bear similar tax burdens and those with greater means bear greater tax burdens than those with lesser means. Finally, there is a need for special measures to benefit SMEs and for these to be measured in terms of cost effectiveness (Freedman 2009).

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In circumstances when a small business is transferred from one generation of family to another or in case of retirement or death it may lead to break-up of the business or closure with subsequent loss of employment and wealth generation. Not only should there be relief available on the death of the business owner but the owner should be encouraged to part with the business whilst alive in order to keep the business alive and intact. The European commission states that there are advantages to intergenerational succession but does not provide evidence. But in the UK it is argued that there should be support relief from inheritance tax and it might also be extended to support capital gains tax concessions.

In UK there is general capital gains tax uplift on death for all property and this is accompanied by business property relief on certain business assets and 100% exemption from inheritance tax. The 100% relief is available to those who meet inheritance tax provisions.

3.6.2 Environmental Regulation

In the USA the largest area of compliance costs and benefits accrue from environmental regulation, whereas in many other countries environmental regulation receives little attention. These costs do not include transfer costs, such as where one group benefits at the expense of another, or include the paperwork costs of compliance. Paperwork costs, referred to as process costs in the USA, represent the majority of compliance costs borne by small firms (Chittenden, Kauser et al. 2002)

Environmental cost can directly affect the costs of utilities such as electricity. It shows as a direct cost for electricity utilities. The increase in electricity creates a ripple effect on the economy in the form of higher energy costs and causes indirect effects on every productive sector (Crain and Hopkins2001).

Sandford (1989) states that for a business the compliance costs include: cost of collecting, remitting and accounting for tax on the products or profits of the business, and on the wages and salaries of its employees; together with the cost of acquiring the knowledge to enable this work to be done which includes knowledge of their legal obligations and penalties. Sandford also classifies the operating costs of a tax system as social costs and psychological costs.

In a UK government paper, paper work was the most important problem facing small businesses. They stated that according to the SBRT quarterly taxation is the area of red tape caused the most work for small businesses. A number of studies on compliance costs indicate that actual costs incurred by small business in complying with the tax system, include the value of time spent by compliance by the business owners and their staff, as well as fees paid to professional advisors and other costs. They also reported that according to literature the costs for administering VAT falls heavily on small firms in UK and it restrained the growth and development of small business. The measures introduced in April 2002 were intended to reduce red tape and improve small business cash flows (Chittenden, Kauser et al. 2003).

3.6.4 Small Business Exemption

In the US a variety of small business exemptions are considered by regulators, either to free businesses or transactions from an entire regulatory scheme or most regulatory schemes. Small size is measured differently for different exemption schemes. Many are based on the size of the regulated firm measured by its assets, number of employees or other measures. There are others who consider not the size of the firm but the regulated transaction. However no matter how the small business is defined, small size justifies the exemptions from regulations. (Bradford 2004).

However, small business exemption from regulation can be justified only if benefits produced by regulations exceed costs. If the costs exceed benefits for small transactions or small entities, it should be exempted from regulation even if it produces net benefits when applied to larger transactions or entities.

Costs of compliance with government regulation will always include variable costs and fixed costs.. Economies of scale in regulation are abundant. Most relate to fixed costs, but some exist with respect to variable costs. Variable costs are associated with size of the regulated transaction Most of regulatory economies of scale involve regulation of activities that incur capital expenditure such as environmental regulation. Information costs such as keeping abreast with new or revised regulations, reporting and record keeping are another source of economies of scale, because federal regulations include paperwork requirements. The number of reports required and time to complete them do not vary with the size of the business.

Even though the benefits of regulations cannot be measured exactly, one characteristic which is clear is that its benefits are almost completely variable.

If small businesses are to be granted regulatory exemptions, the question is whether it should be based on the size of the transaction or size of the firm engaged in the transaction. It could be based on any measure of size which supports an exemption. In the case of corporate governance exemptions would be considered efficient if they increased the net benefit of a regulation by eliminating applications of the regulation that resulted in a net loss (Bradford 2004).

According to the OMB (2000) report it is difficult and impossible to estimate the actual costs and benefits of existing federal regulation with accuracy. One of the reasons is lack of good information about complex interactions between the different regulation and economy. The main concerns were the baseline against which costs and benefits should be measured; which costs should be measured; the effect of technological change; the many factors involved in causality; how regulation can be assessed once having been implemented; and when comparing costs and benefits, and in any case is there an “Apples and Orange” problem? (Chittenden, Kauser et al. 2002).

3.7 Difficulties for regulators

Schaper (2009-10) identifies many of the difficulties for regulators of small business activities. These include the difficulties of detecting breaches and non-compliance or of communicating with small businesses because of their diversity, size and lack public profile of businesses in the sector, the high rates of churn, the lack of knowledge and understanding of regulations by small businesses and the methodological difficulties of providing ‘evidence’ from research that might support the development of appropriate policy initiatives. As a result, many regulators rly on public complaints and reporting to detect breaches, rather then their own internally-initiaited monitoring and compliance auditing. Others utilise business organisation (such as professional bodies) as a conduit to the private business sector. However, the membership by SMEs can be quite low. And Even where there are industry bodies, they are frequently poorly resourced in comparison to other peak industry groups.

3.7.Summary

This chapter examined what is meant by regulation and what are the consequences of regulation for small business. Regulation can be categorised as social, economic and administrative. Primary regulation is enacted through acts of Parliament and endorsed by legal sanctions. Quasi or co-regulation is promulgated through statutes and other regulations and often involves those who are being regulated. Implementation is related to the type of regulation. For example Acts of parliament such as the Corporations Law are prescriptive, and apply to all. Performance based regulation offers some flexibility related to the ability of a corporation to comply.

The main theories that determine the design and purpose of regulation are public interest, private interest and institutional theories. Governments are increasingly engaging in institutional theories to support the involvement of industry in self-regulation. The argument is that it reduces administration costs for government and the rise of unintended consequences for business.

A substantive program of regulation reform has been in operation in Australia from the 1990s and is still progressing today. Following the recommendations of several taskforces and inquiries, major steps have been taken to reduce the regulatory burden by better regulation design, clear language and communication, simplification of implementation and compliance and increasing use of ITC.

Much of the previous research has focussed on the costs to business of taxation, the environment and opportunities to reduce compliance costs for small businesses by exemptions from regulation. All the suggestions have their own difficulties and limitations.

While the emphasis has been on reducing the costs of regulation, many studies have investigated different ways of measuring the costs and benefits of regulation. These are almost exclusively directed towards large corporations and there are few studies that actually compare the costs with the benefits of specific regulation or the costs and benefits for the small business sector.

Despite the reforms, regulation still poses challenges for small business. The nature of regulation, their number and complexity, the lack of resources, the difficulties of becoming aware of and understanding new regulation, are all a competitive disadvantage when compared with large corporations. This is particularly true when examining corporate governance regulation and how it is applied to the small corporations.

When small business is such a large component of the economy, and the source of innovation and growth, it deserves greater attention. This research addresses this issue in relation to corporate governance.

Chapter 4

Governance and regulation

Governance and regulation are intimately related. The word „*governance*‟ originally derived from a Latin word *gubernar* means to rule or to steer (Tricker, 1984). Corporate governance is "t*he framework of rules, relationships, systems and processes within and by which authority is exercised and controlled in corporations". (*Justice Owen, HIH Royal Commission) It is the system or structure of rules and relationships, supervision and control of those who exercise the authority, accountability, stewardship, leadership, direction and control which aims to ensure accountability and efficient use of resources in balancing the achievement of goals of corporations, society and individuals (Armstrong 2004). External governance mechanisms are those rules which guide the internal governance of a company. External governance mechanisms are those imposed from outside the organisation most notably, government regulation.

This chapter discusses the relationship between governance and regulation, and what governance means in a small business environment. Chapter 4 describes regulation reform in Australia and its implications for small business.

4.1 Corporate governance and regulation

The purpose of regulation by governments is to maintain the social order. The purpose of regulation of corporate governance is to reduce risk and maintain order and confidence in the corporate capital market and to safeguard the investments of shareholders. These include both direct owners of shares and secondary owners such as those contributing to social and financial institutions such as superannuation funds.

Good governance supports business performance: "Good corporate governance structures encourage companies to create value (through entrepreneurism, innovation, development and exploration, and provide accountability and control systems commensurate with the risks involved". (ASX, 2003, p.3). However, it is not that simple. "The corporate governance practices appropriate for a company will be constantly changing as the business develops and alters its direction. This is particularly true for SMEs whose governance needs are very different from mature ASX 100 companies" (Dibbs Abbott Stillman Group , 2007).

Regulation of the governance of corporations in Australia is largely captured in the Corporations Law. All companies in Australia are registered under the Corporations Act 2001 which is administered by the Australian Securities and Investment Commission (ASIC). The law provides for the formation of Australian companies and the registration of foreign companies operating in Australia. It also regulates fundraising by companies, company management, reo-organisations, takeovers, and the liquidation and winding up of companies. The Corporations Act is also the statute that regulates the operation of financial market, the provision of financial services and the offer of financial products in Australia.

The Australian Corporations Law

- Specifies the legal structure of corporations (for example, a company, a partnership or a sole trader) and the appointment, functions and duties of the board of directors and how the business of a board should be managed.
- Provides for formation (termination) of companies
- Confers on companies a separate legal personality, limited liability
- Sets out rules for relationships: members' rights; directors duties, responsibilities
    - Facilitates dealings between companies and outsiders (creditors, customers, etc)
- Specifies the duties of board members:
    - Duty of loyalty and good faith: which includes acting in the interests of the company and avoid conflicts of interest.
    - Duty of care: to be prudent and diligent in attending to the policies, business and affairs of the corporation.
    - Duty of skill: to use one's level of knowledge and expertise efficiently and effectively in dealing with the affairs of the organisation, internal control and risk management; report appropriately to stakeholders.

Accountability to external stakeholders, employees, customers, creditors and communities in which a company operates, are increasingly important as not only shareholders but these other external parties intrude more and more into company domains. While legislation covers many of these relationships, the ability to give objective consideration to stakeholder issues is not only an ethical but a risk management issue. These issues are incorporated in the concept of corporate governance.

While the corporations Act defines the relationships between stakeholders in an entity through the statutes dealing with directors' duties and responsibilities, the role of auditors, and disclosure of information, etc, the internal management of an organisation is guided by its constitution. The Act provides that these can be replaced by a set of model rules.

The internal governance rules of a company were traditionally contained in the company memorandum of association and articles of association. The memorandum of association was the document by which the original incorporators signalled their intention to for a company; it contained details of the company name, number of shares, and details of the directors. The articles of association were its bylaws containing the governance rules such as appointment, removal and powers of officers, meeting procedures and so on.

These are now specified in the 'Replaceable Rules'. Section 1.6 the Corporations Act 'contains a basic set of rules for the internal management of a company (appointments, meetings etc.). Some of these rules are mandatory for all companies but the replaceable rules do not apply to a single shareholder/single director company.

In addition to compliance with the corporations law, companies that are listed on the Australian Securities Exchange (ASX) must also meet the ASX Guidelines for Corporate Governance, the international accounting federation and banking regulators, and most industry and professional associations have codes of corporate governance standards (Armstrong, 2004, 2008). The ASX *Principles of Good Governance* (2003, 2006) were drafted by the ASX Corporate Governance Council (CGC), a body set up by the ASX in August 2002. While these regulations are not supported by law, their compliance is required for listed companies, who, if they do not comply must explain "why not".

Compliance with professional governance regulations is a requirement for bodies monitored by the financial regulator, APRA, and for members of associations such as the National Institute of Accountants or Chartered Professional Accountants.

Table 4. 1 Selected provisions from replaceable rules that are relevant to small business

Issues	Relevant provision
Officers and Employees	Disclosure of director's personal interests Powers of directors Appointment of directors Remuneration of directors Removal of directors
Directors' meetings	Calling meetings
Meetings' of members	Notice Quorum Voting
Shares	Issue Transmission Dividend rights

4.2 Corporate Governance

Although the term "Corporate Governance" is universally recognised, there are various definition that over that last decade have expanded on what corporate governance has come to mean. The OECD (2004) definition is the basis for most definitions used by Securities Exchanges throughout the world:

> *Corporate governance is the system by which business corporations are directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs.*

The OECD's definition of governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as the board, managers, shareholders and other stakeholders. These include responsibilities for human rights in regards to employees and the safeguard of minority shareholder rights.

The definition proposed by the "Father" of the modern corporate governance movement expands the areas of corporate responsibility from internal governance to external governance mechanisms that impact on society:

> *Corporate governance is concerned with holding the balance between economic and social goals and between individual and communal goals. The governance framework is there to encourage the efficient use of resources and equally to require accountability for the stewardship of those resources. The aim is to align as nearly as possible the interests of individuals, corporations and society* (Cadbury, 2004).

In general, corporate governance is concerned with the internal structures and processes for decision-making, accountability, control and behaviour at the top of organisations (Clarke, 2004) and the external mechanisms for accountability. It is essentially about the control and direction of companies, exercised by their directors and those holding power and authority and any decision making in all those matters which affect the vision, performance and long term sustainability of an organisation.

The main focus of governance in this study is the regulation of companies by the Corporations Law. Legislation binds directors to comply with legal duties of loyalty and good faith ; exert internal control of procedural, financial and operational systems; exercise risk management; ensure funds are safeguarded, used economically, efficiently and appropriately; and provide appropriate and balanced reporting to stakeholders.

The study also canvasses some of the matters regarded as within the scope of best practice governance. Numerous guidelines and standards for best practice governance have been developed (Armstrong, 2004). In Australia, possibly the most influential is the ASX *Corporate Governance Principles and Recommendations* that apply to all listed companies.

While not mandated, if a company does not comply with the Principles, it is required to explain why. The ASX makes few concessions for small business other than recognising that the where a requirement, such as the appointment of board committees, is onerous it applies only to the top 300 companies (Clarke and Klettner, 2009).

Guidelines from other public, private and non-profit entities address such issues as governance principles, values and best practice, fraud and corruption control, organisational codes of and conduct, whistleblower protection and corporate social responsibility (Standards Australia International 2003). However, for the most part, although aspects of many of these guidelines are relevant for the small business sector, they are directed at ‘big’ corporations.

4.3 Governance theories

The governance theories that have been the focus of most research are agency theory and stakeholder theory. Agency theory owes its origin to the need for companies to seek investment outside a company to support further development and growth. This led to the emergence of many owners and the separation of owners and control (mangers). Investors take the risks while managers end up with “substantial residual control rights, and therefore discretion over how to allocate investors funds” (Thomas, 2004, p5). The theory assumes that a problem occurs because managers (the agents) will act in their own interests and that these may conflict with those of their shareholders (the principals). A good example of conflicting interests is when a shareholder seeks the highest dividend while a manager might be more interested in retaining funds to grow the company. Misuse, but not necessarily misappropriation of funds, might be an investment in a company yacht or jet or an excessive level of executive remuneration. Hence, there is a need for shareholders to monitor and control the managers.

Stakeholder theory suggests that companies have a social ‘license to operate’ and therefore owe a debt to society and responsibilities to other stakeholders, such as employees, creditors, customers and society at large. Stakeholders are those who are impacted by the company or impact on the company. Rather than regarding corporations as “bundles of assets that belong to shareholders”, companies can be regarded as social institutions that contribute assets to all the parties (Blair, quoted in Thomas, 2004). This theory has provided a rationale for the corporate social responsibility movement (Armstrong 2004) and has been the subject of several government reports (see Parliamentary Joint Committee, 2006). Each of these theories has limited relevance to governance in small business.

4.4 Governance in small corporations

As stated above, governance is about the decision making and control exercised by those who are in charge of a corporations. The Corporations Law uses the term “Director” in referring to those legally appointed and responsible for the duties and responsibilities of directors, but owners and managers of small corporations see themselves as owners and managers rather than as directors. When the roles of management and ownership are located in the same person, the agency problem does not emerge and agency theory does not offer an appropriate explanation of governance in small corporations.

Besides size, assets and level of employment as described above, the Corporations Law distinguishes in other ways between small and large companies. Adams (2009) describes a major distinction that relates to the level of disclosure required by the regulators and the requirement to produce formal accounts and auditing. A small proprietary company under s 292(2) generally does not have to provide a financial report nor a directors’ report unless there is a direction (request) from the shareholders (s 293) or ASIC (s 294). However, all companies, including small proprietary companies have an obligation to keep financial records under s 286 *Corporations Act* 2001 (Cth). The financial records must correctly record and explain all transactions and the financial position of the company and would enable a true and fair financial statement to be prepared. The records must be kept for seven years and it is a strict liability criminal offence to fail to keep such records. This obligation is in addition to any tax law provisions.

There are other ways in which management of corporate governance in small corporations differs from that found in larger businesses. These include decision making, ownership and board structure and composition.

4.4.1 Decision making and authority

In many small businesses only one or two persons, mainly the owners and/or managers, make all the critical decisions such as finance, accounting, personnel, purchasing, processing or servicing, marketing, selling without the aid of internal specialists and with specific knowledge in only one or two areas (Wiltshire Committee 1971). For them governance is a combination of views of the owners and the manner in which they run the business (Burgess, Sellitto et al. 2009).

For these people governance of small businesses is mainly concerned with improving their performance and allowing the commensurate benefits to flow to stakeholders such as owners and employees. (Burgess, Sellitto et al. 2009). Many are not interested in economic growth, but rather battle survival on a day to day basis and aim to provide themselves and their employees with a comfortable living (Burgess and Hill 2004). Others seek a certain life style and autonomy not available when employed in a large organisation.

4.4.2 Family Ownership

Good governance principles in relation to the structure of company boards include recommendations to separate the roles of Chair and CEO, and appoint independent directors to boards and committees. Their purpose is to meet the requirements of government and other regulators for accountability and transparency for reporting by a board to the owners.

However, these will not be a priority for a small company. As indicated above, "when the owner and the manager are the same person, corporate governance practices based on agency theory may be inappropriate. Stewardship theory, in which the interests of managers and owners are congruent appears to describe the situation more realistically. Securing resources, their efficient use and ensuring the viability of the business is central to stewardship and to the interests of the owner/manager. The danger is that a strong leader may dominate the business and when a business moves beyond start-up to a growth phase, the business may suffer from poor management" (Muenjohn et al 2010, p.72).

Governance in family businesses refers to the relations between the family, other stakeholders and the family**.** Family ownership is a significant factor in establishing small business. The family home or other relatives are often the source of initial finance and guarantees for start up businesses and the ownership structure in family businesses have a major impact on corporate governance structures. Family businesses are often small with closely held share ownership. They are the precursors of big business. In the USA they represent 35% of publicly traded firms, in Europe over 50% of businesses are controlled by a single shareholder (Faccio and Lang, 2002) and in Asia over two-thirds of businesses (Claussens et al 2002). In Australia, over 80% of the small corporations in Australia are family owned.

Family ownership shapes corporate governance structures. Navarro and Anson (2009) found that, in family businesses, families own a larger proportion of shares, boards tend to be smaller and their chairman have longer tenure than in non-family firms. Board committees are few and membership of boards and committees are biased towards the family.

Much of the wider debate about governance has centred on the separation of the roles of Chair and CEO, the appointment of independent directors, and more recently, the diversity of board members. The arguments for separation of the Chair and CEO are drawn from agency theory. The argument is that there is a separation of ownership from control of companies leading to a conflict of interests between owners and managers. Based on the same theory is the requirement for the performance of boards to be assessed, and that this is a role that engages the shareholders.

As most small businesses are owner managed or family owned this argument is often irrelevant to small businesses, until second or even third generation of their businesses. This is likely raise issues of succession: when should the owner/manager hand over the reins and to whom.

Where agency theory could apply is when the business has a combination of inside owners and smaller outside investors. The minority shareholders could be disadvantaged if resources were hived off or directed to the advantage of the families and disadvantage of the other investors (Claussens 2002, Kanthapanit et al 2010).

Independent boards and independent directors are seen as essential for achieving transparency and accountability in large companies. In small companies, a board and independent directors are not regarded as of value but as a cost to a business that cannot be afforded.

4.4.3 Diversity of board membership

Research shows that even in large companies, diversity in terms of gender, age and nationality is poor. A recent review of women on boards of companies indicated that only 10% of directors on the top 500 companies were women (the Age, p.1. 2010). Research into small family businesses has found that in the past women's contribution to the businesses was not recognised and that, unlike male family members, they were not groomed nor given the same opportunities to learn to be leaders of small businesses (Barrett and Moores, 2009). However, because women often meet the 'glass ceiling' in big business, many seek to operate as the proprietors of small or micro businesses.

4.5 Summary

As stated above small corporations in Australia regulated by the Corporations Law are largely proprietary companies whose 'small' definition under the Corporations law is based on satisfying two out of the three criteria based on their size, assets and income.

Small corporations (Clarke 2010) act in isolation and often act in ignorance while trying to meet their governance obligations. The demands of the business are constant and a first priority of owners/managers who regard regulatory compliance a distraction from their core business.

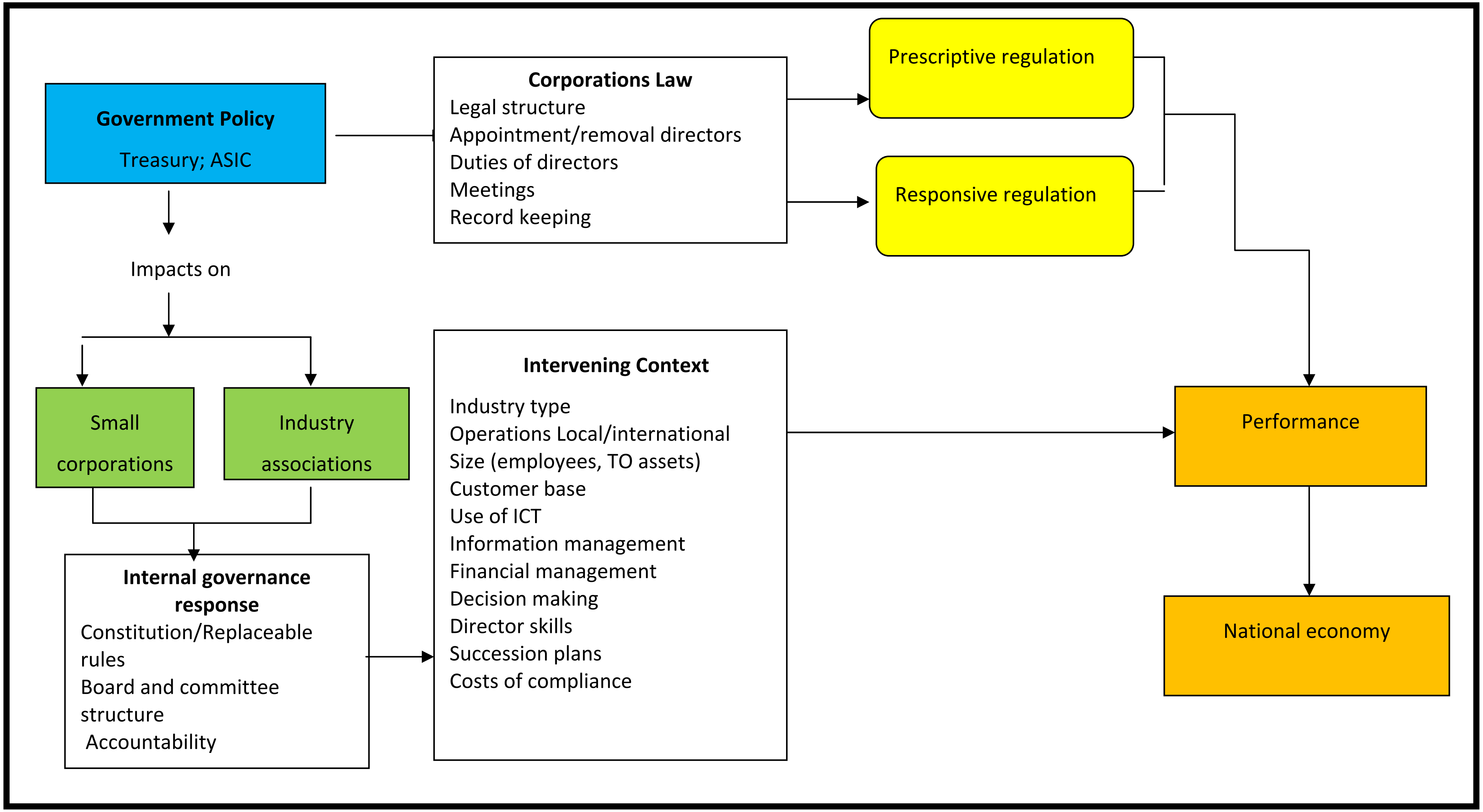
The main difference between the regulation of large and small companies relates to the level of disclosure by the companies and the requirement for large companies to produce formal audited accounts.

Governance also differs significantly in small corporations from that found in larger corporations in respect to size, resources, level of employment, directors' perceptions of their role, decision making authority, family business structures, independence of board chair and CEO/manager, use of independent directors, diversity and accountability.

Given these differences, a question is raised as to the appropriateness of the present corporate regulation for small corporations.

As the complexity of regulations increases, the financial impact of the regulations increases. The fixed-cost nature of the regulation creates an environment, where the regulatory costs are disproportionately borne by small businesses (Green 2002). However, it can be argued that small businesses generate benefits for the whole of the economy and should be promoted by government policies and regulation (Freedman 2003). Regulation offers both burdens and benefits to small corporations. This issue is explored more fully in the next chapter.

Figure 5. 1 The relationships between governance regulation, small corporations and their performance



Australian Research Council Linkage Grant

Chapter 5

Analytical framework for the study

The purpose of the ARC project was to develop a model of the impact of governance regulation on SMEs with the objective of achieving the aims of regulation in the most efficient and effective way for all stakeholders. The primary aim of this research was to determine how the Corporations Law affected the governance of small business and their operations, and whether changes to regulations in this area could assist small corporations. It will report on the constructs or variables that are drivers for regulation (e.g. context variables, regulatory culture); the independent variables, the processes e.g. compliance, self-regulation, modes of reporting and audition, use of technology, the intervening variables, both in place and that stakeholders (in this study: government, small corporations and small business associations) perceive as most desirable. Other factors include the various options for regulation, and outcomes or dependent variable, such as the entrepreneurial activity and the performance of the firm. Regulation requirements are often termed external governance mechanisms. Internal governance mechanisms are about the ways in which firms respond to the regulation.

The literature review in chapter two identified governance and regulation theories that are relevant to this study. Governance theories suggest that good governance principles address such issues as the composition and independence of boards, corporate structures, separation of management and control, decision making, and accountability demonstrated by transparency and disclosure.

This second stage study was designed to determine the constructs or drivers that the small business sector identify as the key issues, related to regulation of governance, that are emerging for small business in Australia today. Figure 5.1 illustrates the conceptual framework for the study. Government regulation promulgated in the Corporations Law impacts on the small business sector. The response to the regulation, evident in internal governance mechanisms, is mediated by the context in which a business operates. The aim of the regulation is to facilitate small business performance which, in turn, has implications for the performance of the economy. Major issues for this study are what are the factors which inhibit or promote god governance in small corporations and whether the kinds of regulation described in chapter two, or some other approach, will best achieve the desired outcomes.

The scope of this study is restricted to compliance with the governance requirements of the Corporations Law and to corporations defined as ‘small’ under the Corporations Act and that are not public or listed companies. Not all aspects of governance, including ownership or stakeholder interests such as minority shareholder rights, were investigated.

Governance regulation in Australia is found in the Corporations Act (the Corporations Act 2001 (Cth)) and is implemented by ASIC. The Corporations Act is the statute governing the creation, operation and termination of companies in Australia. The governance provisions of the Act set out the desirable structures of companies, the duties of company directors, the relations between various stakeholders and internal governance rules such as the procedures for holding meetings (Francis and Armstrong 2009, 2011). The internal governance rules of a company were traditionally contained in the company memorandum of association and articles of association. The memorandum of association was the document by which the original incorporators signalled their intention to form a company; it contained details of the company name, number of shares, and details of the directors. The articles of association were its bylaws containing the governance rules such as appointment, removal and powers of officers, meting procedures and so on.

These are now specified in the ‘Replaceable Rules’. Section 1.6 the Corporations Act ‘contains a basic set of rules for the internal management of a company (appointments, meetings etc.). Some of these rules are mandatory for all companies. There are a few special rules for single shareholder/single director companies. For example, the replaceable rules do not apply to a single shareholder/single director company, or a company that had a constitution before the introduction of the replaceable rules regime and has not repealed it. A company now has a choice to adopt its own constitution or modify or add to the replaceable rules.

Some of the differences between small and large corporations were recognised by the introduction of the first Corporate Law Simplification Act (see p.34) in 1995 which relieved small business from preparing annual Reports or being audited unless requested by ASIC.

Nevertheless, Miller (2010) reported that 30,000 small businesses are required to meet the full requirements of the act.

The major theories of regulation are public interest, private interest and institutional theories. As discussed above, public and private interest theories are usually prescriptive in form. In keeping with these theories, regulation of the small business corporations would be strongly influenced by the regulators.

The study measures perceptions of the Corporate Law regulation, the constructs or variables that are drivers for corporate governance regulation (e.g. context, regulatory culture, type of SME); the processes (e.g. compliance, self-regulation, modes of reporting and auditing, use of technology), both in place and that the small business corporations perceive as most desirable; the impact of the various options on accountability, (e.g. disclosure, reputation) and performance.

In institutional theories, corporations tend to be seen as part of a larger system or network of players or legal, economic and political subsystems. Institutional theories suggest the merit of engaging people in thinking about regulating themselves. Hence, support for institutional theories from this study would support the study methodology which seeks the views of those being regulated, the small business corporations, and for regulators to respond to their views.

Two groups of respondents were invited to participate in this study: executive officers of small business industry associations and small business owner/managers were interviewed. Both groups of both groups were invited to participate because of their expertise and experience in small business matters. Executive officers were not only familiar with the sector but were in practice operating small business entities themselves.

The first group, representatives of small business associations, provided information on their experience of regulatory compliance as small businesses by themselves, including how they facilitated their members to meet the changing regulatory schemes and their observations of the regulatory burdens their small business members are bearing due to regulations from various levels of the governments.

The second group, representatives of small corporations, were also asked to identify key difficulties pertinent to their survival and growth, their experience on meeting regulation requirements, their expenses on compliance and practice of corporate governance.

The purpose of this study was to determine the critical regulation issues that were important to the small business sector in relation to the corporations law and their governance.

In particular, the study was designed to answer the research questions:

- What were the key governance issues that were a problem for the operation and growth of small business?
    - Is corporate governance regulation a burden for small business?
    - Was the Corporations Law, as it now stood, appropriate for small business?
    - How does it affect the governance of small business?
    - What were the factors that promoted or inhibited compliance with the Corporations Law?
- What is the aim of corporate governance regulation of small corporations?
- What could the regulators do to improve regulation of small corporations
    - Should regulation be withdrawn, modified, or changed?
    - Should or could it be made simpler? How?
    - Were there were changes to corporate regulation that would facilitate the growth and success of small corporations?
    - What impacts might changes to corporate governance regulation have on small business performance
- What are the real issues that inhibit efficiency and effectiveness in small businesses?

The following chapters describe the details of the samples (corporate characteristic, use of it, board structures, succession plans, sources of advice), the participants' responses to governance regulation (Replaceable rules, directors duties and independence, and the costs of compliance), difficulties encountered, and suggestions for improvement.

Chapter 6

Descriptive statistics of the respondents

This chapter describes the characteristics of the two sample groups, first the executive officers of the industry associations Section 6.1 followed by the small business owner/managers Section 6.2.

6.1 Introduction

Two samples consisted of representatives of twelve industry associations (a response rate of 46% of COSBOA member associations) and nine small businesses. The demographics of the samples are reported for (a) representatives of the small business industry associations and (b) small businesses.

6.2 Industry Associations

Demographics of the respondents and the industry associations they represent include:

- position of the association respondents,
- industry the respondents' associations represent,
- regions the respondents' association represent,
- whether the association has a website,
- whether the association is a member of other associations,
- legal status of the associations,
- and the number of members in each association.

Position of the Association respondents

As shown in Table 6.1, ten out of the twelve respondents being interviewed are either Executive Officer, or Chief Executive Officer or Director, accounting for 83.33%. The other two respondents are policy specialists, accounting for 16.67%. The executive level officers provide a relatively comprehensive understanding of their members' overall situation as well as the practice and impacts of corporate governance and government regulation. Two policy specialists critically evaluated the critical needs for small corporations in their sector and potential solutions (as shown in Table 6.1).

Table 6. 1 The position of the respondents

Role	Number of respondents	Percentage
EO/CEO/Director	10	83.33%
Policy Specialists	2	16.67%

Industries represented by the respondents' associations

As shown in Table 6.2, five respondents are of industry associations represent the retail trade, (accounting for 41.67%); three represent the manufacturing sector (25%), two represent professional, scientific and technical services (16.67%), two represent other services (16.67%) and one represent wholesale trade (8.33%). Among these twelve organisations, one organisation represents more than three industries (8.33%).

Table 6. 2 The industry sectors represented by the respondents' associations

Industry	Number of respondents	Percentage
Retail Trade	5	41.67%
Manufacturing	3	25.00%
Professional, Scientific and Technical Services	2	16.67%
Other Services	2	16.67%
Wholesale Trade	1	8.33%

Regions the associations represent

Eight of the twelve organisations operate at national level (66.67%), and three represent members in more than one State. Three have members from Victoria (25%), and one industry association responded from each of Queensland, Western Australia and Tasmania (8.33% each). The sample is therefore representative of industry associations representing members from across Australia

Table 6. 3 Regions represented by the respondents' associations

Region	Number of respondents	Percentage
National	8	66.67%
Vic	3	25.00%
Qld	1	8.33%
WA	1	8.33%
Tas	1	8.33%

Location of associations

Two respondents replied that they have six sites Australia-wide (16.67%); two other associations have seven sites each (66.67%). Eight respondents mentioned that they only have one domestic site (66.67%). None of the associations in the sample operated any sites outside Australia.

The multi-site characteristic reflects the flexibility and heterogeneity of the associations in terms of location.

Table 6. 4 Number of sites in Australia

Domestic sites	Number of respondents	Percentage
1	8	66.67%
6	2	16.67%
7	2	16.67%

Does the industry association have a website?

Eleven organisations have their own website (91.67%) while one organisation does not have a website (8.33%).

Table 6. 5 Website

Website	**Number of respondents**	**Percentage**
Yes	11	91.67%
No	1	8.33%

Association membership of other associations

Ten associations are members of some other associations (83.33%). Two respondents are not clear whether they are members of any other associations (16.67%). Being a member of an association provides networking and knowledge transfer opportunities.

Table 6. 6 Whether the association is a member of other associations

A member of other associations	**Number of respondents**	**Percentage**
Yes	10	83.33%
Not applicable	2	16.67%

Legal status of the associations

Seven of the respondents’ organisations (Table 6.7) are registered as not - for- profit incorporated organisations (58%), three are public companies (25%) and two are privately held companies (16.67%). None are listed on the stock market.

Most companies that are registered (or incorporated) under the Corporations Act are proprietary companies limited by shares unless they are public companies. The main difference between proprietary companies and public companies are that proprietary companies are not permitted to have more than 50 shareholders nor to raise capital by issuing shares. Irrespective of their size, public companies are required to hold an annual general meeting, and to lodge financial reports that must include details of the Company Secretary and statements about the qualifications of directors, their attendance at meetings and any contracts they have with the company.

An association incorporated under the Association Incorporation Act can hold assets in its own name, and provides the protection of limited liability for members but cannot trade or distribute profits for members.

Table 6. 7 Legal structure

Organisation type	Number of respondents	Percentage
Not-for-profit/Incorporated association	7	58.30%
Public company	3	25%
Proprietary	2	16.67%

Size of the associations: number of members

Membership of associations ise represented in table 6.8. Six associations have more than 90 and less than 650 members (50%). Four associations have 750 to 2400 members (16.67%). Two associations have more than 2400 members (16.67%).

Table 6. 8 Number of members in each association

Number of members	Number of respondents	Percentage
90-650	6	50.00%
750-2400	4	16.67%
2400-77000	2	16.67%

6.3 Demographics of Small Business Participants

Some of the characteristics that are considered important for small business in literature were identified as the education, experience of the owner-manager, firm size, age or ownership and the stage of organizational development (Doern 2009).

The demographics of the characteristics of the small businesses are presented in Table 6.9. The majority 4 (44.4%) of the respondents were in the age category of 56-66. The next highest 3 (33.3%) category was in the age range from 46-55. Most of the participants (7) were male and 2 were female (Table 6.10). Among the participants' highest level of education achieved were 3(33%) who had a bachelor degree, 2(22%) had post graduate qualifications and a further 2(22%) had completed secondary education (Table 6.11). Over 50% were tertiary qualified.

Table 6. 9 Respondents Age

Age	Number (n)	Percentage
36-45	2	22%
46-55	3	33%
56-66	4	44%

Table 6. 10 Respondents Gender

Gender	Number (n)	Percentage
Male	7	77%
Female	2	22%

Table 6. 11 Respondent Qualifications

Qualifications	Number (n)	Percentage
Grad Diploma/ grad certificate	2	22%
Bachelor degree	3	33%
Advanced diploma, Diploma	1	11%
Certificate	1	11%
Secondary	2	22%

The table 6.12 shows the industry represented by small business. The results show that over 4 (44%) of small business respondents were in retail trade and 2 (22%) were in professional scientific and technical services. The rest were spread across financial and insurance services, administrative support and others.

Table 6. 12 Industry Sector Represented by Small Business

Industry Sector	Number (n)	Percentage
Retail Trade	4	44%
Professional scientific and technical services	2	22%
Financial and Insurance services	1	11%
Administrative support	1	11%
Other services	1	11%

The majority of the respondents (88%) were located in Victoria and one (11%) was from interstate (QLD) (table 6.13).

Table 6. 13 Location of the business

State	Number (n)	Percentage
Victoria	8	88%
QLD	1	11%

The majority (55%) were owners and 33% were CEOs or managers and one was a senior accountant Table 6.14).

Table 6. 14 Respondents Position

Position	Number (n)	Percentage
Other (Owner/Manager)	5	55.5%
CEO, Managing Director	3	33.3%
General Manager	1	11.1%

Small businesses (88.8%) reported they were members of industry or professional associations (Table 6.14). Among the small business sample 44.4% held voluntary or remunerated positions on an industry association or peak body. However, 66% said they were not members of the board.

Table 6. 15 Membership of Associations

Association	Number (n)
CPA	3
Furnishers Society Vic	1
Pharmacy Guild	1
CAMBA	1
Toy association	1
REIV	1
AREI	1
Superannuation self management professional association	1

A majority (66%) of the companies in the sample were private and 22% were partnerships. None of the companies were listed (Table 6.16).

Table 6. 16 Legal structure of the 9 small business companies

Company Type	Number (n)	Percentage
Private Company	6	66.6%
Partnership	2	22.2%
Sole proprietor	1	11.1%

A majority 7 (77.7%) operated only in one site (Table 6.17). None of the respondents had overseas sites. However, 22.2% (2) reported they operated or provided services in countries other than Australia. Again, a majority 4 (44.4%) were in the maturity stage in their development cycle and 3 (33.3%) were in the expansion stage (Table 6.18).

Table 6. 17 Number of Sites

Sites	Number (n)	Percentage
1 sites	7	77.7%
2 sites	1	11.1%
5 sites	1	11.1%

Table 6. 18 Development stage of the business

Stage of the business	Number (n)	Percentage
Maturity	4	44.4%
Expansion	3	33.3%
Establishment	1	11.1%

Over 55% have a website (5). Eleven per cent (1) intend to develop a website in the future. Three (33%) had no website (table 6.19).

Table 6. 19 Website

Website	Number of respondents	Percentage
yes	5	55.5%
no	4	44.4%

The study also reported that 88.8% had less than $5 million assets and 11.1% had assets between $12.5 million to $15 million (table 6.20). It also reported that 77.7% had less $5 million turnover, 11.1% had turn over between $5 million to $10 million, and another 11.1% had turn over between $12.5 million to $15 million (table 6.21). The Table 6.22 reported the number of employees. They all had less than 50 employees.

Small businesses were defined under the criteria classified in Section 112 of the Corporation Act 2001 in Australia based on the assets, turnover and number of employees.

Table 6. 20 Assets

Total Assets	Number (n)	Percentage
Less than $5 million	8	88.8%
$12.5 million to $15 million	1	11.1%

Table 6. 21 Annual Turnover

Turnover	Number (n)	Percentage
Less than $5 million	7	77.7%
$5 million to $10 million	1	11.1%
$12.5 million to $15 million	1	11.1%

Table 6. 22 Number of Employees

Number of Employees	Number (n)	Percentage
1	4	44.4%
2-10	3	33.3%
11-20	1	11.1%
21-50	1	11.1%

6.4 Summary

This chapter described the two components of our sample, the CEOs of 12 industry associations and the small business mostly operated by owner/managers.

The results of the assessment of assets, turnover and number of employees confirm that the small business samples from both groups of respondents studied fall within the small business criteria of the Corporations Law, which is defined under the criteria classified in Section 112 of the Corporation Act 2001 in Australia based on the assets, turnover and number of employees.

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Chapter 7

Corporate governance in small corporations

The aim of this study was to determine the issues related to corporate governance that are important to small business.

As indicted in Chapter four, governance differs significantly in small corporations from that found in larger corporations in respect to size, resources, level of employment, directors' perceptions of their role, decision making authority, family business structures, independence of board chair and CEO/manager, use of independent directors, diversity and accountability.

Corporate governance in the context of this study referred to the provisions of the Corporations Act, particularly the Replaceable Rules and aspects of the Law which had been simplified for the regulation of small businesses, plus some aspects of best practice governance as recommended by the ASX guidelines.

The first section in this chapter describes the governance practices in place in small corporations. The second section describes the perceptions of difficulties that small businesses encountered with the governance regulations.

Corporate governance regulation investigated here referred to the structure of a board, the independence of directors and the direction and accountability exerted by those in control. Questions were also asked about whether the small business corporations complied with best practice guidelines recommendations: independence of a board, the separation of ownership and control, skills and diversity of directors, succession plans, a code of conduct and record keeping and information disclosure

These questions were designed to build a picture of the operations of boards and directors of the small business sector.

7.1 The response of the small business sector to governance regulation

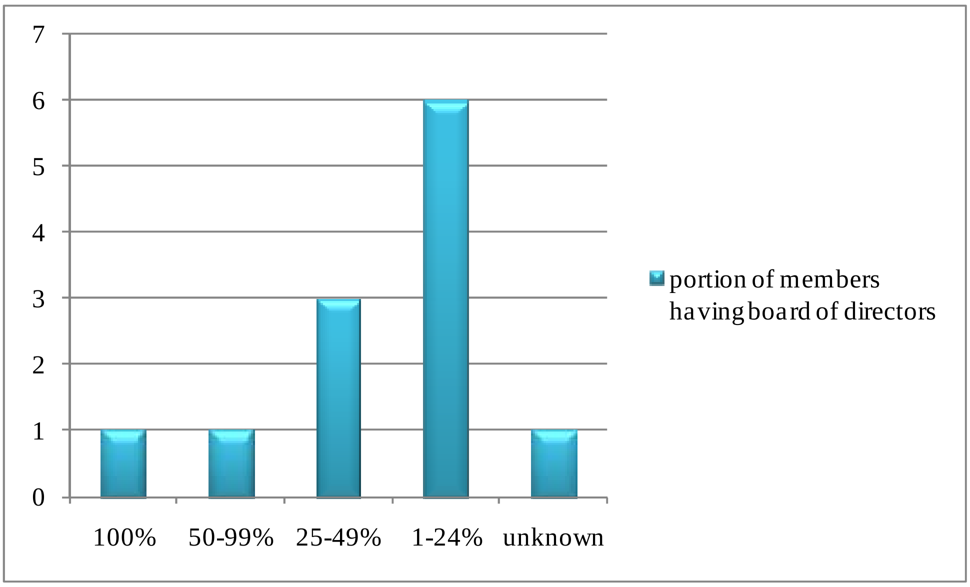
7.1.1 A Board of Directors

Eight of the nine small businesses were proprietary companies. The exception was one which was a partnership. Six had a single owner manger who was the sole director. Only three of the businesses had a board of directors. In most cases the board members were shareholders or members of the family who owned the business. It appears that a board was formed when there were more than two shareholders and that these then became the board members.

The industry association respondents were asked what proportion of their members had a board of directors, and small businesses were asked if they had a board of directors.

Six association CEOs reported that less than a quarter of their members have a board of directors. Only one association, the largest, reported that all their members had a board in place. Three estimated between 25% to 49%, of their members have a board of directors. One respondents disclosed that more than 50% of their members have a board of directors (Figure7.1).

Figure 7. 1 Proportion of member companies having board of directors



Nearly all these businesses were well established. Only one was in the ‘establishment phase’ of development. To most of the respondents, unless there were shareholders with a substantial interest in the business, a board seemed to be unnecessary.

7.1.2 Board sub-committee structures

Best practice governance recommends board structure s that include sub-committees. The members of these can provide specific expertise and manage functions such as overview of auditing or selection of directors on behalf of a board.

Most of the CEO respondents mentioned that their members do not have any sub-committees. Some said they are not clear whether their members have such sub-committees or not. Others acknowledged that some of their members may have audit committee, risk management committee, remuneration committee or nomination committee, but the proportion would be less than a quarter.

Among the small business respondents, one reported having a risk management committee and one had a remuneration committee.

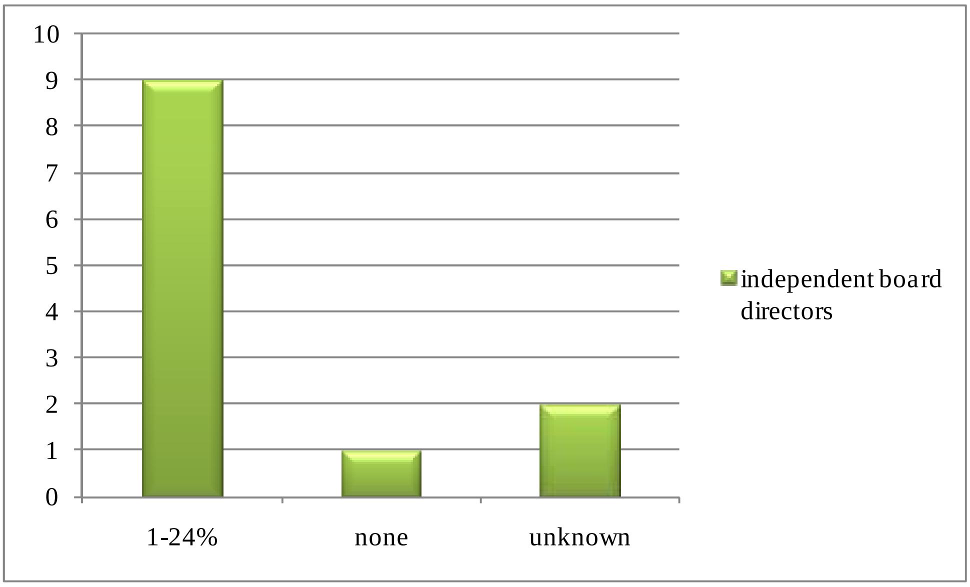
7.1.3 Independence of directors

Respondents were asked how many had independent directors (i.e. not employees, substantial shareholders or suppliers to/ customers of the business) appointed to their boards.

Independence of the board, that is the ability to make decisions independent of managment, and to monitor management, is seen as governance best practice in the ASX Principles. A debate continues about how useful independent directors are if they are not familiar with the business. For small businesses dominated by owner/managers, the point of appointing independent directors to monitor management seems superfluous. Further, it is debatable how much value independent directors add to small businesses when their cost is taken into account.

Nine associations CEOs reported that less than 25% of their members have an independent director sitting on the board. The other three respondents said the proportion of their members having an independent director is either zero or unknown (shown in Figure 7.2).

Figure 7. 2 Proportion of members having an independent director



The results appear to confirm ASX surveys and previous research (Clarke and Klettner 2009) which showed that even many listed SMEs do not invest in independent directors. Most of the entities assessed in this study not only did not have independent directors, they did not have a board.

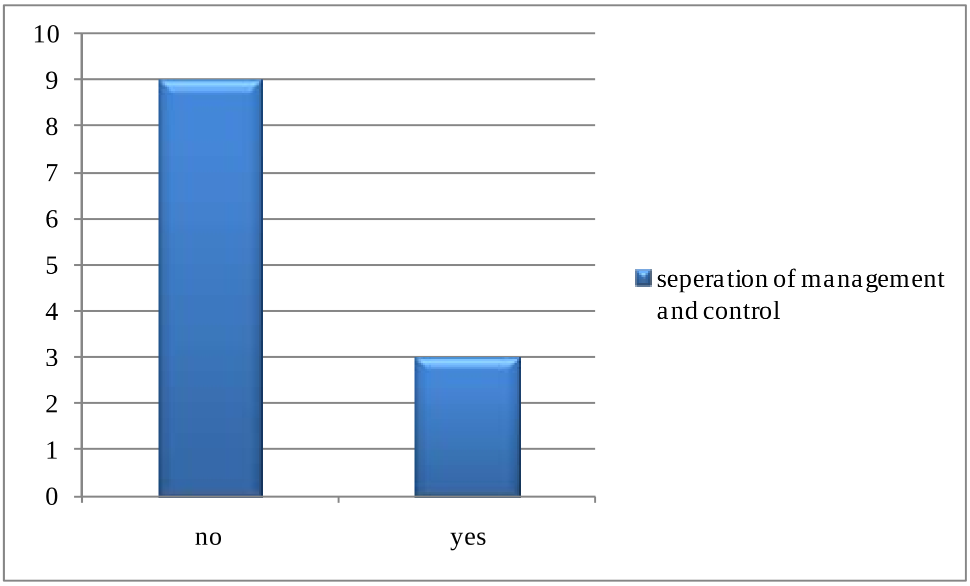
7.1.4 Separation of the roles and responsibilities of the board and management

Separation of the roles of board and management is another governance best practice principle that is intended to enable shareholders to safeguard their interests by maintaining the independence of a board.

Three associations reported that their members have separation of management and control, and two of these have procedures in place to monitor and review the arrangement.

The other associations did not agree)Figure 7.3).

Figure 7. 3 Whether their members have the separation of management and control



7.1.5 Information disclosure of small business members

In the context of listed companies, continuous and full disclosure of the operations of a company to the market is an important requirement.

In contrast, small proprietary businesses hold their information close. Although some associations CEOs have witnessed information disclosure on financial and operating information, share ownership and voting right, and foreseeable risk factors, it was rare. Most of the association respondents either do not know or have not observed any information disclosure from their small business members

Small business respondents disclosed information for tax and GST matters or to banks for financial planning, and this was usually provided to their accountants. One respondent disclosed information in regard to material risks to their insurers.

7.1.6 Succession plan

Eight association respondents out of twelve observed that less than 25% of their small business members have a succession plan. Where there was one, the plan was most likely to be directed towards the senior management or the owner manager position. Nine of the respondents reported that, to some extent the succession plan of their members covered owner or managers. Six respondents admit that the succession plan of their small business members covers senior managers (Table 7.1).

Five respondents reported that none of their members address ownership in their succession plans. Five respondents mentioned that they are not clear whether the succession plan of their members covers board members, while the other six respondents said that the succession plan of their members to some extent covers board members.

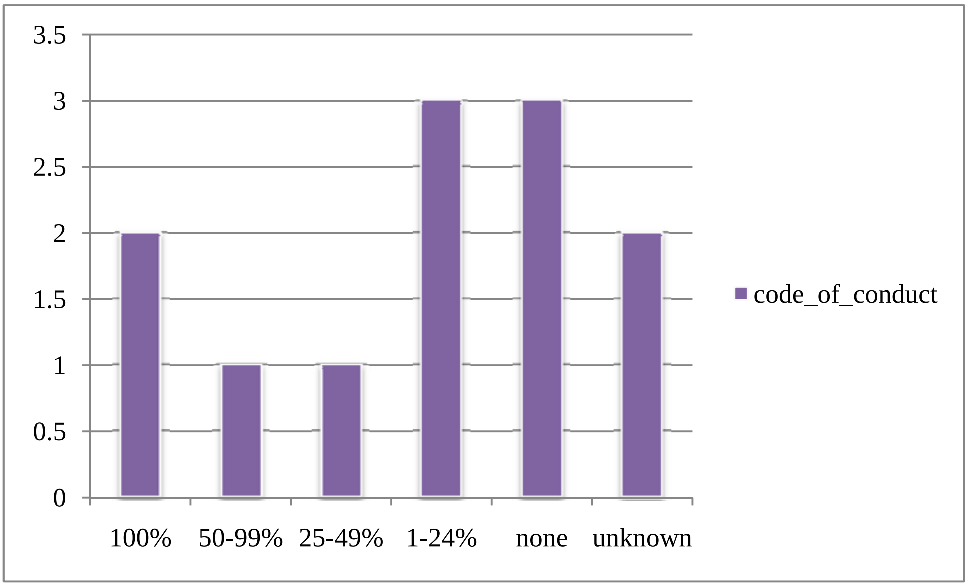
Table 7. 1 Succession plan

	Succession Plan	Succession Plan Covers Ownership	Succession Plan Covers Board Members	Succession Plan Covers Owner/Manager	Succession Plan Covers Senior Managers
100%			1	1	1
50-99%			1	1	
25-49%		1	1	2	1
1-24%	8	2	3	5	6
None		5	1		1
unknown	3	4	5	3	3

7.1.7 Code of conduct

Two respondents confirmed that all their members have a code of conduct. One respondent said 50% to 99% of their members have a code of conduct. One respondent mentioned that 25% to 49% of their members have a code of conduct. Three respondents said less than 25% of their members have a code of conduct. Three respondents said their members do not have a code of conduct. The other respondents are not clear whether their members have a code of conduct or not (Figure 7.4).

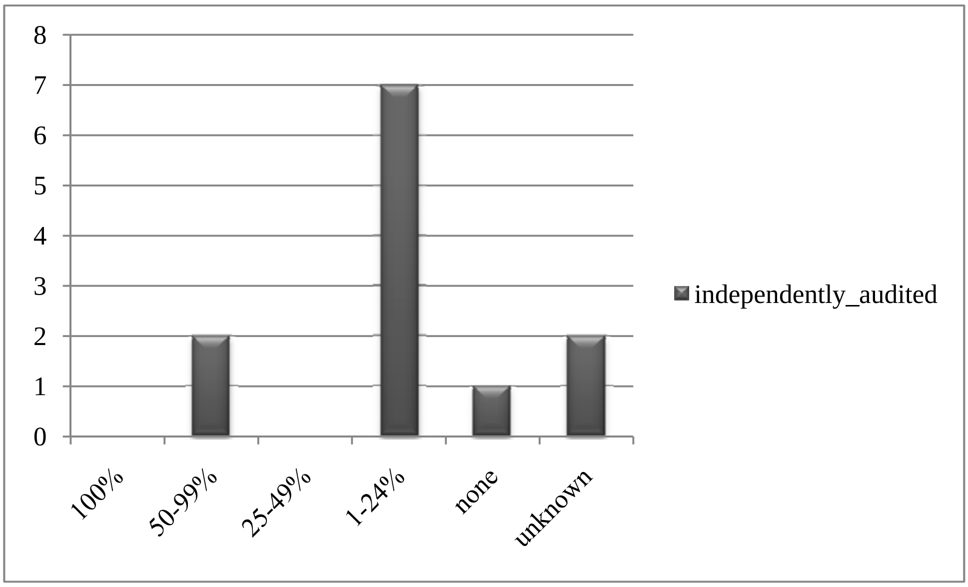
Figure 7. 4 Proportion of small business members having a code of conduct



7.1.8 Independent audit

Seven associations interviewees mentioned that less than 25% of their members are independently audited. Two respondents said that the proportion of their members independently audited was between 50% to 99%. One association said their members are not independently audited and two other respondents are not clear whether their members are audited or not (Figure 7.5).

Figure 7. 5 Proportion of members independently audited



7.1.9 Qualifications of Directors

Among the association CEOs several were directors of their associations. One director said they were a CPA, others were reported to have business expertise, commercial experience and a Diploma.

7.1.10 Decision making

With regards to decision making at the top, most businesses had a CEO/Owner/Manager who was also the managing director and major decision maker. These results show that there is a lack of distinction between owners and managers in small businesses.

7.1.11 Diversity of directors

With regards to diversity, the results of this study showed that, of the 9 small business respondents, only 1 reported having a female director.

In response to a question about whether greater diversity at board level would be of value, only one respondent perceived increased diversity in terms of gender or background would be beneficial.

7.1.12 Board meetings

The number of times the board met annually was reported by only 2 respondents who said their boards met 2-4 times a year.

7.1.13 Conclusion

The first section in this chapter describes the governance regulation and best practices in place in regard to boards in small corporations. The research investigated the formation of a board and its committee structure, the independence of directors, information disclosure, audit, decision making, succession plans, the qualifications and diversity of directors, and the frequency of meetings,

The conclusion from this section of the report, on the formation of boards and compliance with the Corporations Law and best practice governance in small business is that few small businesses have a board and consequently boards, sub-committee structure and independent directors were a rarity. Only 25% of the small corporations represented were believed to have a board. For many small businesses, either a board is seen as not applicable or not necessary.

A board became necessary when a company had more than one shareholder. These usually took a seat on the board due to the need to exercise control over their investments. This confirms previous research which suggested that this happened when a company had moved to a more ‘mature’ stage of development. In practice this seems to be when the number of employees increases and the amount of regulation with BAS, OH&S, etc grows.

In the majority of small companies the operations of the company are managed by the manger/owner who in many cases is the sole director. Hence, the separation of management and control was not an issue. Indeed, it may have been seen as a strength of small business.

Two areas that could (a) promote good governance and (b) monitor results are a code of conduct and independent auditing. Half of the small businesses said that their companies had a code of conduct

Only two of the twenty one respondents reported that their entities were audited. This is not surprising given the small size of both associations, the small businesses in the study and the lack of regulation requiring auditing. However, as associations are responsible to their members, both reporting and information distribution could be expected to be important parts of their functions.

In general, although the industry associations respondents had on various occasions been exposed to financial and operating information, share ownership and voting rights, and foreseeable risk factors, most small business members disclosed information about their companies only to their accountants or for tax purposes.

In relation to succession planning, only four of the responding entities have an established succession plan.

The above description of the small business sector presents a rather diverse picture of a sector that is not overly concerned with corporate governance regulations or best practices.

A purpose of this study was to determine what were the key governance issues that were a problem for the regulation of small business. The following section addresses this question by identifying the difficulties that the small business sector encountered in responding to the regulations.

7.2 Difficulties encountered by small corporations with compliance with regulations, and suggestions for improvement

As discussed in Chapter 4 companies are subject to both external and internal governance mechanisms. External mechanisms such as the Corporations Act are those imposed from outside the corporation. This provides for the structure, formation, termination of companies, the duties of directors, the relationships between shareholders and other stakeholders and confers on companies a separate legal identify. All corporations must be registered by ASIC and, with the exceptions for small businesses outlined in chapter 4, comply with the regulations.

Internal mechanisms are the rules that govern the internal operations of a corporation. Expressed in a company’s constitution or in the Replaceable Rules. These refer to the power of directors, conflicts of interest, appointment, remuneration and removal of directors, managing meetings and the issue of shares and dividends. Compliance with the rules is not required by single owner/operated businesses.

This section examines the extent to which the regulations meet the needs of small business and where there are difficulties, how these could be improved. It also describes the sources of advice to small businesses and the use of information and communication technologies (ICT), as these have a bearing on future communication between government and small businesses.

These issues were investigated by presenting respondents with a list of items drawn from the Corporations Act and asked to rate the difficulties caused by compliance with the item.

7.2.1 Corporate registration and record keeping by small businesses

The small businesses owners were asked if ASIC requirements to provide information and keep records caused any difficulties.

All the small businesses that participated in the study were incorporated and had an ABN number. Most small business respondents confirmed that there were few difficulties with registering a company, or exhibiting the name of the company at its premises.

Compliance with the corporate regulations was in many cases left to accountants. As one respondent said:

The accountant does it all!

It was noted that when starting a business most people did not understand what was required by the corporations law.

Six of the nine respondents commented on the difficulties encountered when notifying ASIC about changes to the company directors, company secretaries and share holdings.

Apart from "*having an adverse reaction to providing information*" the main problems were with the time frames for reporting being "too short" and the penalties were disproportionate compared with an offence. As one respondent said:

Penalties were too high for such a simple thing as a late notification of a change in an address; (small business)

and

ASIC fines and timelines are inappropriate and inconsiderate of the constraints of small business.(small business)

Association CEOs agreed:

ASIC is too inflexible for small business management.(Association CEO)

and there is a

lack of control; regulations are subject to change without knowledge.

It was felt that dealing with ASIC should be easier and that ASIC provided poor phone advice and was not tune with modern IT.

Record keeping (Table 7.2) is in general, not difficult, but the requirements were complex and difficult to understand and follow. It was also time consuming, doubly so because the lack of a skill set for preparing financial documents meant that the task was referred to accountants and incurred associated costs.

Table 7. 2 Record Keeping

Record Keeping
A company must keep in its register of shareholders information including the names and addresses of shareholders and details of shares held by individual shareholders.
A company must keep a register of charges if the company gives a bank, trade creditor or anybody else a charge over company assets.
Each year the company must notify ASIC of any corrections on a printed form, or if an agreement is in place, electronically.
If ASIC or a shareholder with at least 5% of the votes in the company directs, a small proprietary company must prepare an annual financial report (profit and loss, balance sheet, statement of cash flows) and a directors' report (about the company's operations, dividends paid/recommended, options issued, etc).
Proprietary companies must keep sufficient financial records to record and explain their transactions and financial position and to allow true and fair financial statements to be prepared and audited.

One record keeping duty was to keep a register of charges a company gives a bank. These were difficult to understand .The suggestion was made that:

> *When charges are registered with ASIC by a bank, ASIC should send out notices confirming them.*

The suggestion from one respondent was for ASIC's to provide a secure web site where small business people could come in and make the changes on-line. ASIC was also praised for pursuing fraudsters.

There were also comparisons made with the Tax Department. The Tax Department had improved but was slow in confirming opinions and was criticised for back dating opinions. ASIC could be more "user friendly". Regulators should communicate in plain language. As one respondent said:

> *ASIC and ACCC language is confused and convoluted.*

> The comment was also made that

> *Small business is constantly reporting to government through the various regulators, but receives little feedback for the collection of data.*

7.2.2 Directors Duties

Regulation rel[ii]ating to directors duties are listed in Table 7.3.

The CEOS of the associations identified several difficulties with the application of the regulations of the duties of directors to the small business sector. As one CEOS said:

> *ASIC assumes that directors understand their responsibilities (Association. CEO)*

and they

> *Don't understand the consequences of being in breach (Association. CEO)*

> *There needs to be a balance between responsibilities and sanctions for non-compliance*

and

as a matter of natural justice to remove a lot of the strict liability. (Association. CEO)

Associated with this is apathy on the part of small businesses coping with lack of time and resources to comply.

In contrast to association CEOs, small business respondents reported no difficulties with the laws regulating directors duties. In many cases they were seen as not applicable. Single director owner/shareholders did not differentiate between the legal identity of the company as an entity separate from themselves.

Table 7. 3 Directors Duties

Directors duties
To act in good faith
To act in the best interests of the company
To avoid conflicts between the interests of the company and of the director;
To act honestly;
To exercise care and diligence;
To prevent the company trading while it is unable to pay its debts

The requirements of directors' duties that created significant difficulties, were specifically, compensate the company for breaching of the directors' duties, pay back debts incurred by the company, actions towards financial problems, discretion to refuse to register transfer of shares, document execution, winding up and liquidity as well as whether to involve a liquidator should that occur.

In summary, the major difficulties for small business members with regards to directors' duties include:

(1) Rules for the directors are difficult to understand;

(2) A good deal of concern about the level of liability/criminal sanctions regarding directors, ASIC assumes that directors understand their responsibilities;

(3) Too many accountability requirements, and

(4) these imposed a hurdle to attracting high quality directors.

Solutions proposed were that:

- The government should clarify and simplify their rules with regards to the directors' duties and educate the directors.
- Industry associations should be funded to provide training to directors.

7.2.3 Directors decision making

Respondents were asked (Table 7.4) to evaluate on a scale of 1 to 5 the "difficulties to businesses caused by directors decisions that are regulated by the Corporation's Act. For ease of understanding the responses were collapsed into three categories, those which were rated 1 or 2, (Not difficult), 3, and 4 or 5 (Difficult). CEOs rated the provisions that caused the most difficulty as the items "Directors are liable to compensate the company for breaches of directors duties" and "Directors are liable for debts incurred when a company is unable to pay them when they fall due". The least difficult were the requirement to sign documents, decide when a dividend was payable, or appoint a liquidator.

Table 7. 4 CEO Perceptions of difficulties with directors duties

	To what extent do you evaluate the difficulties caused by:	Not difficult		Difficult
	(s1.5.1.3) Directors are liable to compensate the company for breaches of directors' duties	3	4	5
2	Directors are liable for debts incurred what a company is unable to pay them when they fall due.	4	2	6
3	(s1.5.12.1).If a company experiences financial problems, the directors may appoint an administrator to take over the operations of the company to see if the company's creditors and the company can work out a solution to the company's problems. If the company's creditors and the company cannot agree, the company may be wound up	4	3	5
4	(s1.5.9.1). Dividends are payments to shareholders out of the company's after tax profits... The directors decide whether the company should pay a dividend	6	4	2
5	(s1.5.6.5). Directors have a discretion to refuse to register a transfer of shares	5	2	5
6	(s1.5.7).A company may execute a document by having it signed by: two directors of the company; or a director and the company secretary; or for a company with a sole director who is also the sole secretary – that director.	6	3	3
7	if the company is being wound up – to report to and to help the liquidator	4	3	5
8	(s1.5.12.4). A liquidator is appointed to administer the winding up of a company.	5	3	4

7.2.4 Regulations applying to a company's assets and shares

Most of the CEOs did not see major difficulties with these legal regulations (Table 7.5). The most difficulty reported was the limitation on the number of shareholders.

Table 7. 5 Regulations applying to a company's assets and shares

To what extent do you evaluate the difficulties caused by:	Not difficult /NA		Difficult
(s1.5.1.1) A company's money and other assets belong to the company and must be used for the company's purposes	5	3	4
Shareholders are not liable for company debts, only to pay for unpaid amounts on their shares	5	4	3
(s1.5.2.1) A proprietary company must have at least one and no more than 50 shareholders (not counting employee shareholders	5		6
Before issuing new shares, a company must first offer them to the existing shareholders in the proportions that the shareholders already hold	5	5	2
If there is only one shareholder and that person dies, their representative is able to ensure that the company continues to operate.	3	5	4

7.2.5 Replaceable rules of the Corporations Act

The Replaceable Rules of the Corporations Act were described in Chapter 3. The Rules are a model set of internal arrangements to follow if a corporation does not have its own constitution.

Nine industry associations (Table 7.6) out of twelve reported having no difficulties with replaceable rules (75%), partly because they have their own constitution. Two thirds of the small businesses had their own constitution while the remaining three stated that they used the Replaceable Rules.

When asked about the Rules: some responses were:

"No Idea"

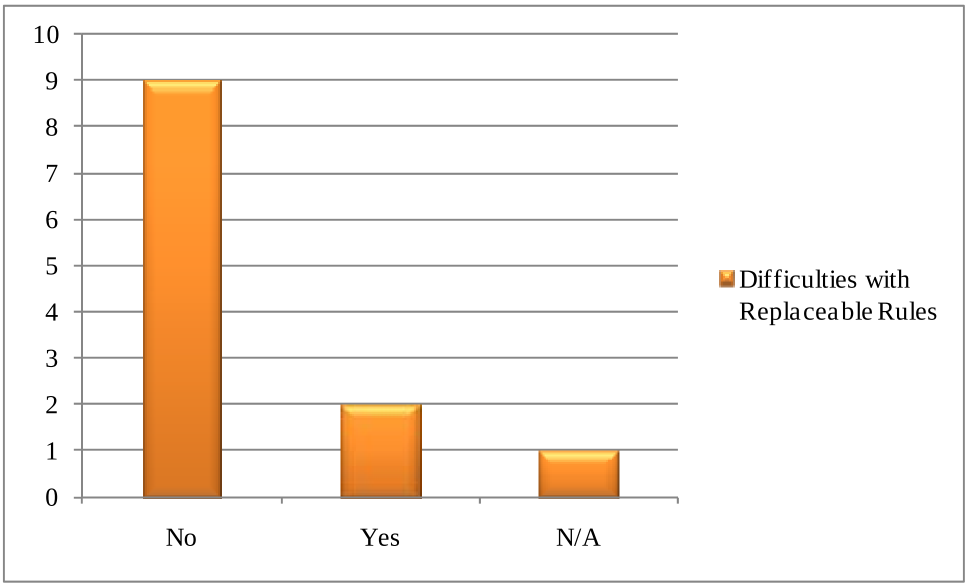
"not applicable"

"different policies"

"Don't know about them"

It appeared that few respondents were aware of the Rules and their role in internal governance.

Figure 7. 6 Difficulties with Replaceable Rules



Some respondents whose organisation used a constitution in preference to the rules indicated that they did so because they felt it was tailored to their organisations specific needs and activities. One respondent also said that the replaceable rules may conflict with their organisation's activities.

7.2.6 Difficulties incurred by different regulatory regimes

The CEOS were presented with a list of issues (Table 7.6) that had been identified in the literature as causing difficulties for small businesses. The small business sample was too small to gauge a reliable response to these items.

The major difficulties were access to finance, tax administration and interest rates. Anticompetitive practices, labour relations and crime were also rated as difficult for the respondents.

Appointment of administrators in times of financial difficulty was too expensive. They had high fees, (often as much as $10K) and “small businesses can’t afford it”

The tax rates were not an issue but the Tax Office administration was both for their lack of timely responses, and for back dating opinions. One respondent said:

Tax rules are too complex for small businesses.

There were recommendations for simplification of tax documentation, although, as one respondent said, that this was despite the fact that the ATO had improved.

In regard to anti-competitive practices, respondents were critical of large monopolies which abused their power. Government Departments such as Trade practices and ACCC do not protect small businesses from big companies. Small business was seen as a “victim of market power”. Government itself was the biggest abuser of power through its contracting, procurement and payment policies. Innovation, Industry, Science and Research (IISR) Small Business division is working well with industry. As one respondent said:

They are notoriously slow and difficult about paying small business for work undertaken, and do not adhere appropriately to agreed contracts.

Table 7. 6 CEO perceptions of other difficulties faced by small business

	Issue	Not difficult		Difficult
1	Telecommunications	6	3	3
2	Carbon reduction	6	2	4
3	Electricity	6	3	3
4	Transportation	6	3	3
5	Access to land	5	3	4
6	Tax rates	3	5	4
7	Tax administration	1	1	10
8	Customs and trade regulations	3	4	5
9	Labour regulations	1	4	7
10	Skills and education of employees	2	5	5
11	Business licensing permits	2	5	5
12	Access to finance	1		11
13	Interest rates		3	9
14	Economic and regulatory policy	1	6	5
16	Corruption	5	4	3
17	Crime, theft, disorder	4	2	6
18	Anti-competitive practices	3	2	7

Labour relations were seen as an issue because:

there is a lot of confusion regarding labour relations and awards which was destabilizing for small business.

Crime, corruption and theft were not major items. However, in relation to money laundering, one respondent said that the new Foreign Investment Review board policy is expected to require employers to report on their own staff

This would be inappropriate and destabilizing for small business.

7.2.7 Other issues of concern

Association CEOs were asked to nominate the three most problematic corporate governance issues facing small corporations today. The following issues were raised further to those already discussed above.

The comment was that new requirement for the ABR register duplicates and increases costs imposed needlessly on small business. The suggestions were that reporting for ASIC and ABR should be streamlined and:

Federal government – provide more supportive export grants;

State government- ease the paper work;

Employee superannuation management is a significant impost on small business. These and the parental leave scheme could be handled through the tax office.

Finally, one respondent summed up their opinion as:

Enforcement and compliance must be rigorous. Many people are getting away with not meeting their obligations.

This respondent felt that there needs to be stronger barriers to entry to a business, perhaps reflected in the capital value of a business. They complained:

They start off with huge ideas, then walk away having spent $2.

7.3 Conclusion: Major issues with governance regulation

There was a general agreement among the CEOs of small business associations that small business owner/managers were not aware of their legal obligations in regard to governance and consequently made little effort to comply. Even if they were aware that there are corporate governance legislation that applied to all businesses, they were written in language that was not understood, and directed to accountants and lawyers.

Several people sought more stability and less changes in regulation, and if there were changes small businesses to be consulted and notified what the changes were.

It was felt that the government should streamline the regulation in regard to small business and that previous efforts for change had been unsuccessful because the efforts were misdirected and resulted in few improvements.

The major problems with governance regulation were:

Small business:

- lack of knowledge of the regulations by small business;
- lack of understanding of the regulations by small business;
- lack of appreciation of the difference between the owner/manager and the company as a separate entity;
- lack of understanding of what it means not to comply with directors duties and governance regulations;
- lack of skills in dealing with regulators;
- reliance on accountants or lawyers and the costs involved.

Regulators:

Inappropriateness of regulation to small business.

- Lack of understanding by ASIC of small business resulting from poor communication, resulting in poor compliance

Recommendations to changes of regulation

The following suggestions arose in the recommendations from the industry association CEOs:

- The regulation requirements, in particular the law, needs to be stabilised and consistent. For example, labour law and health & safety regulations are changing so frequently that it is very difficult for industry associations to follow.
- Second is unified requirements between the States: i.e. adoption of unified definitions in legislation; adoption of standard business reporting; and adoption of uniform hours among the states.
- Third is streamlining the requirements of tax administration and other reporting requirements.
- Governments should improve communication with the industry and small businesses.

Chapter 8

The cost of regulation compliance

The Productivity Commission estimates that the cost of compliance for small business in Australia is $38 billion equivalent to 10.2% of GDP

A major impetus to this study is the desire to reduce the 'regulatory burden'. In general, this refers to the time and costs taken in compliance that may reduce the efficiency of small corporations because of the demands made on their limited resources. This chapter reports the perceptions of the CEOs of the costs of compliance and a comparison of their responses with the responses of the small business corporations to determine if any differences existed. The specific demands of record keeping were discussed in Chapter 8.

8.1 What are the costs of regulation

Quantifying the direct and indirect costs of regulation is such a difficult task that there is no consensus so far on allocating an exact dollar value to regulation. However, the federal government has acknowledged that poorly designed regulation is increasingly becoming an economic burden on business entities, and in particular, on small businesses. In addition, regulation "can increase compliance costs for business, stifle innovation and expansion, and restrict competition" (Sherry 2011, p. 4)[3].

From a stakeholders' perspective, the regulatory burden incurs costs to businesses, governments at various levels, hence taxpayers, and the broader community (Productivity Commission 2006). Putting it specifically, for businesses, the most visible costs are the paperwork burden and related compliance costs, i.e. providing management and staff time to fill in forms and assist with audits, recruiting and training additional staff for the purpose of meeting compliance requirements, purchasing and maintaining IT systems for compliance purposes, obtaining licenses and attending courses to meet regulatory requirements. Beside monetary costs, regulation compliance obligations can distract management attention from

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[3] Sherry, Nick. (2011) Regulatory reform in 2011- a focus on delivery, with a view to the future. Address to the Australian Chamber of Commerce and Industry (ACCI) Economics Committee. 3 March 2011.

the company's core business[4]. In turn, regulation costs can also cause businesses to adjust their processes in ways that such unnecessary costs must be taken into account. Where they hamper the incentives for productive endeavour, they further exert adverse impacts on investment, employment, income, tax receipts and overall economic growth.

The direct regulatory cost to governments at various levels includes the costs in designing, implementing, enforcing, reviewing and updating regulation[5].

The cost of regulation targeting businesses must subsequently be passed on to consumers in the form of higher prices for goods and services. Further, the distorted price regime may restrict consumers' choice and thus decrease the profit of business owners which will further jeopardize business opportunities[6].

Though the direct costs of regulation to businesses, governments and community are worth-noticing, the unintended social and economic side-effects associated with imprudent regulatory designs are yet to be assessed.

Adding up the compliance costs of regulation from the aforementioned aspects, OECD (2001) estimated that in 1998, the Australian small and medium enterprises were imposed some $17 billion in direct compliance costs from tax, employment and environmental regulations. A 2005 study by ACCI (2005) updated that data to $86 billion in 2005, or 10.2% of GDP.

Firm level estimation on the compliance costs of Australian businesses is not readily available, even though this study sheds some light on the compliance costs in terms of man-power and monetary expenses. As a reference, a U.S. study (Crain and Crain 2010)[7]estimated that in 2005, the total cost of federal regulations in US was US$1.75 trillion, with the average being $8,086 per employee for all firms. The federal regulatory cost for business employing less than 20 employees is $10,585, which is far higher than their larger counterparts.

[4] Ibid.
[5] Ibid.
[6] Ibid.
[7] Crain, N. and Crain, M. (2010) The Impact of Regulatory Costs on Small Firms. U.S. Small Business Administration, Office of Advocacy.

8.2 The time spent on compliance

CEO respondents were asked: how many days (equivalent) would you estimate that your staff spent last financial year on meeting compliance costs?

Five industry associations are spending more than 1 month in the last financial year on regulatory compliance (41.67%). Four industry associations are spending 11 days to 19 days on regulatory compliance (33.33%). Two industry associations are spending 20 to 29 days on regulatory compliance and only one industry association is spending less than 5 days on regulatory compliance.

Three of the small corporations reported spending more than a month on regulatory compliance.

It is appalling to find that more than 40% of entities in each group spend more than one month on meeting regulatory compliance requirements, which are not their core businesses.

Table 8. 1 Days spent on regulatory compliance of Industry Associations

Days on compliance	Number of respondents	Percentage
more than 1 month	5	41.67%
11-19 days	4	33.33%
20-29 days	2	16.67%
less than 5 days	1	8.33%

Table 8. 2 Days spent on regulatory compliance of small corporations

Days on compliance	Number of respondents
more than 1 month	3
20-29 days	2
11-19 days	1
less than 5 days	1

8.3 The cost of compliance

Five industry associations spent more than $20,000 each year on regulatory compliance (41.67%). Three industry associations spent $10,000 to $20,000. Two were spending $1,000 to $5,000 on regulatory compliance and another two industry associations were spending $5000 to $10000.

Table 8. 3 Regulatory compliance costs of Industry Associations

compliance cost	Number of respondents	Percentage
more than $20000	5	41.67%
$10000-$20000	3	25.00%
$1000-$5000	2	16.67%
$5000-$10000	2	16.67%

Table 8. 4 Regulatory compliance costs of Small Business

compliance costs	**Number of respondents**
more than $20000	4
$10000-$20000	1
$5000-$10000	1
$1000-$5000	1

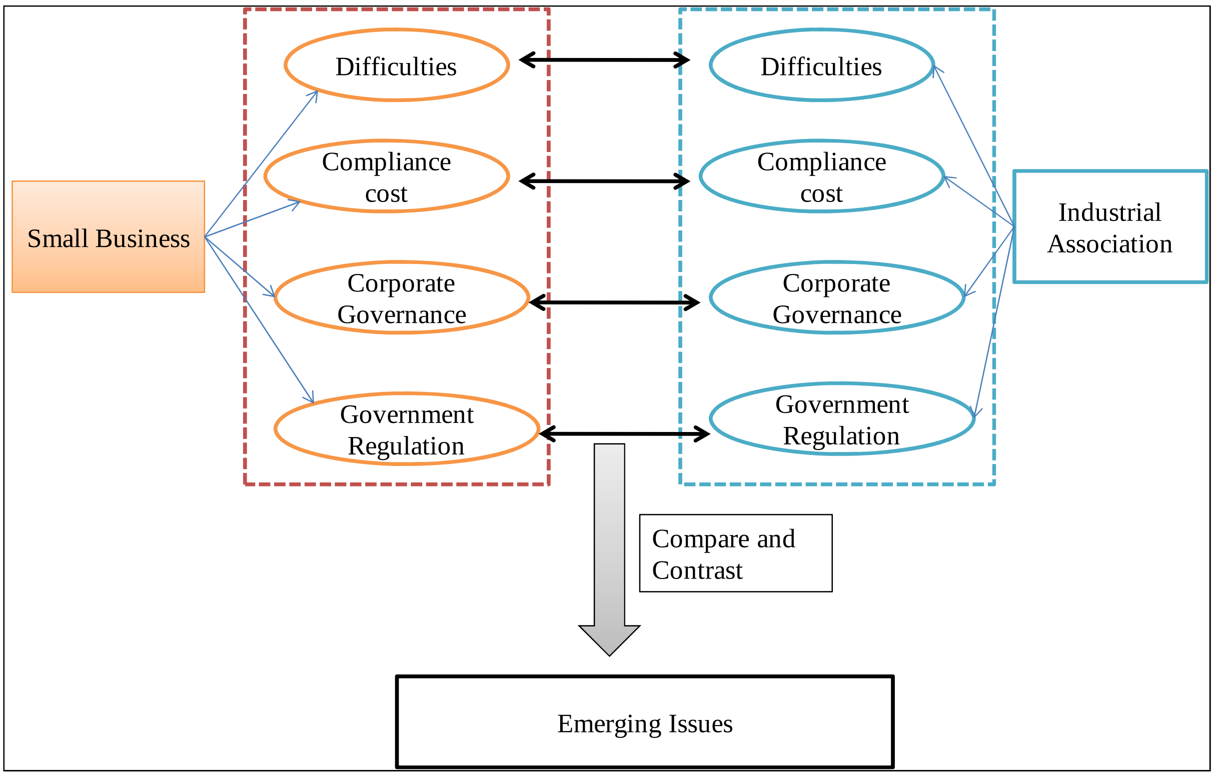
Four of small businesses spent more than $20,000 on compliance cost. The costs to the remaining three small businesses were $10000-$20000, $5000-$10000 and $1000-$5000 correspondingly. Overall, more than 40% of the entities interviewed spent more than $20,000 on compliance costs.

8.4. Compare and contrast of the views of industry associations and small corporations.

This section compares and contrasts the views of small businesses and industry associations on issues relating to the time spent on compliance with government regulation.

Industry associations are both providers of information and services for their members and also serve as a major source of information to governments. The congruence between the industry association views and the small corporations is therefore a crucial test of their reliability and relevance. When the industry associations are well informed they are best able to represent their members and governments are able to rely on them as facilitators and channels of information between the government and their members.

Figure 8. 1 Comparative Framework



8.4.1 Methodology for comparison

Given that the answers are all categorical, Chi-square test can be utilised to detect whether the answers within two small business groups (one is small business, the other one is industry association) are significantly different. The Chi-square statistic is defined as follows:

$$\chi^2 = \sum \frac{(\text{Group1} - \text{Group2})^2}{\text{Group2}}$$

Degree of freedom = (number of options – 1) (number of groups – 1)

Critical values for the Chi-square distribution can be obtained from excel using "chidist" function.

The hypothesis of testing whether the two groups are significantly different is below

H0: The two groups are not significantly different.

H1: The two groups are significantly different.

8.4.2 Government regulation compliance time

The table 8.5 shows that, on average, 42.11% of the organisations spent more than one month on regulatory compliance. 26.32% spent 20 to 29 days for compliance, 15.79% spent less than 5 days.

Table 8. 5 Comparison of two groups on days spent on regulatory compliance

Days on compliance	more than 1 month	20-29 days	11-19 days	Less than 5 days	Tot al	Percent age
Number of small business respondents	3	2	1	1	7	36.84%
Number of industry association respondents	5	3	2	2	12	63.16%
Total	8	5	3	3	19	100.00%
Percentage	42.11%	26.32%	15.79%	15.79%	100.00%	

Computation for Chi-square and the corresponding critical value at 5% significance level is given below

$$\chi^2(2.33, 3) = 0.55$$

$$\text{critical value for } \chi^2(3) = 7.82$$

Given that the actual chi-square value is less than its corresponding critical value at 5% significance level, there is insufficient information to reject the null hypothesis, in other words the null hypothesis is accepted, meaning that there are no significant differences between the perceptions of small business and industry association on days of meeting compliance cost. But the validity of this decision will potentially be hindered by the Type II errors.

Thus, in our sample, nearly seventy percent (42.11% + 26.32%) of the organisations spend more than one month (20 working days) to meet the compliance requirements.

8.5 How to relieve the small business regulatory burden?

Small businesses were asked to recommend any changes to regulations or compliance activities to reduce your costs.

Among the comments were:

Recommend a reductions in number of changes to reduce costs.

Simplification of tax documentation.

Superannuation multiple (40 different) schemes should be simplified.

Bring in super to go with PAYG – the Government can pay funds to the super companies.

Big ones such as Coles and Safeway have the same regulation as small business.

Regulate wholesale prices.

Compliance should be according to the size of a business.

Completion of the auction documentation requirement to give a price/or quote a range is unnecessary and often impossible to comply with or for regulators to enforce. Causes endless changes. It is commercially naive and should be scrapped.

The answers given by the respondents reflect the difficulties discussed above and the perceptions that regulation duplication should be reduced, documentation simplified and that the imposition of similar regulation on small and large business was inappropriate and unfair.

Some respondents identified problems specific to their industry, such as the example from estate agents.

Other difficulties are evident across all small business sectors. As Franco summed up on a Lateline session on small business referring to the constant and repetitive nature of the returns:

> *Every day they need to lodge a company tax return, a business activity statement, PAYG forms to employees, superannuation statements and a fringe benefit statement if they have one during a different time of the year, and with the Australian Securities and Investment Commission, they need to lodge an annual statement*
>
> (Jackie Franco Lateline Business 17/08/2010)

Chapter 9

Factors which inhibit or promote the performance of small businesses

Among the factors which may have a bearing on the performance of small business are the difficulties they face, taxation, the regulation of utilities, influence at government level, the relationship of government and industry, access to finance, level of skills and knowledge, their level of information and communications technology (ICT) expertise and use, and where they obtain information and advice.

9.1 Difficulties for business operations

Respondents were presented with a list of eighteen areas which may have presented a difficulty to their business. Table 9.1 lists some of the major difficulties reported by industry associations. Apart from the following they also identified other difficulties such as customs and trade regulations, labour regulations, lack of skilled & educated employees, access to finance, interest rates, anti-competitive and corporate regulations.

Table 9. 1 Difficulties for the business operation of industry associations

Area of difficulty	Number	Percentage
Tax administration	11	91.7%
tax rates	9	75.0%
carbon reduction	7	58.3%
access to land	7	58.3%
Electricity	6	50.0%
Transportation	6	50.0%
Telecommunications	6	50.0%

9.2 Tax burden

Among the small business respondents 44.4% said tax administration was a cost burden to them.

Tax regulation covers business tax, income tax, GST and other Taxes Freedman (2009) states that there are significant differences between the main forms in which business activities are conducted by small businesses. In order to achieve a more equitable tax system it is important to identify the differences in the business activities, so that those with like means bear similar tax and those with greater means bear higher tax burdens. According to Bradford (2004) regulation can be justified if the benefits provided by the regulation exceeds cost, and if the costs exceed benefits small businesses should be exempted from tax.

One industry association respondent argued that not-for-profit organisations should be receive same tax treatment as their no- profit counterparts, given that both are non-governmental organisations and their operations are roughly the same.

9.3 Superannuation and paid maternity leave

Employment regulations require companies to manage employee superannuation and pay for the maternity leave. One interviewee said the superannuation management is such a drain on their business operation in that, as a small business, they lack the skills to manage superannuation.

One interviewee argued that the requirement for employers to pay employee for maternity leave is a significant cost burden because employee salary is a large portion of the business expenditure. He also maintained that the government is shifting the responsibility of maternity leave payment to businesses without considering the difficulties of small business operation.

9.4 Professional Health and Safety

Employment relationship regulation was regarded as a concern by an industry association respondent. Health and safety requirement is acceptable but signing the contract, in particular the long term contracts, will always be regarded as a potential risk for most of them small business members.

9.5 Re-regulation of monopolies (supermarkets, i.e. Woolworth and Coles)

One interviewee, a local grocery store owner, complained a lot about the lack of government regulation toward monopolies. He mentioned that the monopolies' lobbying for preferential policy, accessing to advanced management & consumer analysis techniques and price advantages from "block ordering" are menacing the destiny of their small competitors. "Both the consumers and suppliers", he continued, "are churning to the monopolies because they provide cheaper and better products". He showed the research group that a lot of the small businesses in his nearby region have gone bankrupt due to unfair competitions. He even wrote a formal letter to advocate the local government for the disadvantaged position of small businesses.

9.6 Re-regulation of the factor market (in particular, utilities, i.e. electricity and water)

One interviewee mentioned that the price of necessities (i.e. electricity and water) are so high that they have to allocate a large proportion into it. According to the Health and Safety requirements, dairy must be frozen 24 hours a day and it consumes a lot of electricity.

9.7 Costs of professional services (in particular, accountants and lawyers, charging too much)

Three respondents from the small businesses and two respondents from the industry association regarded the professional service providers, in particular accountants and lawyers, are “charging too much” for lodging tax documents and looking after their regulatory compliance. The industry respondents even advocate that, given that the regulation is beyond the capacity of small businesses, it may yield better results if regulators could consider regulating the practice and charges of small business related professionals.

9.8 Overlaps and complexity of laws

All the interviewees from industry associations have perceived significant overlaps of laws at local, state and federal levels. Most of them claimed that the legal system is so complex and the updates and overlaps are so significant that not only small businesses, but also professionals, can hardly understand it. Recommendations with regards to the overlaps of small business regarded laws including streamlining the regulation requirements and assigning a task force to develop small business targeted laws.

9.9 Having a Small Business Minister in the cabinet

Small businesses say their voices are not being heard. Yet they account for 96 percent of businesses in Australia, employing an estimated five million people and paying millions of dollars in tax. Therefore, a small business minister in the cabinet would provide a tremendous ability to advocate for small business policy in a whole raft of legislation that government is putting forward.

Two policy analysts from the industry association argued that one of the critical reasons for small business problem being ignored is because small businesses are not represented by someone in particular in the cabinet, and thus “small business concerns were hardly addressed” during the roundtable discussions within the cabinet.

9.10 Governments’ relationships with industry

Government’s lack of understanding of the industry is regarded by the interviewees from the industry associations as one of the barriers that prevent regulators designing better regulation for small businesses. They further argued that industry associations are able to assume the responsibility of facilitating government understanding of small businesses and reinforcing government business relationships. However, the linkage task of small business industry associations has never been recognised by the government in terms of official accreditation and financial support.

The small business participants were asked to recommend three changes to corporate regulation that would facilitate the success of small corporations. Following were the recommendations

“sufficient initial capitalisation by small businesses”

“ More onus on directors and controllers”

“Use of appropriate advisors and professionals”

“Streamlining reporting for ASIC and ABR”

“Simplified processes- once per year reporting”

“Can't do anything”

“ Streamline, get rid of duplication”

“Streamline compliance regulation for small business, leasing compliance fees - state government particularly”

Small businesses suggested changes to regulation were:

"More improved compliance requirements on taxation. More improved compliance requirement with ASIC. (Strengthen regimes) (not enough requirement to make citizens pay their fare share)"

"More stability in regulation"

"Bring in super to go with PAYG- Govt to then pay the funds to Super companies"

"Regulate wholesale prices fair- Compliance according to the size of the business"

"a) Federal - more supportive export grants and

b) State - easing paperwork"

9.11 Small business access to finance

Access to finance is considered a real challenge for small businesses, because they are expected to provide personal assets and mortgages. Apart from the above, providers of external finance requires audited financial reports (McMahon 1999). As a result small businesses find it difficult to obtain finance. Therefore, 80% of new businesses fails due to undercapitalization which is regarded as serious problem for small businesses (Festervand and Forrest 1991). Access to finance by small business was reported as difficult by 33.3% and another 33.3% thought it was not difficult.

As small businesses, only one industry association regarded financing as a concern for their business operation, while others have not perceived it a problem.

9.12 Directors skills and training

As noted above, many of the respondents lacked knowledge of governance and regulation requirements and responsibilities, which makes it necessary to provide them with the skills and training to directors in these areas.

The Table 9.2 shows that nearly half of the directors spent less than 10 days on training. Only one director mentioned that he spent more than a month on training.

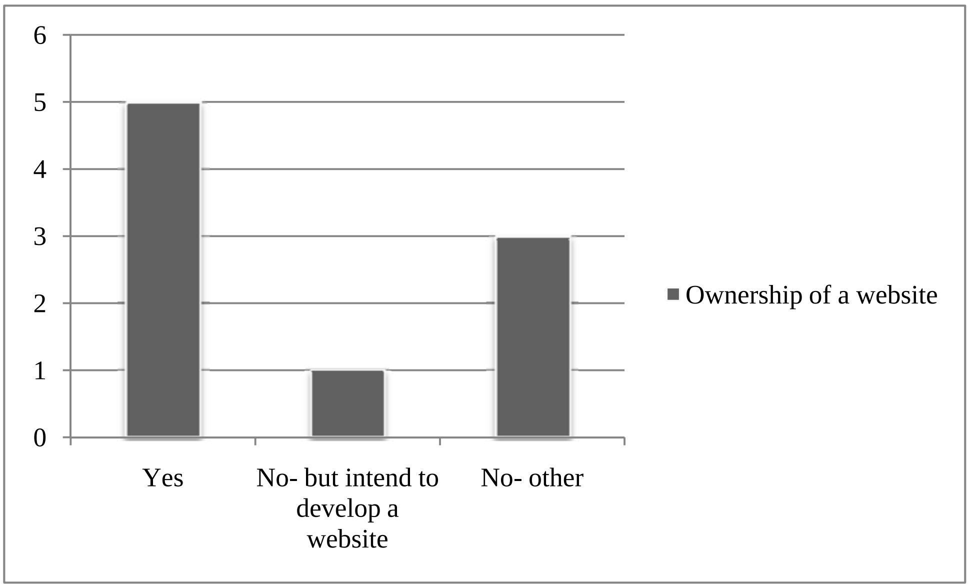
Table 9. 2 Days spent on staff training and professional development of Small Business

Days spent on staff training	Number of respondents
More than 30 days	1
21-30	2
11-20	1
6-10	1
Less than 5 days	2

9.13 Use of ICT

Communication from the government was reported a major difficulty experienced by small businesses. A previous study of small businesses, ICT and accountants, (Armstrong et al 2010) found that better use of technologies would enable government to reduce the burden of compliance with regulation through the development of policies that would encourage small businesses to adopt new technology

Figure 9. 1 Ownership of a web site



The use of communications technology reported by small business was:

Fixed line telephone	88.9% (8),
Internet/web	66.7% (6),
Fax	66.7% (6),
Mobile telephones	66.7% (6),
Email	77.8% (7),
Database	33.3% (3) stated always

There was now growing use of mobiles, and emails. Faxes were used less often and the web was used more often. Approximately half of the small businesses had a web page.

Small business respondents reported use of following ICT for major business activities ranged from never considered to always. Majority of small businesses used ICT tools for business activities.

Table 9. 3 Use of ICT in Small Business for major business activities

ICT Tools	Never considered	Sometimes	Often	Always
Fixed line telephone			1	8
Fax	1	1	1	6
Mobile Telephone		2	1	6
Email	1	1		7
Internet/web	1	2		6
Database	2	1	3	3
e-business	3	2	2	2

Use of Information Communication Technology (ICT) by small businesses to respond to company registration, health and safety reporting and GST were reported as follows:

Use of email was reported as always by 33.3%, sometimes by 22.2% and 55.6 % said they always used internet, whereas fixed line telephones and faxes were used sometimes by 44.4% and 33.3% also stated they sometimes used mobile phones.

Fixed-line telephone, fax, mobile and e-business are used frequently for compliance purposes, while email and internet are always used. Data transmission is the least likely to be used.

Table 9. 4 Use of ICT in Small Business for company registration, health and safety reporting and GST

ICT Tools	Never considered	Sometimes	Often	Always
Fixed line telephone	1	4	2	
Fax	1	4	2	
Mobile Telephone	2	3	1	
Email		2	2	3
Internet/web		1	1	5
Database	4	1	1	1
e-business	2	2	1	2

9.14 Sources of advice

All the industry associations respondents represented their own associations as members of COSBOA. Ninety per cent of the small business associations were members of industry associations, most of which were members of COSBOA.

The major sources of advice to small businesses were accountants, lawyers and industry associations. The most frequently used were accountants. Government agencies had been used by one, and another reported doing a search on Google.

A possibility is that industry association or professionals such as accountant could take a larger role in facilitating communications between government and small businesses.

9.15 Government-industry relationship is weakening

One interviewee mentioned that the government failed to look after the industrial relationship with businesses “at the bottom”. Though small businesses are playing such an important role in the national economy, hardly any of the small businesses’ diversified needs are understood and addressed by policy options. Governments tried unsuccessfully to understand business, but they were not able to, due to various reasons. Industry associations can assume such tasks and reinforce the relationship between government and industry.

9.16 Environmental protection

Protecting the environment is important. Three interviewees mentioned that small business associations and their small business members are very keen on environment protection and they would like to contribute to environment protection.

9.17 Industry association and social networks

The role of industry associations as a nexus for small business social networking and knowledge transfer has yet to be encouraged. Respondents from industry associations admitted that small business associations failed to link the small businesses and government due to lack of financial and official support from the governments.

9.18 Summary

The performance of small business is impacted by various externalities that include taxation, the direction of regulation of utilities, and access to finance. Government’s response to the sector depends on the ability of small business to influence government, on the level of access to government, the relationship of government with industry, the latter most often represented by industry associations.

Internal factors which can promote performance are high levels of skills and knowledge by owner/manager/directors, their expertise in the use of information and communications technology (ICT), and ability to obtain information and advice. This is to some extent dependent on their relationship with and the quality of their sources of advice and information, professionals such as accountants and lawyers and their industry associations.

Emerging issues that will be important in the future are the environment and social networking, and social responsibility.

Chapter 10

Conclusion

Australia's small corporations play a vital role in national economic and social wellbeing. The purpose of this project is to develop a responsive regulatory model for small corporations drawing together the experiences of small corporation's owners/mangers, CEOs of industry associations, regulators, the Federal Treasury, industry leaders and academic experts.

The project is being conducted in four stages. The first stage was designed to identify the theoretical stances found in previous research that would support the appropriate design and direction of the regulation of small business. Stage two, in-depth interviews with CEOS of small business associations and small businesses owner/managers, is the subject of this report. The next steps are to survey a sample of small business proprietors and to canvas the outcomes and recommendations with the regulators.

The aims of this study, stage two of the project, were to determine what are the factors which inhibit or promote good governance in small corporations and what kinds of regulation, or some other approach, will best achieve the desired outcomes.

The research questions were:

- What were the key governance issues that were a problem for the operation and growth of small business?
- What is the aim of corporate governance regulation of small corporations?
- What are the real issues that inhibit efficiency and effectiveness in small businesses?
- What could the regulators do to improve regulation of small corporations?

10.1 Small business in Australia

The scope of this study was restricted to compliance with the governance requirements of the Corporations Law and to corporations defined as 'small' under the Corporations Act and that are not public or listed companies.

The definition of small business adopted in this research is that of S45A of the Corporation's Act:

A proprietary company is a small proprietary company for a financial year if it satisfies at least two of the following:

- consolidated gross revenue of less than $25 million;
- value of consolidated gross assets less than $12.5 million; and
- fewer than 50 full-time equivalent employees.

Small corporations comprise more than 99% of all firms, employing more than 5 million people. As indicated in chapter two, they make a major contribution to Australian economic activity contributing over half of the value added by business to the Australian economy.

Of the over 2 million small entities, 32% are registered companies, 29% are sole operators and 17% are partnerships. SMEs accounts for about 99.71% of all private sector entities, while large firms never exceeded 1% of aggregate firm numbers during 1983-2007 (Australia Bureau of Statistics 2007).

The analysis of the small businesses in chapter two showed that they are concentrated in industries of Communication, Finance, Insurance, Property and Business Services. Overall, the small business sector operates with a higher profit margin than big business. This seems to suggest that despite the concentration of regulation on big business, it is in the small business sector where return on investment may be highest for the economy.

10.2 Regulation and corporate governance

Regulation is the means by which governments set requirements on enterprises and citizens. In the business environment, these may be to prohibit undesirable behaviour to promote and facilitate action that will improve the efficiency and operations of the business sector and its contribution to the economy.

Three theories of regulation canvassed in Chapter 3 were public interest, private interest and institutional theories. Public interest theory identifies the responsibilities of the regulators in designing and implementing regulation. Private interest theory draws on economic assumptions about how responses to regulation will be driven by the pursuit of self interest. Institutional theory suggests that regulation should be responsive to the needs of those being regulated. One aspect of institutional theory is “Tripartism” which is defined as a regulatory policy that fosters participation with relevant private interest groups in which the groups operate as private sector regulators, with access to same information and the same standing to sue or prosecute under the regulatory statute as the regulator. Industry associations and organizations provide a forum for negotiations with politicians and regulators and constrain the actions of individual member firms. It is the balancing act between speaking with a united voice, and actually being heard by Government, which neatly proscribes the role of COABOA and other industry associations in the law reform arena.

Corporate governance (Chapter 4) is the framework of rules, relationships, systems and processes within and by which authority is exercised and controlled in corporations. The most significant theories of governance are agency theory and stakeholder theory. Agency theory, which addresses the problems of conflicts of interests between owners and managers of corporations, fits most readily with private interest theories of regulation. Stakeholder theory is about the responsibilities of business to those who impact on a business or are impacted by its operations (shareholders, employees, consumers, etc). Responsive regulation reflects many of the issues addressed by stakeholder theory.

The purpose of regulation of corporate governance is to reduce risk and maintain order and confidence in the corporate capital market and to safeguard the investments of shareholders. Regulation of the governance of corporations in Australia is largely captured in the Corporations Law which is administered by the Australian Securities and Investment Commission (ASIC). Responses from the small business participants in the study showed that many comments about corporate regulation also applied to regulation by ACCC, ATO and APRA, although the impacts of their regulations were not directly addressed by this project,

10.3 The Corporations Law as a regulatory scheme for small companies

The Australian law provides a low entry cost to the market. That is, a company, as a ‘registrable body’ under Australian law, can be inexpensively and quickly established under s117 Corporations Act 2001. In most respects, small and large firm are undifferentiated under the Act. They were the same as large companies until 1995 when, as part of the *First Corporate Law Simplification Act*, it was first proposed that proprietary companies would be divided into small and large. Several amendments to regulations contained in the Act can be found in Part 1.5, a Small Business Guide, that summarises the main rules that apply to small businesses. The major differences between the main provisions of the Act and the Guide are that if there is a single shareholder/director, Replaceable Rules and meeting rules do not apply, annual reports do not have to be submitted to ASIC, and a resolution can be passed by the single director recording and signing the resolution.

The difficulties that regulation poses for small businesses is well known. Chapter 3 discusses the burden of regulation for small business. The difficulties for policy makers are also noted. Their major challenge is how to ensure that laws treat all businesses equally and fairly, and so promote full competition, yet still take into account the unique nature of small enterprises.

This study provides some of the research evidence required to support the fairer regulation of the small business sector. The following summarises the results of the interviews and the small business perceptions of the major problems with the governance regulation.

10.4 The results of the interviews

The responses to the interviews addressed the research questions: What were the key governance issues that were a problem for the operation and growth of small business? What are the real issues that inhibit efficiency and effectiveness in small businesses?

There was a general agreement among the CEOs of small business associations that small business owner/managers were not aware of their legal obligations in regard to governance. For this reason they reported few difficulties with the regulation. Compliance with legal obligations was managed by their accountants and lawyers and they were apathetic in regard to complying with bet practice governance. Even if they were aware that there were corporate governance legislation that applied to all businesses, they were written in language that was not understood, and directed to accountants and lawyers.

Several people sought more stability and less changes in regulation, and, if there were changes, they wanted to be consulted and notified what the changes were.

It was felt that the government should streamline the regulation in regard to small business and that previous efforts for change had been unsuccessful because the efforts were misdirected and resulted in few improvements.

The major problems with governance regulation were for:

Small business:

- Lack of ability to influence government by small business
- lack of knowledge of the regulations by small business;
- lack of understanding of the regulations by small business;
- lack of appreciation of the difference between the owner/manager and the company as a separate entity;
- lack of understanding of what it means not to comply with directors duties and governance regulations;
- lack of skills in dealing with regulators;
- reliance on accountants or lawyers and the costs involved.

Regulators:

Inappropriateness of regulation to small business.

- Lack of understanding by ASIC of small business resulting from poor communication, resulting in poor compliance
- The regulation requirements, needs to be stabile and consistent.
- Unified requirements between the States: i.e. adoption of unified definitions in legislation; adoption of standard business reporting; and adoption of uniform hours among the states.

- Streamlining the requirements of tax administration and other reporting requirements.
- Governments should improve communication with the industry and small businesses.
- The most problematic corporate governance issues facing small corporations in Australia today were reported as follows:

Table 10. 1 Initiatives and policy options suggested by respondents

Initiatives	Policy Options
Actions by Governments	A Small Business Department
	Get rid of duplication: A whole-of-government reporting regime for ATO, ASIC and ACCC
	Unified requirements between the States
Changes to inappropriate regulations for the small business sector	Review of liability and criminal sanctions regarding directors.
	Create separate legislation for small business compliance related to the size of the businesses, with their own replaceable rules, in plain simple language..
	Exclude small business single owner/operators from governance regulation
	Make accountants accountable, not the businesses
Improve communication with the small business sector	Consultation with the small business sector prior to introducing changes to regulation
	Form clusters or networks of small business advisors to

	advise the regulators. Collect and distribute information about the growth and performance of small business and new developments at a level that small business understands. Require all small businesses to be members of business associations and use business associations as a vehicle to connect regulators and small businesses.
Improve ASIC inflexibility	Develop a new communication/consultation strategy similar to the ATO consultative committees Develop web page suitable for and accessible to small business Provide access to a friendly and free advisory service Review charges and time frames for compliance Regulate fair prices for businesses based on compliance
Address small business lack of knowledge and understanding of governance	Develop specific national curriculum on governance for delivery to small businesses Develop new training packages and modes of delivery

Policy options put forward by the respondents in response to the difficulties identified in the study are summarised in Table 10.1.The include action suggested by the respondents to changes by Australian governments, improvements in communication, changes to accountability, and suggestions for ASIC.

Another suggestions was for greater representation of small business in cabinet. While the Treasury, has a Business Liaison Program and the ATO and other government agencies conduct various surveys relevant to their needs, they are almost exclusively directed at the large business corporations. Yet, as discussed above, although they represent only 1% of the business community they are the ones able to put their views to the government. In the recent debate about a mining tax, the three biggest mining firms were given the opportunity to negotiate directly with senior members of the Government. As such, they gained particular rights to seek to resolve the political impasse at the Federal level. This exclusive club was so obvious in public-political terms that second tier and third tier firms resorted to complaining loudly to being shut out of the process. In regulation and regulation reform, the law appears instinctively to striate the market into layers relevant to firm size and political capacity. This works against the interests of small firms who lack political resources.

Table 10.2 address the research question: What could the regulators do to improve regulation of small corporations? Recommendations for changes to the Corporations Law (Table 10.2) that emerged from the study include initiatives to reduce the time and costs of small corporations, changes to director requirements, and collecting data and adopting the same definitions for SMEs across all Government agencies. These raise the questions:

- Should the regulators reduce the ‘staying incorporated’ time and costs for small corporations? How could this be done? Should the small business definitions be expanded? How can the corporations Act be made more ‘user friendly’ for small businesses?
- Should entry to business be made more difficult? Should there be character or competency requirements for directors? Should the $2 capital threshold be raised to something more meaningful?
- How can we obtain better information about small businesses? Can definitions be made consistent across all governments and regulatory authorities? Should ABS conduct a regular census of small businesses?

Table 10. 2 Options for changes to the Corporations Laws

Initiative	Policy options
Reduce the ‘staying incorporated’ time and costs for small corporations	• Have a triennial statement, rather than the part 2N annual statement. • Annual solvency requirement be explored to reduce stress and expense. • Changes to s294: Provide that shareholders must hold 20% of shares (up from 5%) in order to have an audited set of accounts lodged. Raising the threshold to 20% then refers to a mainstream cohort of shareholders, rather than a disaffected minor rump at 5%. • Expand the small business guide part 1.5, sIIIJ. Have it as a stand-alone piece of the Act, or as a differentiated from the Act. Colour code the pages in the Act for easier identification for small corporations. This is a tangible, cost effective, visual means of making particular provision for small firms. • Include Replaceable Rules, Part 2B, ss 134-136, as part of or adjacent tot he small business guide, rather than as separate and hard to locate within the Act. Colour-code them in the Act. • Increase the definition of small companies to include more firms. Keep the two our of three criteria, but double the criterion (a) and (b0. That is in S45A (2) increase the the revenue test to %50 million from $25 million, and increase gross assets to $25 million from $12.5 million. Criteria (c) could also be increased from 50 to 100 employees.
Raise the entry costs to incorporation	• Raise the entry requirement for directors. focus on director track record at the incorporation stage. • Require training and instruction in the role and responsibilities of directors. • Require a simple character/competency test for potential directors. (Are they fit for purpose? Avoid the Re city equitable example of no viable directorial standards). • Be rigorous with disqualification of directors. • Raise the $2 capital threshold to something meaningful.
Provide information and consistency in small business data collections	• Audit commonwealth statute and regulations for definitions relevant to small corporations and small business • Settle on fixed definitions • Define SMEs and small corporations and other terms consistently across different Commonwealth contexts • Align ABS and regulatory definitions , e.g. in all Commonwealth statutes, • Introduce at least tri-annual census of small businesses

Some regulatory changes could make it easier for small business owner/mangers and reduce time and costs. Others, to expand the definition of small businesses, would make it easier for small businesses to incorporate and reduce the demands on reporting until later stages in their development. The effect will be to rely for due diligence from banks. This will reflect the reality that banks will require personal guarantees from the key personnel of small corporations and will do a lot of the due diligence for financial competence.

These changes are intended to allow ASIC to give greater leeway to small firms in their formative stages to grow more quickly in the start up and ‘gazelle’ phase, and to let them focus on survival and growth, rather than compliance and reportage. These changes would allow the Commonwealth to set the tone for other areas of regulation relevant to small corporations.

A basic fit-for-purpose test for directors accompanied by appropriate training for the directors of small corporations, would raise the qualifications expected of directors and should be reflected in performance.

Finally, any policy initiative put forward at this time suffers from inadequate and consistent data. Data on small businesses used in this study is based on the ABS 2007 collection. Despite its limitations it is more useful to have some information than no information. Because of the gap in knowledge about small businesses in 2011, the changes taken place in the economy since the GFC are most probably only partially reflected n this study. ABS is the prime source of data collection. It and the Corporations Law should be consistent. Agreement in definitions should be established and adopted by all Governments in Australia and regular census of small businesses introduced.

Australia needs a system of regulation that promotes economic activity. If small business is ‘the engine of growth’, then regulators must make it easy for the small business sector to flourish and enable it to make the contribution it promises to the economic prosperity of both the families and employees of the nation’s entrepreneurs and to the nation.

10.5 Future directions

Over the last fifteen years Governments in Australia have embarked on major programs of regulatory reform. Actions taken to reduce the regulatory burden include better quality regulation design, communication, and simplification. Approaches to managing compliance include a responsive regulatory approach (refer to Chapter three) that responds to the needs of those being regulated. It also places an onus on those regulated to be responsive to government efforts, and to co-operate in building strategic alliances with the regulators and setting the regulatory standards. This approach is reflected in the performance based adoption of regulations and risk-based approaches to compliance.

This project is complementary to this approach. This report of the second stage in the study presents a comprehensive analysis of the profile of small business in Australia, and the perceptions of the small business sector specifically in regard to governance and its regulation.

The study is limited by the number of respondents. Nevertheless, those CEOs who participated were selected for their expertise and the positions that they hold as leaders of the various associations which are members of the Council of Small Business Associations. Similarly, the small business respondents were selected for their expertise and in-depth knowledge of small business.

The conclusions from the study are also affected by the availability of statistical information. The study presents the most recent small business data available in Australia. ABS data for the year 2007 was used in the development of a small business profile. This cannot reflect the changes in the economy since 2007 nor how small business may have been impacted by the global financial crisis (GFC) of 2008. Further research is required in this area.

Another problem is the different definitions of small business used by the ABS and the Corporations Act discussed in Chapter one. It is extremely difficult to cross-tabulate data from various sources if the definitions and analyses are using different criteria. As stated above agreement on definitions of small business should be established across all Governments.

While the present study has its limitations it makes a significant contribution to identifying the issues which small business industry associations regard as significant to the welfare and performance of small corporations.

The next steps in this research are a Small Business Forum to confirm with the Small Business sector the important issues that should be addressed by regulators and how they should be addressed. At the same time the research team will be seeking a larger sample with randomly selected respondents so that the results of this study can be verified and the results analysed with greater reliability.

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1. SECTION A: INTERVIEW DETAILS

1. Case number

2. Interviewer name

3. Interview date

4. Interview time

5. Respondent name

6. Association name

7. Company name (if different from the association name)

8. Address and contact telephone number

9. Industry your association represents

- ☐ 1 Agriculture, Forestry and Fishing
- ☐ 2 Mining
- ☐ 3 Manufacturing
- ☐ 4 Electricity, Gas, Water and Waste Services
- ☐ 5 Construction
- ☐ 11 Financial and Insurance Services
- ☐ 12 Rental, Hiring and Real Estate Services
- ☐ 13 Professional, Scientific and Technical Services
- ☐ 14 Administrative and Support

- ☐ 6 Wholesale Trade
- ☐ 7 Retail Trade
- ☐ 8 Accommodation and Food Services
- ☐ 9 Transport, Postal and Warehousing
- ☐ 10 Information Media and Telecommunications

Services

- ☐ 15 Public Administration and Safety
- ☐ 16 Education and Training
- ☐ 17 Health Care and Social Assistance
- ☐ 18 Arts and Recreation Services
- ☐ 19 Other Services

10. State your association represents

- ☐ 1 Vic
- ☐ 2 NT
- ☐ 3 SA
- ☐ 4 Qld
- ☐ 5 NSW
- ☐ 6 ACT
- ☐ 7 WA
- ☐ 8 Tas
- ☐ 9 National

11. ABN

[ ]

12. Does your organisation have a web site?

- ☐ 1 Yes [ ]
- ☐ 2 No - but had a web site in the past
- ☐ 3 No - but intend to develop a web site
- ☐ 4 No - (Other: …………………………….)

13. Are you, or is your organisation, a member of any industry or professional associations?

- ☐ 1. No (GO TO Section B)
- ☐ 2. Yes (GO TO Question 14)

14. Which association/s is that?

[ ]

2. SECTION B: BUSINESS DETAILS

1. Is your organisation a ___?

- ☐ 1 Public company (GO TO question 2)
- ☐ 2 Private company (GO TO question 3)
- ☐ 3 Sole proprietor (GO TO question 3)
- ☐ 4 Partnership (GO TO question 3)
- ☐ 5 (Other:………………) (GO TO question 3)

2. Is your organisation a listed company? (i.e. trades shares on the stock exchange)

☐ 1 Yes ☐ 2 No

3. How many members does your organisation have?

____

4. How many sites does the business have in Australia?

____

5. How many overseas sites does your organisation have?

____

6. Does your organisation operate in or provide services in countries other than Australia?

☐ 1 Yes. How many? ☐ 2 No

____

7. What is the value of your organisation's total assets?

- ☐ 1. Less than $5 million
- ☐ 2. $5 million to $10 million
- ☐ 3. $10 million to $12.5 million
- ☐ 4. $12.5 million to $15 million
- ☐ 5. $15 million to $20 million
- ☐ 6. $20 million to $25 million
- ☐ 7. $25 million or more
- ☐ 8. Unknown

8. How many days (equivalent) would you estimate your staff have spent last financial year on meeting compliance costs? (e.g. filling forms, reading and

understanding regulatory requirements, consultation with regulators / accountants)

- [ ] 1. Less than 5
- [ ] 2. 6-10
- [ ] 3. 11-19
- [ ] 4. 20-29
- [ ] 5. 30 +
- [ ] 6. unknown

9. How much would your firm have spent last year on meeting compliance costs? (Tax, Super., environment, HR/OH&S, BAS, GST, and other documentation & reporting burdens)

- [ ] 1. less than $1,000
- [ ] 2. $1,001- $5,000
- [ ] 3. $5,001 - $10,000
- [ ] 4. $10,001 - $ 20,000
- [ ] 5. $20,001 +
- [ ] 6. unknown

10. Are any of these areas a particular cost burden to your organisation?

- [ ] 1. Access to financing (e.g., collateral required or financing not available from banks)
- [ ] 2. Cost of financing (e.g., interest rates and charges)
- [ ] 3. Telecommunications
- [ ] 4. Electricity
- [ ] 5. Transportation
- [ ] 6. Access to land
- [ ] 7. Title or leasing of land
- [ ] 8. Tax rates
- [ ] 9. Tax administration
- [ ] 10. Customs and trade regulations
- [ ] 11. Business licensing and permits
- [ ] 12. Labour regulations
- [ ] 13. Skills and education of available workers
- [ ] 14. Uncertainty about regulatory policies
- [ ] 15. Functioning of the judiciary
- [ ] 16. Corruption
- [ ] 17. Anti-competitive practices of other competitors
- [ ] 18. Contract violations by customers and suppliers

11. Would you recommend any changes to regulations or compliance activities to reduce costs to your organisation?

12. How often does your organisation use the following Information and Communication Technology (ICT) tools to respond to company registration, Health and Safety reporting and GST?

	1. Never consider it	2. Sometimes	3. Often	4. Always	5. Outsource to others
1. fixed-line telephone	☐	☐	☐	☐	☐
2. fax	☐	☐	☐	☐	☐
3. mobile telephone	☐	☐	☐	☐	☐
4. email	☐	☐	☐	☐	☐
5. internet	☐	☐	☐	☐	☐
6. database	☐	☐	☐	☐	☐
7. e-business	☐	☐	☐	☐	☐

13. Would you recommend any changes to regulations that would promote your organisation growth?

☐ 1. Yes (Go to Question 14) ☐ 2. No (Go to Section D)

14. What changes to regulations do you recommend?

3. SECTION C: CORPORATIONS LAW

The next set of questions is about issues to do with the corporations' law

1. Does your organisation have its own constitution or does it use the model (Replaceable Rules) specified in the Corporations Act (the default arrangement)?

☐ 1. The organisation has its own constitution (GO TO question 2)

- [ ] 2. The organisation uses the model in corporate Replaceable Rules (GO TO question 3)
- [ ] 3. Others____________ (GO TO question 4)
- [ ] 4. Unknown

2. Are there any difficulties that you are aware of with the Replaceable Rules?

- [ ] 1. No
- [ ] 2. Yes (Please GO TO Question 3)

3. What are the key difficulties that you are aware of with the Replaceable Rules?

4. What are the main sources of advice about corporate governance used by members (small businesses) of your organisation?

- [ ] 1. Our industry/prof. association
- [ ] 2. Lawyer
- [ ] 3. Accountant
- [ ] 4. Govt/regulatory agency
- [ ] 5. Other peak body
- [ ] 6. Other: ....
- [ ] 7. No external sources used
- [ ] 8. Don't know

5. Which of the sources of advice in Question 4 do your small business members use the most?

- [ ] 1. Our industry/prof. association
- [ ] 2. Lawyer
- [ ] 3. Accountant
- [ ] 4. Govt/regulatory agency
- [ ] 5. Other peak body
- [ ] 6. Other: ....
- [ ] 7. No external sources used
- [ ] 8. Don't know

6. What proportion of your members would have a board of directors?

- [ ] 1. 100%
- [ ] 4. 1-24%

- ☐ 2. 50-99%
- ☐ 3. 25-49%
- ☐ 5. None (GO TO Question 8)
- ☐ 6. Unknown (GO TO Question 8)

7. How many would have independent directors? (ie not employees, substantial shareholders or suppliers to/ customers of the business)

- ☐ 1. 100%
- ☐ 2. 50-99%
- ☐ 3. 25-49%
- ☐ 4. 1- 24%
- ☐ 5. None
- ☐ 6. Unknown

8. Do these companies separate the roles and responsibilities of the board and management?

- ☐ 1. No
- ☐ 2. Yes. How? ________________________________

9. Do they have processes to monitor and review the separation of the roles of the board and management?

- ☐ 1. No
- ☐ 2. Yes

10. What proportion of your small business members would have

	1. 100%	2. 50-99%	3. 25-49%	4. 1-24%	5. None	6. Unknown
An audit committee	☐	☐	☐	☐	☐	☐
A risk management committee?	☐	☐	☐	☐	☐	☐
A remuneration committee?	☐	☐	☐	☐	☐	☐
Have a nomination committee?	☐	☐	☐	☐	☐	☐

11. What proportion of your small business members would disclose information:

	1. 100%	2. 50-99%	3. 25-49%	4. 1-24%	5. None	6. Unknown
relating to the financial and operating results of the corporation?	☐	☐	☐	☐	☐	☐
major share ownership and voting rights?	☐	☐	☐	☐	☐	☐

	1. 100%	2. 50-99%	3. 25-49%	4. 1-24%	5. None	6. Unknown
material foreseeable risk factors?						

12. What proportion of your members would

	1. 100%	2. 50-99%	3. 25-49%	4. 1-24%	5. None	6. Unknown
have established a succession plan?						
if have a succession plan, it covers ownership?						
if have a succession plan, it covers board members?						
if have a succession plan, it covers owner/manger?						
if have a succession plan, it covers senior management?						

13. What proportion of your members would

	1. 100%	2. 50-99%	3. 25-49%	4. 1-24%	5. None	6. Unknown
have a code of conduct?						
be independently audited?						

4. SECTION D: RECORDS

1. How would you rate the difficulties caused by the following issues to your small business members (1 = not difficult at all, 5 = most difficult)

	1	2	3	4	5
1. A company must keep in its register of shareholders information including the names and addresses of shareholders and details of shares held by individual shareholders.					
2. A company must keep a register of					

	1	2	3	4	5
charges if the company gives a bank, trade creditor or anybody else a charge over company assets.					
3. Each year the company must notify ASIC of any corrections on a printed form, or if an agreement is in place, electronically.	☐	☐	☐	☐	☐
4. If ASIC or a shareholder with at least 5% of the votes in the company directs, a small proprietary company must prepare an annual financial report (profit and loss, balance sheet, statement of cash flows) and a directors' report (about the company's operations, dividends paid/recommended, options issued, etc).	☐	☐	☐	☐	☐
5. Proprietary companies must keep sufficient financial records to record and explain their transactions and financial position and to allow true and fair financial statements to be prepared and audited.	☐	☐	☐	☐	☐

2. What are the main difficulties for your small business members?

3. What could be done to overcome or minimise this problem?

5. SECTION E: DIRECTORS' DUTIES

1. To what extent would you evaluate the difficulties to your small business members caused by each of the following factors (1 = not difficult at all, 5 = most difficult):

	1	2	3	4	5
1. Directors are liable to compensate the company for breaches of directors' duties.	☐	☐	☐	☐	☐
2. Directors are liable for debts incurred what a company is unable to pay them when they fall due.	☐	☐	☐	☐	☐
3. If a company experiences financial problems, the directors may appoint an administrator to take over the operations of the company to see if the company's creditors and the company can work out a solution to the company's problems. If the company's creditors and the company cannot agree, the company may be wound up.	☐	☐	☐	☐	☐
4. Dividends are payments to shareholders out of the company's after tax profits. The directors decide	☐	☐	☐	☐	☐

	1	2	3	4	5
whether the company should pay a dividend.					
5. Directors have discretion to refuse to register a transfer of shares.	☐	☐	☐	☐	☐
6. A company may execute a document by having it signed by two directors of the company; or a director and the company secretary; or for a company with a sole director who is also the sole secretary – that director.	☐	☐	☐	☐	☐
7. If the company is being wound up – to report to and to help the liquidator.	☐	☐	☐	☐	☐
8. A liquidator is appointed to administer the winding up of a company.	☐	☐	☐	☐	☐

2. Looking at the major difficulties identified above, what could be done to minimise the difficulties?

3. What are the other difficulties for your small business members have you perceived?

4. What could be done to overcome or minimise this problem?

6. SECTION F: LEGAL DIFFICULTIES FOR COMPANIES AND DIRECTORS

1. How would you rate the difficulties caused by the following issues for your small business members (1 = not difficult at all, 5 = most difficult)

	1	2	3	4	5
1. A company's money and other assets belong to the company and must be used for the company's purposes.					
2. Shareholders are not liable for company debts, only to pay for unpaid amounts on their shares.					
3. A proprietary company must have at least one and no more than 50 shareholders (not counting employee shareholders).					
4. Before issuing new shares, a company must first offer them to the existing shareholders in the proportions that the shareholders already hold.					
5. If there is only one shareholder and that person dies, their representative is able to ensure that the company continues to operate.					

7. SECTION G: MAJOR ISSUES WITH REGULATION

Please tell us if any of the following issues are a problem for the operation and growth of your business. For each item, I'll ask you to indicate the extent to which you think the issue poses difficulties, of any type, for the small corporations such as yours.

1. In summary, what would you nominate as being the three most problematic corporate governance issues facing small corporations in Australia today?

2. And, what three changes to corporate regulation would you recommend to facilitate the success of small corporations?

3. In your opinion, what have been the most positive changes or trends in the corporate governance area in recent years? (Regulatory change, changes in business practices, etc)

4. How would you rate the difficulties caused by the following issues for your small business members (1 = not difficult at all, 5 = most difficult)

	1	2	3	4	5
1. Telecommunications	☐	☐	☐	☐	☐
2. Carbon reduction	☐	☐	☐	☐	☐

	1	2	3	4	5
3. Electricity	☐	☐	☐	☐	☐
4. Transportation	☐	☐	☐	☐	☐
5. Access to land	☐	☐	☐	☐	☐
6. Tax rates	☐	☐	☐	☐	☐
7. Tax administration	☐	☐	☐	☐	☐
8. Customs and trade regulations	☐	☐	☐	☐	☐
9. Labour regulations	☐	☐	☐	☐	☐
10. Skills and education of employees	☐	☐	☐	☐	☐
11. Business and licensing permits	☐	☐	☐	☐	☐
12. Access to finance	☐	☐	☐	☐	☐
13. Interest rates	☐	☐	☐	☐	☐
14. Economic and regulatory policy	☐	☐	☐	☐	☐
15. Macroeconomic policy(inflation, exchange rates)	☐	☐	☐	☐	☐
16. Corruption	☐	☐	☐	☐	☐
17. Crime, theft and disorder	☐	☐	☐	☐	☐
18. Anti-competitive practices	☐	☐	☐	☐	☐
19. Corporate regulations	☐	☐	☐	☐	☐

5. What other comments or recommendations do you have with regards to small business members' regulatory burdens and remedies?

8. SECTION H: ACKNOWLEDGEMENT

Thank you very much for your time.

1. Would you like a copy of the final report?

☐ Yes - Please provide your email address________________________________

☐ No

Appendix 2: Questionnaire for small business corporations

1. SECTION A: INTERVIEW DETAILS

1. Case number

2. Interviewer name

3. Interview date

4. Interview time

5. Respondent

6. Business trading name

7. Company name (if different from business trading name)

8. Address and contact telephone number

9. Industry your organisation represents

- 1 Agriculture, Forestry and Fishing
- 2 Mining
- 3 Manufacturing
- 4 Electricity, Gas, Water and Waste Services
- 5 Construction
- 6 Wholesale Trade
- 7 Retail Trade
- 8 Accommodation and Food Services
- 9 Transport, Postal and Warehousing
- 10 Information Media and Telecommunications
- 11 Financial and Insurance Services
- 12 Rental, Hiring and Real Estate Services
- 13 Professional, Scientific and Technical Services
- 14 Administrative and Support Services
- 15 Public Administration and Safety
- 16 Education and Training
- 17 Health Care and Social Assistance
- 18 Arts and Recreation Services
- 19 Other Services

10. State your organisation represents

- ☐ 1 Vic
- ☐ 2 NT
- ☐ 3 SA
- ☐ 4 Qld
- ☐ 5 NSW
- ☐ 6 ACT
- ☐ 7 WA
- ☐ 8 Tas
- ☐ 9 National

11. ABN

12. In what year was the business incorporated?

- ☐ 1 Business is not incorporated
- ☐ 2 Year ________________________

13. Does the business have a web site?

- ☐ 1 Yes, www.________________________________
- ☐ 2 No - but had a web site in the past
- ☐ 3 No - but intend to develop a web site
- ☐ 4 No - (Other: ……………………………….)

2. SECTION B: RESPONDENT DETAILS

1. What is your position?

- ☐ 1 CEO, Manager Director
- ☐ 2 General Manager,
- ☐ 3 CFO, Finance Director/Manager
- ☐ 4 Other ------------------

2. Since when have you held that position?

3. Gender

- ☐ 1 Male
- ☐ 2 Female

4. What is the highest level of education you have completed?

- ☐ 1 Post-grad degree (incl Doctors, Masters)
- ☐ 2 Grad diploma, grad certificate
- ☐ 3 Bachelor degree
- ☐ 4 Advanced diploma, Diploma
- ☐ 5 Certificate
- ☐ 6 Secondary
- ☐ 7 Primary
- ☐ 8 Other: ……………………….

5. Are you a member of the company's board?

☐ 1 Yes ☐ 2 No (Go to question 8)

6. Since when have you been a member of the board?

____

7. How many directorships do your board members currently hold? (incl public & private companies, Not-For-Profit, government bodies, etc)

	1	2	3	4	5	more than 5
Director1	☐	☐	☐	☐	☐	☐
Director2	☐	☐	☐	☐	☐	☐
Director3	☐	☐	☐	☐	☐	☐
Director4	☐	☐	☐	☐	☐	☐
Director5	☐	☐	☐	☐	☐	☐
Director6	☐	☐	☐	☐	☐	☐
Director7	☐	☐	☐	☐	☐	☐
Director8	☐	☐	☐	☐	☐	☐

8. Are you, or is your organisation, a member of any industry or professional associations?

☐ 1 Yes ☐ 2 No (Go to question 10)

9. Which association/s is that? (Multiple Responses)

1 ________________

2 ________________

3 ________________

4 ________________

5 ________________

10. Have you ever held a voluntary or remunerated position on an industry association or peak body?

☐ 1 Yes ☐ 2 No (Go to question 12)

11. Which industry association(s) or peak body(ies) was that? (Multiple Responses)

1
2
3
4
5

12. What is your age category?

- ☐ 1. under 25
- ☐ 2. 26-35
- ☐ 3. 36-45
- ☐ 4. 46-55
- ☐ 5. 56-66
- ☐ 6. 67+

3. SECTION C: BUSINESS DETAILS

1. Is your company a ___?

- ☐ 1 Public company (Go to question 2)
- ☐ 2 Private company (Go to question 3)
- ☐ 3 Sole proprietor (Go to question 3)
- ☐ 4 Partnership (Go to question 3)
- ☐ 5 (Other:………………) (Go to question 3)

2. Is the company a listed company? (i.e. trades shares on the stock exchange)

- ☐ 1 Yes
- ☐ 2 No

3. How many sites does the business have in Australia?

4. Number of the following positions the business have (incl any overseas' based employees)

full-time, paid, and non-manager employees

part-time, paid, employees

managers

5. How many overseas sites does the business have?

6. What is the development stage of your business on the business cycle?

- ☐ 1. establishment
- ☐ 3. expansion
- ☐ 5. decline

☐ 2. growth ☐ 4. maturity ☐ 6. unknown

7. Does the business operate in or provide services in countries other than Australia?

☐ 1 Yes. How many? ☐ 2 No

____

8. During the financial year 2008/09, please indicate the following financial indicators of your business

	1. Less than $5 million	2. $5 million to $10 million	3. $10 million to $12.5 million	4. $12.5 million to $15 million	5. $15 million to $20 million	6. $20 million to $25 million	7. $25 million or more	8. unknown
total assets	☐	☐	☐	☐	☐	☐	☐	☐
annual turnover	☐	☐	☐	☐	☐	☐	☐	☐
total sales	☐	☐	☐	☐	☐	☐	☐	☐
total equity	☐	☐	☐	☐	☐	☐	☐	☐
total debt	☐	☐	☐	☐	☐	☐	☐	☐
debts payable within one year	☐	☐	☐	☐	☐	☐	☐	☐
debts payable within one year	☐	☐	☐	☐	☐	☐	☐	☐
cash flow	☐	☐	☐	☐	☐	☐	☐	☐

9. In the 2008/09 financial year, what is the growth rate of the following financial indicators

	less than 5%	5% - 9%	10% - 14%	15%- 19%	20% - 24%	25% - 30%	30% +	unknown
1. equity	☐	☐	☐	☐	☐	☐	☐	☐
2. net profit	☐	☐	☐	☐	☐	☐	☐	☐
3. sales	☐	☐	☐	☐	☐	☐	☐	☐
4. total debt	☐	☐	☐	☐	☐	☐	☐	☐

	less than 5%	5% - 9%	10% - 14%	15%-19%	20% - 24%	25% - 30%	30% +	unknown
5. debt payable in less than 1 year								
6. debt payable in more than 1 year								
7. annual turnover								

10. What percentage of your domestic sales are to:

	0	less than 5%	5% - 9%	10% - 14%	15% - 19%	20% - 24%	25% - 30%	30% +	unknown
1. government or government agencies (excluding state-owned enterprises)									
2. not for profit organisations									
3. state-owned or controlled enterprises									
4. multinationals located in Australia									
5. parent company or affiliated subsidiaries									
6. large domestic firms (more than 50 employees)									
7. small and medium size businesses									
8. overseas companies									

11. Rate the importance of the following stakeholders for your business decision making (1 = not important at all; 5 = very important)

	1	2	3	4	5
1. customers	1	2	3	4	5
2. suppliers	1	2	3	4	5
3. employees	1	2	3	4	5
4. financial investors	1	2	3	4	5

	1	2	3	4	5
5. philanthropy (incl. volunteering)	1	2	3	4	5
6. environment	1	2	3	4	5

12. What is the percentage of total expenses are allocated to research and development (R & D)?

- ☐ 1. less than 5%
- ☐ 2. 5% - 9%
- ☐ 3. 10% - 14%
- ☐ 4. 15%- 19%
- ☐ 5. 20% - 24%
- ☐ 6. 25% - 30%
- ☐ 7. 30% +
- ☐ 8. unknown

13. Does your corporation have inventory management?

- ☐ 1. Yes
- ☐ 2. No (Go to question 14)

14. If so, currently how many days of inventory does your corporation have?

15. How many key products, patents and services does your company have in total?

16. How many days (equivalent) would you estimate your staff have spent last financial year on meeting compliance costs? (e.g. filling forms, reading and understanding regulatory requirements, consultation with regulators/accountants)

- ☐ 1. less than 5
- ☐ 2. 6-10
- ☐ 3. 11-19
- ☐ 4. 20-29
- ☐ 5. 30 +
- ☐ 6. unknown

17. How much would your firm have spent last year on meeting compliance costs? (Tax, Super., environment, HR/OH&S, BAS, GST, and other documentation & reporting burdens)

- ☐ 1. less than $1,000
- ☐ 2. $1,001- $5,000
- ☐ 3. $5,001 - $10,000
- ☐ 4. $10,001 - $ 20,000
- ☐ 5. $20,001 +
- ☐ 6. unknown

18. How many working days does your company provide to staff training and professional development during the financial year 2008/09?

- ☐ 1. less than 5 days
- ☐ 2. 6 - 10 days
- ☐ 3. 11 - 20 days
- ☐ 4. 21 - 30 days
- ☐ 5. more than 30 days

19. Are any of these areas a particular cost burden to your business?

- ☐ 1. Access to financing (e.g., collateral
- ☐ 10. Customs and trade regulations

required or financing not available from banks)

- 2. Cost of financing (e.g., interest rates and charges)
- 3. Telecommunications
- 4. Electricity
- 5. Transportation
- 6. Access to land
- 7. Title or leasing of land
- 8. Tax rates
- 9. Tax administration
- 11. Business licensing and permits
- 12. Labour regulations
- 13. Skills and education of available workers
- 14. Uncertainty about regulatory policies
- 15. Functioning of the judiciary
- 16. Corruption
- 17. Anti-competitive practices of other competitors
- 18. Contract violations by customers and suppliers

20. Would you recommend any changes to regulations or compliance activities to reduce your costs?

21. How often does your business use the following Information and Communication Technology (ICT) tools to for major business activities?

	1. Never consider it	2. Sometimes	3. Often	4. Always	5. Outsource to others
1. fixed-line telephone					
2. fax					
3. mobile telephone					
4. email					
5. internet/web					
6. database					
7. e-business					

22. How often does your business use the following Information and Communication Technology (ICT) tools to respond to company registration, Health and Safety reporting and GST?

	1. Never consider it	2. Sometimes	3. Often	4. Always	5. Outsource to others
1. fixed-line telephone	☐	☐	☐	☐	☐
2. fax	☐	☐	☐	☐	☐
3. mobile telephone	☐	☐	☐	☐	☐
4. email	☐	☐	☐	☐	☐
5. internet	☐	☐	☐	☐	☐
6. database	☐	☐	☐	☐	☐
7. e-business	☐	☐	☐	☐	☐

23. What are you expecting from your accountant(s)?

☐ 1. Company Registration

☐ 2. Health and Safety related reporting

☐ 3. GST

☐ 4. Others ____________________

24. Would you recommend any changes to regulations that would promote your business growth?

☐ 1. Yes

☐ 2. No (Go to Section D)

25. What changes to regulations do you recommend?

4. SECTION D: CORPORATIONS LAW

The next set of questions is about your business' constitution

1. Does the business have its own constitution or does it use the model (Replaceable Rules) specified in the Corporations Act (the default arrangement)?

- 1. The business has its own constitution (Go to question 2)
- 2. The business uses the model in corporate Replaceable Rules (Go to question 3)
- 3. Others____________ (Go to question 4)
- 4. Unknown

2. What are the key differences between the business' constitution and the Replaceable Rules?

3. Are there any difficulties that you are aware of with the Replaceable Rules?

- 1. No
- 2. Yes, please describe ____________________________________

4. Rank the main sources of advice about corporate governance used by your business. (6= the most frequently used, 0 = don't know)

- 1. Industry/prof. association, peak body
- 2. Lawyer
- 3. Accountant
- 4. Govt/regulatory agency
- 5. Other: ....
- 6. No external sources used
- 7. Don't know

5. How difficult do you rate the following to the development of your business(1 = not difficult at all, 5 = very difficult)

	1	2	3	4	5	unknown

	1	2	3	4	5	unknown
new laws compliance	1	2	3	4	5	unknown
complexity of regulation	1	2	3	4	5	unknown
workplace crisis	1	2	3	4	5	unknown
change management	1	2	3	4	5	unknown
supplier chain management	1	2	3	4	5	unknown
human capital management	1	2	3	4	5	unknown
anti-takeover	1	2	3	4	5	unknown
IT and new technology-related costs	1	2	3	4	5	unknown

5. SECTION E: ABOUT THE BOARD

1. Does your business have a board of directors?

1. Yes
2. No (Go to question 21)

2. How many directors are on the board?

3. Is the CEO/Owner/Manager also the director on the board?

1. yes
2. no

4. What is the process for appointment of directors?

5. How many are independent directors? (ie not employees, substantial shareholders or suppliers to/ customers of the business)

6. How are independent directors identified and appointed to the board?

7. How many directors are female?

8. Would your board benefit from increased diversity in terms of gender or background?

- 1. Yes
- 2. No
- 3. Not sure

9. Is the board able to bring independent judgement to bear in decision-making?

- 1. Yes
- 2. No/not always

10. How does the board ensure its independence?

11. What are the major skills and other attributes of the board?
re areas of expertise, prior board experience, etc

12. Does the business have a process for board and director evaluation and professional development?

- 1. Yes - has both
- 2. Has an evaluation process (but not a prof development process)
- 3. Has a professional development process (but not an evaluation process)
- 4. No - has neither
- 5. Don't know

13. What are the challenges in achieving this?

14. Does the company separate the roles and responsibilities of the board and management? If so , how?

- 1. Yes ____
- 2. No

15. Is there a process to monitor and review the separation of the roles of the board and management?

- 1. Yes
- 2. No

16. Is this separation of powers useful in practice?

- 1. Yes
- 2. No

17. How many shareholders does the company have?

18. What percentage of shares is owned by the largest shareholder?

19. How many times does your board meet annually?

- 1. Not at all
- 2. Once
- 4. 5-12 times
- 5. More often

3. 2-4 times

20. How would you rate the difficulties caused by the following issues (1 = not difficult at all, 5 = most difficult)

	1	2	3	4	5
1. A directors' meeting can be called by any director giving notice individually to every other director.	1	2	3	4	5
2. The directors must elect a director present as chair and determine the period for which the director is the chair.	1	2	3	4	5
3. A resolution is passed by a majority of directors votes; the chair has a casting vote.	1	2	3	4	5
4. Where there are joint members, notice is given to the first named member in the register.	1	2	3	4	5
5. Unless a company has written advice to the contrary before a meeting, a vote cast by a proxy will be valid.	1	2	3	4	5
6. Voting may be by a show of hands unless a poll is demanded.	1	2	3	4	5

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21. Does your business disclose information relating to the following?

	Yes, to whom?	No	Don't know
1. the financial and operating results of the corporation			
2. major share ownership and voting rights			
3. materialising foreseeable risk factors			

22. How does your business disclose information relating to the financial and operating results of the corporation?

23. How does your business disclose information relating to major share ownership and voting rights?

24. How does your business disclose information relating to materialising foreseeable risk factors?

25. Is the CEO also:

	Yes	No
1. The chair of the board	☐ Is the CEO also: 1. The chair of the board Yes	☐ No
2. the Managing Director?	☐ 2. the Managing Director? Yes	☐ No
3. Major owner?	☐ 3. Major owner? Yes	☐ No

26. Does the company have a policy concerning trading in company securities by directors, officers and employees?

☐ 1. Yes
☐ 2. No
☐ 3. Don't know

27. Does the board have subcommittees?

☐ 1. Yes - (Go to Question 28)
☐ 2. No- (Go to Question 29)

28. What responsibilities does the board delegate to sub-committees?

29. The following questions are about the succession plans

	1. Yes	2. No	3. Don't know
Does the company have an established succession plan?			
Does the succession plan cover ownership?			
Does the succession plan cover board members?			
Does the succession plan cover the CEO?			
Does the succession plan cover senior management?			

30. The following questions are about the audit committee

	1. Yes	2. No	3. Don't know
Does the company have an audit committee?			
Does the audit committee consist of only non-executive directors?			
Are the majority of audit committee members, independent directors?			
Is the chairperson of the audit committee also the chair of the board?			
Does the audit committee have a formal policies and procedures or guideline?			

31. How many members does the audit committee have?

32. Does the company have

	Yes	No	Don't know
1. a risk management committee?			

	Yes	No	Don’t know
2. a remuneration committee?	☐	☐	☐
3. have a nomination committee?	☐	☐	☐

33. Does the company have a code of conduct ?

☐ 1. Yes
☐ 2. No
☐ 3. Don’t know

34. Is your company independently audited?

☐ 1. Yes
☐ 2. No
☐ 3. Don’t know

35. Who designs the director's remuneration plan?

6. SECTION F INSTITUTIONAL FACTORS

This section is focused on the firm-level institutional factors pertinent to the business development, covering asset specificity, uncertainty and frequency.

1. What are the following ratios?

the proportion of products ordered from the top 5 suppliers

the proportion of products sold to the top 5 clients

2. To what degree do you agree with the following statements (1 = strongly disagree, 5 = strongly agree)

	1	2	3	4	5
1. my company is keen to have employees, particularly salesman involved in decision making process	☐	☐	☐	☐	☐
2. my company is requiring employees to know all the details of our products	☐	☐	☐	☐	☐
3. employees are all allowed to access company secrets	☐	☐	☐	☐	☐
4. my employees are all very experienced in meeting clients' needs	☐	☐	☐	☐	☐
5. our customers are very loyal business partners	☐	☐	☐	☐	☐
6. the percentage of market our product penetrated will be very stable in the future	☐	☐	☐	☐	☐
7. it is easy for us to monitor the market trends in the future	☐	☐	☐	☐	☐

	1	2	3	4	5
8. the volume of products demanded in our industry is stable in the future					
9. we are able to forecast the sales accurately					
10. the market trends are predictable					
11. we are able to predict the supply changes due to technological changes in the factor market for raw materials					

3. Please evaluate the following issues based on your experience and perceptions

	yes	no
1. is it adequate to evaluate the suppliers' strategies based on component prices		
2. are the suppliers following the approved production and quality control procedures		
3. are the major 5 suppliers expecting a long-lasting relationship		
4. are the major 5 clients expecting a long-lasting relationship		
5. whether the suppliers are major 5 suppliers are expecting a block purchase in the short term		

4. How often do your trade with the following stakeholders in total(times/year)

major 5 suppliers

major 5 clients

7. SECTION G: ASIC COMPANY REGISTRATION

1. How would you rate the difficulties caused by the following issues (1 = not difficult at all, 5 = most difficult)

	1	2	3	4	5
1. The name of the company and its ACN or ABN must be shown at all its business premises that are open to the public.	1	2	3	4	5
2. The company secretary is responsible for ensuring that the company: notifies ASIC about changes to the identities, names and addresses of the company's directors and company secretaries; notifies ASIC about changes to the register of members; notifies ASIC about changes to any ultimate holding company.	1	2	3	4	5

	1	2	3	4	5
3. A company must have a registered office in Australia and must inform ASIC of the location of the office. A post box cannot be a registered office of a company.	1	2	3	4	5
4. A director may resign by giving notice of the resignation to the company. If the director does not notify ASIC of the resignation, the company must do so.	1	2	3	4	5

2. What are the main difficulties?

3. What could be done to overcome or minimise this problem?

8. SECTION H: RECORDS

1. How would you rate the difficulties caused by the following issues (1 = not difficult at all, 5 = most difficult)

	1	2	3	4	5
1. A company must keep in its register of shareholders information including the names and addresses of shareholders and details of shares held by individual shareholders.	1	2	3	4	5
2. A company must keep a register of charges if the company gives a bank, trade creditor or anybody else a charge over company assets.	1	2	3	4	5
3. Each year the company must notify ASIC of any corrections on a printed form, or if an agreement is in place, electronically.	1	2	3	4	5
4. If ASIC or a shareholder with at least 5% of the votes in the company directs, a small proprietary company must prepare an annual	1	2	3	4	5

	1	2	3	4	5
financial report (profit and loss, balance sheet, statement of cash flows) and a directors' report (about the company's operations, dividends paid/recommended, options issued, etc).					
5. Proprietary companies must keep sufficient financial records to record and explain their transactions and financial position and to allow true and fair financial statements to be prepared and audited.	1	2	3	4	5

2. What are the main difficulties?

3. What could be done to overcome or minimise this problem?

9. SECTION I: DIRECTORS' DUTIES

1. How would you rate the difficulties caused by the following issues (1 = not difficult at all, 5 = most difficult)

	1	2	3	4	5
1. to act in good faith;	1	2	3	4	5
2. to act in the best interests of the company;	1	2	3	4	5
3. to avoid conflicts between the interests of the company and of the director;	1	2	3	4	5
4. to act honestly;	1	2	3	4	5

	1	2	3	4	5
5. to exercise care and diligence;	1	2	3	4	5
6. to prevent the company trading while it is unable to pay its debts;	1	2	3	4	5

2. To what extent would you evaluate the difficulties to your business caused by each of the following factors(1 = most difficult, 5 = least difficult):

	1	2	3	4	5
1. Directors are liable to compensate the company for breaches of directors' duties.	1	2	3	4	5
2. Directors are liable for debts incurred what a company is unable to pay them when they fall due.	1	2	3	4	5
3. If a company experiences financial problems, the directors may appoint an administrator to take over the operations of the company to see if the company's creditors and the company can work out a solution to the company's problems. If the company's creditors and the company cannot agree, the company may be wound up.	1	2	3	4	5
4. Dividends are payments to shareholders out of the company's after tax profits. The directors decide whether the company should pay a dividend.	1	2	3	4	5
5. Directors have discretion to refuse to register a transfer of shares.	1	2	3	4	5
6. A company may execute a document by having it signed by two directors of the company; or a director and the company secretary; or for a company with a sole director who is also the sole secretary – that director.	1	2	3	4	5
7. If the company is being wound up – to report to and to help the liquidator.	1	2	3	4	5
8. A liquidator is appointed to administer the winding up of a company.	1	2	3	4	5

3. Looking at the major difficulties identified above, what could be done to minimise the difficulties?

4. What are the other difficulties have you perceived?

5. What could be done to overcome or minimise this problem?

10. SECTION J:LEGAL DIFFICULTIES FOR COMPANIES AND DIRECTORS

1. How would you rate the difficulties caused by the following issues (1 = not difficult at all, 5 = most difficult)

	1	2	3	4	5
1. A company's money and other assets belong to the company and must be used for the company's purposes.	1	2	3	4	5
2. Shareholders are not liable for company debts, only to pay for unpaid amounts on their shares.	1	2	3	4	5
3. A proprietary company must have at least one and no more than 50 shareholders (not counting employee shareholders).	1	2	3	4	5

	1	2	3	4	5
4. Before issuing new shares, a company must first offer them to the existing shareholders in the proportions that the shareholders already hold.	1	2	3	4	5
5. If there is only one shareholder and that person dies, their representative is able to ensure that the company continues to operate.	1	2	3	4	5

11. SECTION K: MAJOR ISSUES WITH REGULATION

Please tell us if any of the following issues are a problem for the operation and growth of your business. For each item, I'll ask you to indicate the extent to which you think the issue poses difficulties, of any type, for the small corporations such as yours.

1. In summary, what would you nominate as being the three most problematic corporate governance issues facing small corporations in Australia today? for details

2. And, what three changes to corporate regulation would you recommend to facilitate the success of small corporations?

3. In your opinion, what have been the most positive changes or trends in the corporate governance area in recent years? (regulatory change, changes in business practices, etc)

4. How would you rate the difficulties caused by the following issues (1 = not difficult at all, 5 = most difficult)

	1	2	3	4	5
1. Telecommunications	1	2	3	4	5
2. Carbon reduction	1	2	3	4	5
3. Electricity	1	2	3	4	5
4. Transportation	1	2	3	4	5
5. Access to land	1	2	3	4	5
6. Tax rates	1	2	3	4	5
7. Tax administration	1	2	3	4	5
8. Customs and trade regulations	1	2	3	4	5
9. Labour regulations	1	2	3	4	5
10. Skills and education of employees	1	2	3	4	5
11. Business and licensing permits	1	2	3	4	5
12. Access to finance	1	2	3	4	5
13. Interest rates	1	2	3	4	5
14. Economic and regulatory policy	1	2	3	4	5
15. Macroeconomic policy(inflation, exchange rates)	1	2	3	4	5

	1	2	3	4	5
16. Corruption	☐ 1	☐ 2	☐ 3	☐ 4	☐ 5
17. Crime, theft and disorder	☐ 1	☐ 2	☐ 3	☐ 4	☐ 5
18. Anti-competitive practices	☐ 1	☐ 2	☐ 3	☐ 4	☐ 5
19. Corporate regulations	☐ 1	☐ 2	☐ 3	☐ 4	☐ 5

5. What other comments or recommendations do you have with regards to small business members' regulatory burdens and remedies?

12. SECTION L: ACKNOWLEDGEMENT

Thank you very much for your time.

1. Would you like a copy of the final report?

☐ Yes - Please provide your email address________________________________

☐ No

MEMO

TO	Prof Anona Armstrong Centre for International Corporate Governance Research City Flinders Campus	DATE	19/03/2010
FROM	Prof Michael Muetzelfeldt Chair Faculty of Business & Law Human Research Ethics Committee		
SUBJECT	Ethics Application – HRETH 09/252		

Dear Prof Armstrong,

Thank you for resubmitting your application for ethical approval of the project entitled:

HRETH 09/252 Developing a responsive regulatory system for Australia's small business corporations.

The Chair of the Business & Law Human Research Ethics Committee resolved to **approve** the application, subject to submission of Year One, Year Two and CEO survey forms for approval as they are developed. All supporting documentation submitted to date has been accepted and deemed to meet the requirements of the National Health and Medical Research Council (NHMRC) 'National Statement on Ethical Conduct in Human Research (2007)'. Approval is granted from 19 March 2010 to 31 December 2012.

Continued approval of this research project by the Victoria University Human Research Ethics Committee (VUHREC) is conditional upon the provision of a report within 12 months of the above approval date (by **19 March 2011**) or upon the completion of the project (if earlier). A report proforma may be downloaded from the VUHREC web site at: http://research.vu.edu.au/hrec.php

Please note that the Human Research Ethics Committee must be informed of the following: any changes to the approved research protocol, project timelines, any serious events or adverse and/or unforeseen events that may affect continued ethical acceptability of the project. In these unlikely events, researchers must immediately cease all data collection until the Committee has approved the changes. Researchers are also reminded of the need to notify the approving HREC of changes to personnel in research projects via a request for a minor amendment.

If you have any queries, please do not hesitate to contact me at Michael.Muetzelfeldt@vu.edu.au.

On behalf of the Committee, I wish you all the best for the conduct of the project.

Prof. Michael Muetzelfeldt
Chair
Faculty of Business & Law Human Research Ethics Committee

Appendix 4: COSBOA Participants

Association of Accounting Technicians

Australian Book Sellers Association

Australian Equipment Lessors Association

Australian Newsagents' Federation Ltd

Australian Toy Association

Business & Professional Women Australia

Business Enterprise Centres

Cabinet Makers Association

Furnisher's Society of VIC

Furnishing Industry Association of Australia (Vic/Tas) Inc

National Independent Retailers Association Inc

National Institute of Australia

Pharmacy Guild of Australia

Photo Marketing Association International

Real Estate Institute of Australia

Tasmanian Small Business Council

The Confectionary & Mixed Business Association

Association of Consulting Engineers of Australia

Independent Retailers Organisation of WA