Paper presented at the Rencontres de St-Gall conference, 3-5 September 2012, St.Gallen, Switzerland.

The Changing Online Marketplace: Some Long-Term Implications For Small Business, Advisers And Regulators

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Abstract

Online trading and commerce has become central to many businesses today, yet it is still an evolving phenomenon. What shape is the electronic marketplace of the future likely to take, and what impact will this have on the small business sector, those who advise them, and the regulators, governments and other policymakers whose job it is to manage the effective operation of those markets on behalf of the community?

Whilst it is difficult to accurately predict how online trading will develop in future, it is possible to take note of a number of existing issues which have, to date, been largely overlooked by many commentators, and which seem likely to have a significant impact on the online marketplace in future.

Five potential "big issues" are identified: the need to ensure that online trading environments remain genuinely competitive; the rising incidence of scams perpetrated online that target small businesses as their victims; growing challenges to the established business models of many product franchise operations; the re-emergence of many self-employed persons trading online in the informal economy; and the difficulty of delivering effective business advice and regulatory compliance information to micro- and small-sized business operators.

Debating Points For Rencontres Participants

1. Will the term 'small business' remain relevant in the online world, when a very small enterprise can employ only a handful of people, yet process millions of sales globally every year? Or are new definitional metrics required, such as the breadth of a firm's cyber-reach?
2. Are online scams a real problem for small businesses?
3. Is trading on the internet a genuine form of self-employment (solo business)?
4. Do governments need to regulate the online marketplace more to (ironically) ensure it remains open to free competition?

[1] The author would like to thank staff of the Commission, particularly Mr Owen Gill, for their comments; the final paper, however, is the author's alone and does not necessarily represent a formal view of the ACCC.

Introduction

Online trading and commerce has become central to many businesses today, yet it is still an evolving phenomenon. What shape is the electronic marketplace of the future likely to take, and what impact will this have on the small business sector, those who advise them, and the regulators, governments and other policymakers whose job it is to manage the effective operation of those marketplaces on behalf of the community?

Markets are central to the notion of successful small business and entrepreneurship. They are the forum through which businesses interact with potential customers – the medium by which enterprises seek to advertise themselves, convince would-be purchasers to invest in their products or services, and the mechanism through which the exchange of money for such goods takes place.

Markets are not, however, a static phenomenon. They never have been: whilst the word "market" instead originally connoted a physical meeting place (such as a defined gathering of buyers and sellers in the towns and cities of imperial Rome and medieval Europe), its meaning has over time changed as the forums through which people bought and sold items has also evolved.

The most recent change to the notion of the market has been that bought on by the development of the internet and other forms of virtual communication. The internet has changed many aspects of both personal and commercial behaviour. It has sped up the process of communication, vastly expanded access to information, and widened the reach of the marketplace so that even the simplest of small businesses can now trade anywhere, anytime, to anyone.

Five Issues To Consider

One thing is certain about the online trading age: its evolution is not yet complete. New products, applications and business methods constantly appear, and just as it seems the model of doing business online has settled down into an established orthodoxy, new challenges and opportunities emerge.

It is not always possible to predict how the future will unfold – but it is possible to take note of a number of existing issues which have, to date, been largely overlooked by many commentators, and which seem likely to have a significant impact on the online marketplace in future. Here are five potential "big issues" that are worthy of more attention in future.

i. Fair Trading In An Online Context

Online trading is now a well-established phenomenon, and indeed an essential business strategy for many firms. Not all businesses trade online (there are, for example, many self-employed people and small-scale retailers who continue to focus on selling their goods and services through person-to-person dealing) but the majority of firms do deal electronically, in one form or another.

There is no doubt that such commerce provides enormous opportunities for micro-, small- and medium-sized businesses. It allows new firms to be born and begin trading with a minimal amount of effort and cost (the expense of commencing online can be much less than that required to fit out and stock a conventional bricks-and-mortar premises); allows such enterprises to reach much wider, extensive customer markets than was ever the case before (indeed, many new small firms "go global" and trade internationally from day one); and helps them to develop new niches.

But online trading also gives rise to some concerns about competition and consumer rights.

Online markets can also produce decidedly anti-competitive outcomes, and create situations which favour large, well-established businesses. First mover effects in the internet era are a case in point: whilst the web initially allowed what were then new, innovative firms with unusual names like Amazon, Google and Microsoft to displace old business models, they in turn then became the established dominant players in these newly-created markets. Their high public visibility, ubiquitous reach and economies of scale have subsequently allowed them to retain a dominant market prescence. This, in turn, makes it harder for new firms to follow in their footstep and establish a market presence.

A case in point was the Microsoft web browser case in 2001, where US antitrust (competition) regulators took action against the computing giant for installing internet explorer as the default web browser in its machines. One of the regulator's stated concerns was that such an action effectively cut out rival browsers from being able to be successfully sold in the market.

Other competition regulators such as the Australian Competition and Consumer Commission (ACCC) have also begun dealing with situations where established firms have attempted to deter or limit competition through exclusive dealing, price fixing, misuse of market power and resale price maintenance, or where consumers and small businesses are likely to suffer. In 2007, for example, the ACCC instituted legal proceedings against Google, alleging misleading and deceptive conduct in relation to sponsored links that had appeared on the Google website. In April 2012, the Full Federal Court of Australia found that Google had engaged in misleading or deceptive conduct when it published four advertisements on the search results pages of its Google Australia website[2] (ACCC 2012).

Protection of consumer interests can also be made difficult in an online trading environment. When products are sold online from a seller in another country, to what extent does a consumer have any rights? And who will enforce them?

Most countries have a set of laws guaranteeing the rights of consumers, as well as laws mandating minimum standards of product safety, to ensure that defective goods are not sold to an unsuspecting public. In the European Union, for example, this is spelt out in laws such as the *Directive on Certain Aspects of the Sale of Consumer Goods and Associated Guarantees* (European Parliament 1999). But when a firm

[2] The decision is currently the subject of an appeal to the High Court of Australia.

trades across borders, which set of consumer protection laws apply? And who enforces product safety?

With all of these questions in mind, there is no doubt that that the online retail marketplace will be an important area of future scrutiny.

A more conceptual question issue for the SME sector is this: will the term ‘small business’ remain relevant in the online world? A small business once meant a firm that had a relatively small number of clients, and, perhaps, operated in a local market. Or it meant a firm with a small number of employees and turnover. But is a retail website that perhaps employs only a handful of people, yet conducts millions of sales globally every year, really ‘small’ in its scope and market presence? In the near future businesses might be defined by new measurement analytics, such as the breadth of their cyber-reach.

ii. Scams

Many business operators will be familiar with the notion of a “scam” – a type of fraudulent illegal activity that tries to lure victims with a seemingly-innocent offer. In reality, it is a deceptive and misleading action executed by an external perpetrator upon a small enterprise, where the owner-manager victim is approached and invited to participate in an activity which unwittingly leads to the loss of financial, organisational or owner resources. A common example of scamming is so-called “phishing”, which refers to the practice of emailing firms or business owners seeking personal financial information, such as bank account details. The emails are often designed to look like a message from a well-known large corporation (such as a bank) or a government agency (such as a tax regulator). Another common example of online scamming is the fake government website, designed to look like an official URL, into which victims put their personal or financial details, only to have this data then used by a fraudster.

Notably, many online scams are actually old frauds perpetrated in a new way. False invoicing, for example, was once perpetrated by mail. Now it is attempted over the internet or via email. Credit card skimming was once conducted by copying a consumer’s credit card in a restaurant or shop; now skimming is attempted online. In Australia, consumer advocates often wearily remark: “Old problem; new technology”.

Whilst there has been only limited research into scamming of small firms, the existing evidence suggests that SMEs are especially vulnerable to this type of criminal activity. They are also less likely to report such events, are more likely to be the victim of repeat attacks, and are more susceptible to online approaches than the general public (Geneste, Weber and Schaper 2012; Weber et al 2011; ABS 2008).

The consequences of scamming can be significant to many SMEs. In many cases, the victim finds that their own bank account has been raided. For many small firms who trade at the margins of financial viability, or who rely heavily on internally-generated cash flow to fund their operating activities, this may be enough to push them into bankruptcy. Even if it does not, there are other negative flow-on effects. The firm may find that their client’s details have also been compromised, resulting in long-term losses of customer confidence and a decline in sales. Insurance premiums may be increased, or the process of reporting the crime and dealing with law enforcement agencies may take up much of the owner-manager's time and energy.

At the same time, online scams are some of the hardest phenomena for enforcement agencies to prosecute. The real identity of an online scammer is often difficult, if not impossible, to detect; they rarely need to disclose any information about themselves or their location; money payments from victims are usually made by international wire transfer, which is very difficult to recover; and they are often based in national jurisdictions which do not have strong legal systems or extradition treaties.

Online fraud already accounts for a large proportion of total scamming activity – in Australia in 2011, for example, it represented almost half of all scam attempts (ACCC 2012a). New evidence suggests that scammers may well deliberately target small firms with a high level of internet presence (Geneste et al 2012). As the number of SMEs trading in the online environment continues to grow, it can be expected that the incidence of scamming will also increase.

iii. Franchising

Franchising is now a major form of business activity, and the creator of many small businesses around the world. In the USA, for example, the franchising sector had almost 830,000 franchisees in 2007; in Australia in 2010 it contained 70,000 firms; and in India there were 50,000 franchisee firms in 2010 (International Franchise Association 2008; Frazer, Weaven & Bodey 2010; World Franchise Council 2010). In the majority of almost all cases, these franchisees are small-scale enterprises.

In a traditional franchising arrangement, the originator of a business product or operating system (a franchisor**)** licenses or contracts with another party (a franchisee**)** to sell their goods and/or to use their business operations system, usually in a clearly defined manner that ensures consistency of brand promotion, product/service delivery, and standardization of operating procedures.

Fundamental to the operations of most franchise systems has been the notion of territoriality. The franchisee's right to sell a product or service has been largely defined on a geographic basis, with franchisees being given exclusive authority to sell in their designated location.

However, online trading changes this dynamic, and threatens to rewrite or damage the conventional logic of many franchise arrangements. It can do this in two ways: by rendering territorial rights as irrelevant, and by allowing franchisors to compete directly with their own franchisees.

The value of a franchise lease or right is the guarantee of exclusivity for a particular geographic region. Such exclusivity gives franchisees an effective monopoly in their area, which in turn is the bedrock upon which they base their estimates of income, expenses and ultimate profitability and financial return. However, when goods are traded online, then such exclusivity can vanish. Customers in a region can easily move to purchase from another franchisee in the same system; they are no longer bound to geographic borders.

More importantly, it also allows franchisors to compete directly with even their own franchisees. Customers can buy online directly from the parent company, and there is often a temptation on the part of the franchisor to increase their own profits by doing so.

Both of these issues are likely to become particularly acute in the traded goods sector. Product franchising, after all, originated because early manufacturers of industrial products such as the Singer sewing machine realised that it would be easier and more logical to focus simply on manufacturing their goods, and licensing out the rights to sell them, then to establish their own network of shops and stores. But today, when product sales can be processed online globally at the one website, and dispatched from a store anywhere in the world, the logic of creating and supporting a network of franchisees may well be called into question.

Interesting, this is unlikely to be such a problem in the services sector (where personal skills, face-to-face contact and local knowledge remain highly important), or in some heavily-franchised sectors such as fast food, where physical storefronts are a critical determinant in selling.

iv. The Re-Emergence of The Informal Economy

Online trading is creating a new informal economy yet it is one which governments, regulators and commentators have barely begun to notice.

The emergence of modern industrial (and then post-industrial) economies in modern liberal democracies was accompanied by the large-scale migration of individuals and businesses out of the informal economy and into the formal regulated sector.

Informal economies – that is, economic activity which is not regulated, enforced or taxed by a government - have traditionally been strongest in places where the writ of the state is low, its capacity to enforce laws is weak, and where high levels of corruption and maladministration drive people to stay outside the knowledge and reach of the public sector (Mehta 1985). Even today, the informal sector is strongest in developing countries such as India, where it accounts for an estimated half of the workforce, and in regions such as the Middle East (Sakthivel & Joddar 2006).

In contrast, in most OCED nations the majority of economic activity occurs within a visibly regulated and transparent legal framework. There are different types of legal structures a person may choose to operate a venture under (such as a sole proprietor, partnership or company); there are formal requirements to register for taxation, employment, social security and other purposes; and there are well-developed mechanisms to detect trading ventures which fail to comply with these.

However, online trading is beginning to change these dynamics. As Giridharadas (2012) has noted, the rise of websites which allow individuals to buy and sell directly to each other is creating an emergent new informal sector: there are numerous websites which allow people to earn an income by letting others drive your car (Relay Rides); that permit people to bid for virtual work (such as oBay and Task Rabbit); or rent out spare rooms in a house (Airbnb), to name but a few. And, of course, there is now a long tradition of earning income by buying and selling on sites such as eBay.

By using a number of these, it is now possible for an individual to create a living income for themselves. Mostly, however, these ventures fall outside the conventional domain of "being in business." They are generally not regarded by most taxation, industrial relations or fair trading regulators as being commercial enterprises, and instead are often treated as personal hobby pursuits, and thus not worthy of regulation. In effect, they operate in a legal no man's land – just as ventures in the informal economy always have.

As Giridharadas (2012: 2) also notes, "…it is a lucrative new labor market, and also a way of going back to what the labor market was like before there were anti-discrimination laws, minimum wages…". It creates many new opportunities for those people who want to create their own portfolio career, who are comfortable with dynamic self-employment options, and who are prepared to be flexible in what services they sell to others.

But it also creates a minefield of interesting challenges for lawmakers and regulatory authorities. Should these ventures which are currently treated as hobbies or personal activities be treated as "proper" businesses – and if so, how does one keep track of them, much less regulate them? What happens if a customer racially discriminates in choosing a service from one of these websites? If a person who contracts for work through such a site is injured performing the work, who is to be held responsible? What about if two or more people using these sites to earn income agree to fix prices or divide up work between themselves – is that a breach of competition (antitrust) laws regarding market-sharing and cartel-like behaviour?

v. Legal Compliance and Advice To Business

Information sharing has always been an issue for governments. The public sector has often placed a high priority on getting information out to business, principally to ensure that firms are aware of, and compliant with, the many various laws and regulations that govern their activities.

Traditional models of business advice largely relied on a limited number of information distribution outlets. These included press releases and the placement of news items in popular media (such as mainstream newspapers and industry-specific trade journals or magazines); production of pamphlets, flyers and information booklets; meetings and briefings with industry associations (on the presumption that these bodies would in turn pass on the information to their members directly); and sometimes personal business advisory services. It was also largely a one-way flow of information: governments produced information and, apart from perhaps initial consultation with some select groups during the writing phase, then "pushed" it out for businesses to absorb. There was little capacity to alter the message once published. Such processes were, in the main, slow, expensive and difficult to change, and information was largely kept in the hands of those who produced it.

Online tools have changed this flow, and in many respects have done so for the better. Recent years have seen an evolution of business advice away from the written publication and towards the electronic. Most governments, for example, now operate a "business.gov" portal which allows owner-managers to access a wide variety of information[3], and individual agencies also typically upload large amounts of information onto their own websites. Information can be accessed at any time, at almost no cost for the entrepreneur, and without geographical limitations.

It is no doubt a far more efficient information dissemination process for governments, regulators and public agencies, but is it producing better outcomes for small business owners and entrepreneurs?

Online information dissemination brings with it a new set of problems and issues. For one, there is the danger of information overload. Websites allow government bodies to post up vast reams of information, much of which may be superfluous. There is no pressure to make messages short, sharp and to the point, yet as many small business researchers have demonstrated, small business owners are frequently time-short (Lane, Ding, Dandridge & Rudolph 1999) and want access to concise explanations of both "the rules of the game" and of their obligations.

Many websites and portals are still essentially didactic in their approach: they are designed for government to give information. There are usually only limited channels by which to give feedback. The increasing use of social media tools (such as Twitter) has begun to go some way to correct this, but a regulatory agency which structures its messaging to focus on telling businesses what to do, or presets the modes of response into tightly constrained options, will often be deaf to the messages that businesses need to tell them.

An electronic presence is a poor substitute for face-to-face counselling. For many entrepreneurs (especially those just about to start a business venture for the first time, as well as existing micro- and small-business operators), the ability to talk directly to another person is essential. It is the mechanism through which they can voice their fears, explore their concerns, and learn to articulate their goals and hopes. Person-to-person discussion, debate and decision-making is essential at this point, and research shows that it can often lead to much more sustainable business start-ups than would otherwise be the case (Chrisman, McMullan, Ring & Holt 2012).

Counsellors and advisers are also essential in helping small business owners work out exactly which laws do apply to them, and which are irrelevant. As past experience has shown, many of these firms do not have the financial resources to employ lawyers, accountants and other professional advisers to help them understand and comply with their legal responsibilities. It is for this reason that governments and NGOs around the world over the last thirty years have created and supported business facilitation and counselling services such as Local Enterprise Agencies (in the UK), the Gatsby Trust (Uganda), Enterprise Development Centres (Singapore) and Business Enterprise Centres (Australia).

These advisory services are expensive, and there is always a danger that governments will be tempted to economise and shift all information dissemination over to an

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[3] Some examples include www.business.gov.au (Australia), www.business.govt..nz (New Zealand), www.gov.hk/en/business (Hong Kong), www.business.gov.sg (Singapore) and www.business.gov.in (India).

electronic format. Whilst superficially tempting, it runs the risk of simply moving the burden of explaining and interpreting regulatory requirements away from governments and onto the shoulders of time-poor entrepreneurs. It may well lead to the unanticipated consequence of discouraging would-be start-ups who are unable to wade through or make sense of a sometimes-confusing, complex maze of laws and policies.

Conclusion

The online marketplace brings with it both risks and rewards, and like any new opportunity, throws up new questions which eventually have to be answered. While entrepreneurs and small business owners are often adept at identifying and taking advantage of new developments in the marketplace, markets evolve quicker than governments, laws and regulatory responses ever do. As the above discussion suggests, there are already a number of emergent issues in the online arena which need to be better understood. Research has a role to play in achieving this – in understanding the phenomena already occurring, in assessing how SMEs are responding to these challenges, and suggesting how governments and regulators can develop effective strategies to manage these. It is a challenge which we all need to rise up to.

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