

The Internet & Consumer Protection

A SUBMISSION TO THE REVIEW OF AUSTRALIA'S CONSUMER POLICY
FRAMEWORK PURSUANT TO THE *PRODUCTIVITY COMMISSION ACT*

A Joint Submission in response to the draft report by:



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1. Comment on Exposure Draft

We are supportive of the broad thrust of the Exposure Draft of the Review of Australia's Consumer Policy Framework. Within that context, we seek to make some additional comments with regard to consumer protection and safety.

2. Introduction

The Commission is correct in pointing out that the advent of the Internet has created a powerful vehicle for consumers to understand, research, compare and purchase goods.

The Internet has also reduced the barriers to entry for those who wish to sell to the Australian consumer – an excellent outcome for both consumers and those who hold the entrepreneurial spirit.

Unfortunately, the Internet has *also* acted to reduce the barriers to entry for significant numbers of operators who act either outside of, or with no reference to, the Australian regulatory framework – to the detriment of Australian consumers. These failures can be broadly categorised as follows:

- A. Failure to comply with key regulatory frameworks such as the *Trade Practices Act*, the various *Sale of Goods Acts*, the *Designs Act*, the *Patents Act*, the *Trade Mark Act* and the *Copyright Act*:
 - i. Illegal goods
 - ii. Goods not fit for the purpose for which they were sold
 - iii. Grey-market specific support issues
 - iv. Price Claims
- B. Failure to comply with industry-specific consumer safeguards
- C. Failure to comply with (or no need to comply) with tax legislation

This document seeks to outline some of the ways the current consumer protection and regulatory framework fails to protect Australian consumers online, along with the implications of these failures to Australian businesses, and potential solutions to these structural failures. Should these regulatory failures be addressed, they will better equip Australian businesses and consumers to do more business online sooner.

In particular, this submission argues that the changed nature of the online environment on consumer protection means that Government has a decreased ability to protect Australian consumers compared to traditional retail paths to market. However, these transactions are largely being facilitated by Online Marketplaces (such as eBay, Amazon, Trading Post Online, and a ballooning number of smaller operators) with significant market clout.

We believe that the relationship between these Online Marketplaces and the vendors is the key to ensuring ongoing consumer protection in Australia.

While the range of industries and sectors who have joined together to make this submission is diverse, we have found that these problems are repeated with increasing frequency across sectors, brands, industries and price-points. In short, we believe that the current regulatory framework for consumer protection is under significant threat, requiring urgent action to maintain the safety and standards all Australians consumers and businesses know and expect.

3. How Australian consumers are being hurt

Australia’s consumer protection and safety standards have developed over decades and are predicated from a detection and enforcement perspective on an environment of largely physical assets (retail premises located in Australia).

The Online environment, however, enables operators to sell directly to the Australian public with very small volumes – in a way that is difficult to detect or enforce current legislation upon.

3.1. Australian Safety Standards

Australian Citizens hold our safety standards in high regard – viewing them as an important protection. However, the online marketplace is enabling a range of transactions for products which fail to meet Australian Safety Standards.

3.1.1. Example – Electrical Safety Compliance

Both grey market and counterfeit electrical goods imported into Australia often fail to comply with Australian electrical standards. In particular not supplying 240 volt power adaptors or plugs with insulated pins, which is now compulsory except in the case of second hand goods.

Electrical compliance is another cost faced by authorised (and proper parallel) importers which is not factored into non-complying goods. If these goods are damaged as a result, this can also revert to a warranty-claim issue.

3.2. Australian Consumer Protection Framework

This section refers to the Australian “consumer protection framework” in the broadest possible sense, and includes the TPA and the State-based Sales of Goods Acts.

3.2.1. *Warranty Support*

There are regular and repeated instances of consumers who have purchased defective goods online who find they are not covered by a warranty, despite the requirement under Australian law to provide warranty and service support. We have been advised that there have been instances of eBay vendors explicitly instructing purchasers to take the faulty goods to the authorised Australian importer because they are covered under an ‘international warranty’.

Obviously this creates a number of problems for consumers (and for authorised wholesalers), including: the authorised importer factors a warranty/service component into their wholesale price, and do not support goods they do not import, so

- Purchasers of many “gray market” goods are effectively not covered by Australia’s consumer protection regime; &
- Sellers of authorised goods are unable to compete on a like-and-like basis with grey market importers which evade their legal obligations.

We understand that parallel importing is legal – our issue is that those who parallel import need to be held to the same standards as those who officially import and retail. This means ensuring that purchasers are not left with the shock of finding that not only is their parallel imported product faulty, but that they have no warranty.

4. How small & medium sized business is being hurt

4.1. *A Level Playing Field for Small Business*

The other side of the increasing problem of non-compliant goods (be they counterfeit, sub-standard or grey market) and non-compliant business practices, is that it provides significant economic advantage to those who do not comply and significant competitive disadvantage on those who are compliant.

4.1.1. *Inequitable Regulatory Burdens*

The regulatory burdens caused by the broader set of consumer protection framework (from the Trade Practices Act through to industry-specific safety standards) rely on the creation of a level playing field. That is to say, individual companies happily comply on the basis that each of their competitors in this market also faces the same costs.

The boom in small non-compliant vendors using the Internet as a sales channel, however, threatens the status quo. Unless actions are put in place to ensure that regulatory burdens are shared equally, there will be increasing pressure on compliant companies to “cut corners” in the downward race to compete on price with non-compliant vendors.

The ultimate loser, of course, in a downward-spiral of compliance is the Australian consumer.

4.1.1.1. Case Study – “C-Tick” Compliance

Certain goods sold in Australia must comply with the regulatory arrangements for electromagnetic compatibility, which is evidenced by a C-Tick logo and number.

We are advised that some online sellers parallel import goods that:

- Should be C-Tick tested but aren't; and/or
- Misuse a C-Tick label - selling goods with a C-Tick label that belongs to the official importer

C-Tick testing costs from \$1,500- \$3,000 per product and has extensive record keeping requirements (often in respect of relatively low-volume goods). Penalties for non-compliance include imprisonment. The authorised importer factors a component for C-Tick testing and compliance into their wholesale price, so sellers of authorised goods are unable to compete on a like-and-like basis with grey market goods that either avoid C-Tick testing or misuse the official importers C-Tick number.

Sometimes, goods are non-compliant or have to be modified for C-Tick compliance. The illegal importation of these goods through unauthorised channels also threatens both consumer safety and the integrity of Australia's spectrum/broadcasting arrangements.

4.1.2. Tax Compliance

Several elements of the Online Marketplace system facilitate non-compliance with Australia's tax laws:

- Use of non-traditional and offshore payment mechanisms (e.g. PayPal, eGold);
- Ability to “hide” large volumes of sales through the use of multiple accounts
- Greater ability to ship directly from third countries, even if masquerading as a local Australian “non-commercial” sale.

4.1.2.1. GST

Many goods sold online are sold GST free because they're purchased from an offshore seller or because the seller is in Australia, but masquerading as vending privately owned goods.

For example, there are numerous examples of sellers consistently importing ongoing quantities of “personal goods” (avoiding GST) and which are then resold again as “personal goods” without GST.

4.1.2.2. Case Study – GST on Imported Toys

The following is an excerpt from an article in “Toy & Hobby Retailer” of August 2004

A Victorian hobby storeowner has already verified this abnormality by testing the system. He placed two orders to a Singapore hobby retail store for a radio control monster truck. One order was purchased using a business credit card for delivery to his hobby business address. The second order was placed an hour later using a personal credit card and residential address.

The interesting part now begins to unfold. The personal shopper order arrived door to door delivered by Australian post four days later with no extra fees.

The business parcel took eight days, it was held by customs for payment of import duty, handling fees, GST of 10 per cent and incidentals. It arrived at the business address costing over \$200 more than the one delivered to the residential address.

This situation clearly presents legitimate Australian importers and distributors with a very unlevel playing field.

4.1.2.3. Income tax

Many non-compliant sellers are not declaring income tax, It is believed that this is being particularly facilitated in the Online Marketplace sector by sellers who operate a PayPal account, who can buy and sell from that account, without declaring any income in Australia

5. Key Consumer Protection & Safety Issues

While the Section 2 above described the consumer protection issues that Australians face, this section describes the mechanisms which are creating these problems.

5.1. Counterfeit Goods

By their nature, counterfeit goods are typically non-compliant to any Australian standards.

While counterfeit goods have always been a problem for brand owners in any market, the Internet has facilitated sale of these goods in volumes never before seen or anticipated. Because of the inability of consumers to check the goods prior to purchase, consumers who would never contemplate the deliberate purchase of a “fake” item are being tricked into purchasing goods which are often dangerous or sub-standard.

5.2. Grey Market Goods

As industries we understand and support the fact that parallel importing is legal and here to stay.

However, we are seeing a marked increase in parallel-imported goods being sold by small vendors with no intention or ability to provide warranty support. This problem is accentuated in items which have localisation or safety issues (electrical standards, safety standards etc).

While turning away the victims of these sales from warranty support does not cost our members anything, it does underscore a considerable fraud being perpetrated on members of the public.

5.3. Other Sub-Standard Goods

5.3.1.1. Case Study – Sub-Standard Instruments

The music products industry is going through huge change. Two things have combined to create this: the extensive low-cost manufacturing in China and the internet.

I've been in this industry for many years, and I believe that music products sold in Australia have never been cheaper in real terms, largely because of the benefits of cheap Chinese manufacturing. Many factories in China produce high quality goods at incredibly low prices.

But many don't.

And combined with the internet that has created a powerful downside. We've coined the phrase 'objects resembling instruments' for many of the goods we see. Trumpets where the valves are soldered closed, trombone slides that don't, and violins where the bridge won't stay upright and the tuning pegs won't hold the tension in the strings. Parents are buying these instruments online from China and India, and when they arrive and are unplayable the seller won't refund or replace the goods. The parents bring the instruments to our stores asking if we can repair them, but they're so poorly manufactured the only thing they're good for is hanging on the wall as a decoration. Parents are then faced with finding the money to buy another (genuine) instrument or their child has to forego music classes.

A musical instrument is a specialty item, many parents are uninformed about what to look for when they buy, many online sellers make enormous quality claims that their products don't live up to, and the result is a consumer that then has their trust taken advantage of and loses their money.

It's easy to say 'let the market sort this out', but how many parents will have to make this mistake before word goes out that buying online is not wise? And the damage will be caused to all online sellers - legitimate and cowboys alike.

- Rob Henneman, National Sales Manager, MusicLink Music Group

6. The Role of Online Marketplaces

The roll out of competitors to eBay is rapid and aggressive. Sites specifically targeting Australian consumers include:

- ComTrader
- Trading Post
- Oztion
- Gum Tree
- Ozbid
- Trade Me
- The Trove
- Craigs List
- Aussie Bids

These auction and sale sites are underfunded and often operated offshore or by sole traders. Unlike eBay, there is little or no recourse should transactions fail.

The experience of related trade associations overseas is that we expect the Online Marketplace segment to fragment even further, making consumer and brand protection even more difficult.

6.1.1.1. Case Study – Sporting Goods & Online Marketplaces

The Australian Sporting Goods Association has commissioned the Global Brand Protection (“GBP”), a discreet investigation consultancy specialising in IP and Trademark protection in an attempt to stem the flood of counterfeit sporting goods in online marketplaces. GBP Reports:

In relation to people, groups, criminals utilizing electronic providers to sell counterfeit merchandise there are a number of key points that always cause difficulty when tracking down the infringers:

- The anonymity of the seller. The seller is able to hide behind a veil of secrecy utilizing various codes and usernames supported by the on-line market place provider.
- Lawfully, the persons details are not for public consumption, even if that person is not engaged in the commission of a crime.
- GBP would argue they should be, the same way a person who is selling a motor vehicle has to be transparent and truthful before, during and after the sale.
- The OM provider in RISK terms does what is reasonable to deter these persons and have a mechanism for removing the seller, if and I stress if it is brought to their attention that the person is committing a crime.
- GBP have many examples where a person or user group has been identified for selling counterfeit goods and their username and site has been closed down, or have been the subject of a policing action, only to appear again a few days later with a variant of the original username.

GBP has purchased just on 5,000 units from electronic selling sites in the past 12 months. One particular purchase led to police raids, the first netted 20,000 units and the second 160,000 units.

There is no assistance provided to investigative organisations and certainly policing agencies do not have the time or the manpower to troll through the many electronic sites where counterfeit, stolen or black market goods regularly appear for sale.

6.2. *Online Market Responsiveness to Industry*

Recent attempts through MIPI and other industry bodies to engage Marketplaces in dialogue have been met in most cases by complete silence by online marketplaces. In many cases, it has not even been possible to contact the owners or operators of Online Marketplaces.

6.3. *Level Playing Field for Online Marketplaces*

The number and specialisation of online marketplaces is currently increasing.

We submit that it is critical to not only build a nationally coherent consumer policy framework, but to ensure that all Online Marketplaces – not just the more responsive and responsible ones – are forced to meet the same standards.

6.3.1. *The importance of eBay*

As the market leader, eBay is the most complained about site. However, we believe that this is a factor of their size and that in fact they are one of the more responsive participants to consumer protection issues (within the current limited regulatory framework).

The irony is that as eBay does remove non-compliant sellers from their site, those sellers move to other smaller and less savoury sites, most of which have no mechanisms whatsoever for consumers or brand owners to pursue violations by sellers.

We strongly contend that in order to make significant further investments in consumer safety viable for websites such as eBay, the same rules must apply to all online marketplaces.

7. Conclusion

We think that the initial draft *Review of Australia's Consumer Policy Framework* does an excellent job of outlining some of the key problems mentioned in more detail in this submission – particularly around access to remedies.

We would urge the commission to explore ways in which consumers and small businesses can be better protected from sub-standard online vendors.