

SUBMISSION to THE PRODUCTIVITY COMMISSION

Review of the Economic Structure and Performance of the Australian Retail Industry

This submission is tendered to expose the multiple factors behind the need to review the Retail Industry and related supply chain elements, also referencing the current GST-Free & Duty-Free allowance for personal goods imported to a declared value <\$1000. This submission addresses:

- Exchange Rates
- Technology Impacts on Retail Business – Overseas and in Australia
- Equity
- Costs of doing business in Australia
- Australian company buying prices ex-factory
- Relative profitability
- Warranty obligations imposed on Australian businesses under the *Competition & Consumer Act (2010)*
- Employment consequences from a 'do-nothing' approach
- Intellectual property and Trade Marks

The basis for some of the views expressed herein comes from 32 years as an importer of photographic merchandise into Australia, 25 of which were for a major Japanese camera brand, *Nikon*, as a private company, and five years as a multinational subsidiary of a brand owner of camera bags, *Lowepr*, manufactured in China. During that time I saw the end of Sales Tax, The Productivity Commission review of Duty-Free Allowances in the late 1980's, introduction of GST and the emergence of the Internet as a major force for change in retail practice and consumer preference.

RECENT BACKGROUND & OVERARCHING PRINCIPLES

What are not in dispute in this submission are basic principles:

- Fair competition should encourage rigorous competitive behaviour designed to afford consumers choice and value
- Based on fair competition some parties will prosper, some will not
- Consumers should be free to choose from domestic or overseas sources, with a varying basket of value propositions, warranties and price considerations

Several high profile retailers have highlighted a perceived inequity in competition behaviour, in that goods imported under the \$1000 threshold are free from duty and GST, whereas Australian retailers have to charge their customers such fees. The bulk of the adverse public commentary in both electronic and print media, to date, has come from people who aren't paying retail taxes on such personal imports. The GST is the only long-term growth consumer tax currently in Australia. Those who choose to buy offshore do so in addition because of greater range, choice, lower prices (whether because of the absence of GST or other factors,) or availability where such goods are not offered in Australia. If an item is not available in Australia, government should not artificially restrict access to such goods, provided the consumer fully bears the cost of the decision to purchase that item across the full transactional process of the supply chain, including processes that involve government agencies carrying out the laws of the Parliament.

EXCHANGE RATES

The appreciation of the Australian Dollar against many other currencies in late 2010, which has accelerated in 2011, brought into focus significant price differences on many small consumer items, laptops, GPS, cameras, lenses etc., compared to prices charged in countries like the USA. In contrast to the appreciation of the A\$, the US\$ currency has reached historically low values compared to trend averages. The public response to such differences has inevitably attacked perceived "gouging" and business models of several retailers, as well as accusing Australian importers of profiteering.

As will be discussed later, costs of doing business in Australia, in part because of employment laws and tax obligations, as well as because of geography and relatively small population, are relatively higher than large nations such as the USA, or emerging developed economies such as Hong Kong, Singapore. In those countries the compact scale of their State significantly lower costs of doing business (transport), while they also enjoy much lower employment costs, along with low-cost advanced freight infrastructure.

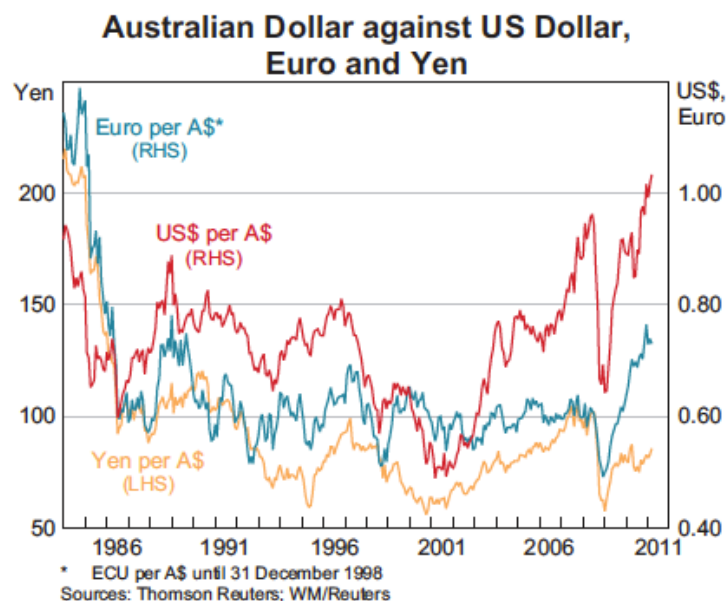
By 2008 the Australian dollar had dropped from a 1979 level of US\$1.23 to the A\$, down to US\$0.59. Over that 29-year period the A\$ had risen back to a level close to parity more than half a dozen times. (See graph over time on the page following.) Over 30 years the Australian dollar seldom varies by less than $\pm 7\%$ against the US\$ in any one year. In the past 10 years that band has often moved out to $\pm 15\%$.

Importers, required to offer consistent prices to their customers, take a midway path in currency planning for such broad swings in currency. Common Commercial practice is to cover for extremes (cost!). This insulates their retail clients from excessive negative bumps in the low point of the A\$ cycle. Importers hold some of the gains back when the A\$ hits unusual highs, which in 30 years, have seldom been sustained for more than a few months. Within the month of March 2011, for example the currency varied up and down by more than six per cent. In April 2011 it appreciated by 11%.

Currency variation therefore is a key factor in highlighting current advantages in overseas purchase. Conversely in late 2008 /early 2009, when Australian importers were offering products purchased at currency translations 30% better than prevailing spot rate, Australians, fuelled with Stimulus disposable funds, enjoyed prices lower than those available from the USA, even when taking into account GST.

Thus, it is important to register that the first factor of Australian Retail competitiveness relative to overseas markets, is the prevailing exchange rate of the Australian dollar, and the impact that results from any lag of forward-dollar covers versus prevailing spot rates over time, as practised by most importing businesses. As of 4th May 2011, our own business is committed to forward purchases of the A\$ at a rate below parity for some months forward, while spot rates are some 10% above parity. This is then reflected in an importer's inability to fully reflect exchange parities in pricing as a result of risk management policies in relation to currency.

Australian Dollar 1984 – 2011: Source – RBA, May 2011 Chart-Pack.



TECHNOLOGY IMPACTS

The second factor causing pressures on local pricing relates to technology change and consumer empowerment. As 1930's economist John Maynard Keynes implied in *The General Theory...* markets work best when buyers are perfectly informed of all available supply, and where no one buyer may influence the price of a product. In that era technological information blocks existed to prevent the most efficient means of achieving real competition. Since the Internet emerged, and price comparison engines can generate instant "worlds' best price comparisons", consumers in all markets may establish what the real price of a good or service is.

In Australia, as has occurred in most advanced economies, retail distribution has become somewhat concentrated in fewer and fewer hands over the past 30 years. The pharmacy industry, the food sector,

the electrical and electronics sectors, home improvement – all have seen diversity of retailers reduced, and relative market power for such retailers has progressively increased. This has led to some efficiencies and the creation of “category killer retailers” in certain industry sectors. It has discernably led to increasing demands for concessionary prices from importers. This in turn has lowered wholesale margins, and forced some efficiencies on the importer segment. Those who failed to achieve such improved efficiencies either failed as enterprises, or had to merge to gain sufficient economic viability. This is the market working as it should, providing sufficient choice and diversity so that consumers are better served in price terms, but not concentrated so much that monopolistic tendencies emerge. Wide-scale computerisation, supply-chain EDI process changes, scanning and real-time demand management, have all lowered cost and given consumers more competitive prices locally. But it is observably true that retail margins in Australia are generally above those seen in many other major retail markets, or in Internet-based businesses, operating overseas. This cannot be ruled out as a factor in price differences seen in Australia.

In the post-WW2 era the world was divided arbitrarily into regions, essentially North America, Europe, Asia/Oceania, Other (mainly Middle East, Africa and Latin America). Because each market had different populations, languages, labour laws, holiday allowances, tax systems and duty regimes, prices were not transparent or easily comparable. Over time costs of doing business were established to conform with those variables. As the world grew smaller, manufacturing of certain technologies centred on fewer and fewer places, prices developed an ability to become more uniform, all other things being equal.

Today Australia finds itself as a country nearly the same physical size as the USA, but with just 22 million inhabitants vs. the 310 million of the USA. Minimum wage rates, local taxes, sales tax and a host of other variables still enable the physical exploitation of markets in the US to be amortised across a market 13X greater than the Australian population. In fact generally every element of cost has a lower marginal cost in the USA than does Australia.

Physical distribution across continents is influenced by quality of infrastructure, cost of transport and the labour laws determining salaries and conditions. So it is that generally consumer products in the USA are amongst the lowest found anywhere – large population, favourable economics of distribution, low taxation, and relatively high disposable income. However, as the US economy went through the effects of the GFC (Global Financial Crisis), market forces tended to lower margins further in the US to retain relative affordability in a market where 30 million families lost their homes. Thus a combination of an informed market through technology and lower marginal costs of distribution further changed relative values between Australia (which enjoyed a non-recessionary marketplace throughout the GFC) and the USA.

HISTORY OF THE GST

When former Treasurer Costello introduced the GST bills into the Parliament in December 1998, he did so to protect the national tax base. In so doing he included the taxation of services as well as goods. At the same time a claimed \$13B of Income tax cuts were passed to Australian taxpayers¹ by way of compensation. GST was intended to be revenue-neutral at time of introduction. Sales Tax previously covered Goods - a diminishing percentage of National Income. Services, according to the ABS, now account for about 75% of National activity², up from 60% in 1970. All retailers and service providers became tax collectors under GST. This added to Australian business costs. Under Sales Tax a reported total of just 35,000 organisations were involved. Retailers were not involved in taxation on consumption at all, just their suppliers. For the GST to be efficient and fair, all goods and services, with minimal exceptions were required to be included. In taking this stand the government and Treasury specifically determined to avoid the UK route of zero-rated goods and reduced rate items, adopted in April 1973 by the Heath Conservative government.

The implementation of a broad-based consumer tax, however, has not been evenly implemented in practice by two sectors of government, Customs and Excise, and Treasury.

“Tax collection by Australian Customs on sub-\$1000 transactions is not required.”
The Australian Customs website states:

“If your goods arrive in Australia by mail and have a declared or assessed value of A\$1,000 or less, the goods may be imported free of duty, taxes and Customs and Border Protection charges, unless they are

¹ Senate Select Committee on *A New Tax System*, Parliament of Australia, 1999.

² ABS Australian National Accounts, Series 5206.0, March 2011.

alcohol products or tobacco products. Apart from alcohol and tobacco products those goods will be cleared by Customs and Border Protection and delivered by Australia Post without you doing anything.

Goods with a declared or assessed value over A\$1,000

You will be sent a First Notice by Australia Post if you have imported goods with a declared or assessed value of more than A\$1,000.

In this case, you need to lodge an import declaration to Customs and Border Protection for the goods. The declaration will be assessed for duty, GST and Wine Equalization Tax (if applicable). An import processing charge will also apply. Customs and Border Protection will advise you of the amount you need to pay before your parcel will be delivered to you.

Customs and Border Protection cannot allow goods with a value over A\$1,000 to be delivered by Australia Post until an import declaration is made and any liability for duty, taxes and charges is paid in full. There may also be AQIS requirements to be met before Australia Post can deliver your goods.”

It is the charter of Customs and Excise to impose those duties and taxes on behalf of Government as shall apply on goods when imported into Australia. It does so under the following authority, as Stated on their website:

“Customs derives its authority principally from the Constitution, which provides for the levying of customs duties and for laws with respect to trade and commerce. Customs constitutional authority is given legislative expression through the Customs Act 1901, the Customs Tariff Act 1995 and related legislation. Customs also administers legislation on behalf of other government agencies, in relation to the movement of goods and people across the Australian border.

Customs was established in its present form on 10 June 1985 by subsection 4(1) of the Customs Administration Act 1985. It became responsible to the Minister for Justice and Customs on 21 October 1998 as an agency under the Attorney-General's portfolio.”

The obvious question that must be asked: Why is there a difference in goods imported below or above \$1000?

In the *Review of the Application of GST to Cross Border Transactions*³ to the Assistant Treasurer in February 2010, the Board of Taxation confirmed that cross-border supply of goods are "connected with Australia." They also confirmed that such goods were consumed within Australia. But they then went on to say that collection was too complex administratively. That same complexity imposed on Australian importers and Australian retailers on goods and services in general business was not deemed too complex or inefficient when the "New Australian Tax System" was introduced as law in July 2000.

There is a fundamental inequity in which an obligation is imposed on the citizens of Australia that the government of those same citizens says is too complex or costly for it to collect itself. At the same time it demands a selected number of those citizens or companies must collect by law, while allowing citizens of a foreign power to act outside of that law, when carrying on the supply of goods, "connected with Australia." Having stated that goods that are "connected with Australia" should have a consumption tax and import duty (as applicable) imposed on them, it is simply a double standard to arbitrarily say that some citizens can buy goods tax free and others must pay tax, entirely based on reasons of administrative simplicity.

That is what a public service is for – to serve the citizens, not to choose on grounds of administrative convenience which citizens pay tax and which don't. Once a law has passed establishing a principle that a consumption tax is payable on goods imported into Australia, it is potentially unconstitutional for the Executive branch of government to establish an arbitrary threshold giving advantages to those with sufficient funds to pay for goods to values up to \$1,000. Further, it extends that privilege as many times as that consumer chooses to buy goods from other countries. It allows these persons to unfairly benefit from not sharing in the obligation of paying consumption tax that benefits all other members of society, through its 100% distribution to State governments for the funding of education, health, Police,

³ *Review of The Application of GST to Cross Border Transactions*, Board of Taxation, 2010

infrastructure and the other duties of States. In the increasing prevalence of Public-Private equity ventures for infrastructure development within Australia, the principle of User Pays has been developed as a broad component of Australian life. It therefore seems inconsistent that those people who choose to purchase goods from overseas should not have to themselves directly reimburse government the full cost of processing those imports while Customs and Excise and Treasury carry out their Excise and tax-collecting obligations under law.

It would be my contention that if Treasury estimates there is a significant cost to administratively process such sub-\$1,000 transactions, then that estimated cost should be imposed on those who choose to import such goods directly, even if such cost imposes some inconvenience to the importer and the need to employ extra personnel within government. Any other course of action is discriminatory and inequitable, both socially, on consumers who do not or cannot avail themselves of such opportunities, and on Australian business who must comply with government laws and regulations.

THE REALITIES OF BUSINESS AS AN AUSTRALIAN IMPORTER

In the case of the photo industry, in which I have spent the last forty years of my life, margins have fallen each year, as global competitive pressures and the Internet's immediate knowledge of "world's lowest price" became possible through comparison price shopping sites. In the years between 2000 and 2006, in which my previous company was an independent importer of a major Japanese camera brand our net margins after company tax were never greater than 3%, averaged 1.3%, and on two occasions a loss was incurred.

Despite rising and falling values of the Australian dollar in that time, (+/- 15% a year was a typical variation in costs) retail prices of cameras, along with technological feature advance, fell by an average between 12 and 15% a year. Affordability of a quality camera for home consumption improved in real terms by a factor of more than 2, from 2000 to 2006, and has done so again, between 2006 and 2011. In 2003 an entry level DSLR retailed for A\$2,200. An equivalent camera today retails for \$750. A home compact point & shoot camera was \$600 in 2003; today's equivalent is \$169.00.

The Internet now comprises, some 9%+ of all retail activity in the UK⁴. Two years ago this was measured by *The Office of National Statistics, UK*, as just 4%.⁵ An estimated 12% of some technology sectors, such as the camera industry in Australia are currently transacted over the Internet, based on warranty claim rates of some camera companies and other anecdotal evidence. It's growing fast, potentially damaging Treasury's ability to collect the planned Tax revenue from Australian Goods consumption.

On the following page I submit a theoretical business model that shows the consequence of a 9% loss of business, from reduced Internet activity caused by GST-free imports. With margins as fine as those found in the consumer electronics/camera industry, <5% sensitivity in volume exists before profit turns to losses.

Importantly, that loss occurs after two other key actions a company would take to arrest falling margins and revenues. Typically a 20% cut in sales personnel or sales costs would have to be made, to cut back on losses incurred. That might be jobs, it might be fewer exhibition space-costs, or cancelled retail cooperative advertising. Conventionally a reduction in advertising and promotional marketing costs would also result. Finally as a loss results, no company income tax is paid. In a small company the labour numbers might at least take it below the threshold for paying State employment taxes.

Ultimately this enterprise would run out of working capital. At that point, as perhaps the only provider of local servicing backup with local parts stocks and of course employment for service technicians, local consumers would lose all local service arrangements supporting warranties under the *Australian Competition & Consumer Law (2010)*. Directors would be in breach of their obligations through no fault of their own. The lack of a level playing field directly would result, over time, in reduced local support, prices being raised by overseas suppliers for lack of local competition, fewer marketing dollars invested and reduced local employment.

In the Productivity Commission's own paper *Economic Structure and Performance of the Australian Retail Industry* (March 2011), the added cost burdens imposed on retailers by wide diversity of trading hours (Pages 27-28), further reduce the hours over which a retailer may amortise their fixed costs of doing

⁴ <http://www.statistics.gov.uk/pdffdir/rs0311.pdf>

⁵ Office of National Statistics, UK, *Retail Internet Sales (Experimental)*, 2009.

business. This restriction, especially in Western Australia, which already has higher transport costs, adds to price premiums for Australian consumers. Such restrictions do not exist in Asia or other tax-free overseas markets, and seldom are seen today in the USA, except in some State food-sale laws.

COSTS OF DOING BUSINESS: HOW MARKET MECHANISMS MIGHT PLAY OUT

When net margins are as low as is the case in camera wholesaling, a 9% reduction in volume can turn a business from a small profit to a significant loss. See theoretical model below:

	Camera Wholesaler	Price response to attempt to compete against tax-free imports bearing no 10% GST imports*
	Pro-Forma Before GST-free imports	
Sales including GST	110	106.26
Net Company Sales	100	96.6
Cost of Goods Sold	85	89.25
Gross Margin	15	7.35
%	15.0%	7.6%
Operating Expenses		
Selling	4.5	3.6
Marketing	5	3.5
Administrative	4	4
Total	13.5	11.1
Operating Income	1.5	-3.75
%	1.5%	-3.9%
Income Tax at 32% effective rate	0.48	-1.2
Net Income	1.02	-2.55
%	1.0%	-2.6%

* Real World actions resulting from competing against 9% loss of business due to GST-free imports

1. Lower revenues mean prices get cut 8% to compete, increasing volume back by 5%
2. Goods don't cost the supplier any less, except lowering price increased volume, so total cost of goods actually rises
3. With less Total GM dollars (actually half), local business cuts sales force by 20%, and drops marketing investment by 30%.
4. Admin costs of accounting, collections, service staff and management not cut, because all functions critical to the business.
5. Net income before tax has dropped from 1.5 (1.5%) to a loss of -3.9% before tax.
6. Sales personnel and local marketing has been cut, 3.75% less GST raised on local sales, no income tax to government.

Examination of the structure of the camera business, of an estimated 2.2 million compact fixed lens cameras sold in Australia each year, 95% would come under the \$1,000 value. So in this case the whole regular industry is potentially at risk of discrimination from personal imports not required to pay GST and priced at levels that do not have to take into account Australian employment legal obligations. Added to this price sensitivity of which GST is a key part, but not the only factor in play, is the competitive technology of the Smartphone, which in the near term, can also be expected to produce marginal consumption loss of the entry-level compact camera, further exacerbating the GST-free impact.

The Interchangeable Lens camera business, of which some 250,000 are sold annually in Australia, 60% of cameras fall below the \$1,000 threshold, and 60% of the lenses used on those cameras. The net result is that substantial imbalances now exist structurally for a whole industry segment worth over \$800 Million at retail, and which have flow-on print and other services worth a further \$700 Million.

EQUITY and THE CREATION OF A LEVEL PLAYING FIELD

It is the contention of many retailers, and smaller importers of goods that have a product value of under \$1,000, that there is a major unintended consequence on thousands of retail and hundreds of Australian importing companies resulting from the administrative decisions made in relation to a tax-free allowance of \$1,000 on imports.

When the "Duty Free Allowance" for personal travellers was lifted from \$400 to \$900 an unintended consequence of this was that only those citizens with enough disposable income to travel overseas could buy products at such concessionary rates. This change was introduced well before commercial Internet purchases had become mainstream. That law specifically prohibited the supply of such concessionary goods to be passed to third parties after importation.

For goods arriving in Australia from overseas a concession based on administrative convenience set at \$1000 theoretically allows a commercial business to import goods of \$365,000 in 365 individual parcels free of duty and tax. There is considerable anecdotal evidence that practices, perhaps not as significant as this, are now a major part of the black economy in which traders using eBay and other similar sales portals are not registered for GST and trade, frequently under multiple different identities.

Goods are regularly advertised on eBay with commercial addresses in Australia in which it clearly states that supply will be from Hong Kong or China. Such advertisements also regularly use as illustrations the Intellectual Property of local Brand owners by way of photographic data files copied without authorisation from the IP owner's or licensed user's website. This is a breach of copyright.⁶ Some suggest or infer that the local registered importer of such goods will undertake the warranty of such goods. The vendor implies this, since the original manufacturer covers many of these goods under the Worldwide Warranty arrangements of such branded goods.

This practice dates back to times when exclusive distribution agreements around the world provided some basis for such programs. Under the *Australian Competition and Consumer Law, 2010* such practices illegally pass the obligation of support, by implied warranty, to a third party who was not the agent for the sale of that good. Equally the prices charged for such goods give a strong impression that even for goods with a normal commercial value of above \$1,000, no GST has been paid, even though an invoice may include a charge for GST.

Such practices allow retail trade to be carried on by a part of the economy of Australia in which a whole range of normal obligations of tax payment, compliance with the *Australian Competition and Consumer Law, 2010*, State and Federal employment laws etc. appear not to be enforced.

On the following page is a list of the differing imposts carried by Australian businesses, wholesale and retail, not necessarily born by overseas entities against whom Australian business must compete.

/ See next page

⁶ *The Australian Copyright Act, 1968 (Cth)*, as amended.

A local commercial entity must address the following costs of doing business, not incurred by their GST-free overseas competitor.

Cost of Doing Business for a <\$1000 Transaction	Local Business	GST-Free O'seas-based Business
ASIC Annual Return Costs	Yes	Free
Quarterly BAS Statements	Yes	Free
State Employment Tax (5.3%-6%)	Yes	No
Monthly GST return & payment	Yes	No
Super'n Guarantee Levy (9%)	Yes	No
Import Duties (0-10%, varies)	Yes	Not if < A\$1,000
GST at 10% on goods & services	Yes	Not if < A\$1,000
Warranty (Competition & Consumer Law, 2010)	Yes	No
Product Stewardship Bill (2011) compliance (Product dependent)	Yes	Unknown
Freight to Consumer	Included Free to all States by most wholesale businesses, or demanded by major retailers	Customer Pays
Local Rent	Yes, ~ \$900-\$1,600 / Sq. M, p.a., for smaller retailers, & \$400-\$800 for major retailers.	Often home-based, nil occupancy

The higher costs of employment, location, support, local marketing and other business costs, all add to the lack of ability to match their lower cost overseas competitor, or a non-conforming Australia-based intermediary business operating on the internet without regulation. In addition, the scale of many overseas-based businesses, especially those in the US, mean that their business models, through sheer volume, enable their employment costs, as a percentage of revenues, to be anything up to half of equivalent companies in Australia.

There are multiple cost premiums that an Australian employer must add to employment cost

- Super – 9%
- State Payroll tax – 5-6%
- OH&S obligations, as well as Equal Opportunity implementation – Unmeasured – perhaps 0.5%.

There are also other key on-costs not necessarily born by overseas traders:

- Warranty Obligations – Up to 2.5% - implication by many that local importers will fulfil “their obligations under worldwide warranty” terms.
- Product stewardship – 0.5 – 0.75% estimated - a necessary and desirable obligation to ensure environmentally responsible disposal of resources and waste goods, sometimes toxic.
- Rent premiums vs. The USA (30-50%) – just another difference in the cost of doing business
- Import Duties – generally lower than USA in high-tech, but higher than Asia which is Duty-Free on many consumer goods

There are other cost differences faced by Australian importers:

The largest global markets have long been offered lower FOB prices, because of the size of the orders placed by traders from large markets (USA) or countries who pay in advance and have low costs of distribution. In the case of photo products, it is likely that Australian independent distributors will typically have paid between 5 and 15% more for goods ex-factory than their US counterparts. **This single factor is likely to be the primary base cost disadvantage faced by Australian wholesalers and retailers,**

and in turn by Consumers. The further impost of GST and other on-costs described above, exacerbate this fundamental cost base difference.

HOW DO OTHER COUNTRIES DEAL WITH THIS GROWING ISSUE OF TRANS-BORDER RETAIL TRADE?

I would like to bring to the attention of the Commission, two countries that have established solutions for the administrative costs of transacting low value items.

Canada

In 1991, the Canadian Federal Government replaced the FST with a GST. Like Australian sales tax, the FST was imposed at wholesale prices, while the GST introduced was a consumption tax taxed on the final consumer, with taxes imposed along the supply chain as being input credits to those producers.

Under **G300-8 Imported Goods (GST 300-8)**⁷ the implementation of the Canadian Customs Act requires Customs to impose GST at time of import, except where dispensation for registered business entities exists. Under Free Trade Agreements between Canada and the USA, duties have progressively been reduced between the two countries, but GST remains payable at the time of import.

In the case of the Photo Industry, American retailers provide a means of collecting that GST obligation of the Canadian buyer, by providing on their websites special payment options exclusive to their Canadian customers. The customs declaration by the vendor lists the GST paid, the GST licence or trader's number. The companies involved then remit such funds monthly or quarterly as required to the Ottawa Government.

Personal import thresholds for returning passengers enable Customs to charge GST and Import duties where thresholds above \$40 apply. In some cases these can rise to an exemption of \$400.

UK

HM Revenue & Customs impose duties and VAT on transactions worth £40 or more.⁸

Under the UK Revenue & Customs practice provisions have been set up, amongst others, for :

- prepayment by vendors overseas, registered to do so with UK Revenue & Customs, and posting goods to the UK to display their licence number and amount paid
- For Royal mail to charge the out of pocket transactional costs on parcels and to act on behalf of Revenue & Customs
- To ensure a full declaration of correct value has been made by the overseas vendor.

I quote from the publication referenced below:

"Charges are calculated by UK Border Agency (UKBA) staff at the postal depots where the packages are received. However, in some cases special arrangements are in place for goods purchased on the Internet (see paragraph 3.4 below).

Value Added Tax (VAT) - Import VAT is charged at the same rate that applies to similar goods sold in the UK and applies to commercial goods over £18 in value, and on gifts that are over £40 in value. The value of the goods for import VAT is based on the:

- basic value of goods, plus
- postage, packing and insurance, plus
- any import (Customs or Excise) duties charged.

Customs duty - Customs duty becomes payable if the goods are over £135 in value but is waived if the

⁷ Canadian Government Document: <http://www.cra-arc.gc.ca/E/pub/gm/g300-8/g300-8-e.html>

⁸ HM Revenue & Customs:

http://customs.hmrc.gov.uk/channelsPortalWebApp/channelsPortalWebApp.portal?nfpb=true&pageLabel=pageTravel_ShowContent&id=HMCE_CL_000014&propertyType=document#P137_11462

amount calculated is less than £9. Customs duty is usually charged as a percentage of the value of the goods.”

CONCLUSIONS & COMMENT

I believe many retailers, in their early comments prior to Christmas 2010, underestimated how much 'leakage' was occurring to their business from trans-border and Australian online activity in the technology sector. As the A\$ increased in value and price drops lagged spot rates, this leakage accelerated in the March Quarter of 2011, and into the June Quarter of the same year.

The efficiency of a given retailer's business model is not the primary driver of price inequity. The market will decide any observed deficiencies in business models over time. If books are too expensive compared to overseas, the market will gradually sort that out by forcing change in the business model of importers and retailing. Amazon's Kindle has completely altered that whole book industry-model globally, just as Apple iTunes has with recorded music and movies. Distribution models of intellectual property which change a physical good into a 'transferrable byte' inevitably will result in a different set of values in each step of the supply chain. This submission does not argue against that inevitable alteration of how people buy music or books. It does differ, however, when physical goods are involved.

"The GST issue" is ultimately one of equity, along with costs of doing business and the desirability of government creating a level playing field. It is unjust and bad law in a competitive economy to tax one supplier and not another. It is unfair to discriminate on Australians with a capacity to pay for goods purchased from offshore and ask other less-wealthy Australians to bear the cost of that lost tax applied in other areas, or reduced services. GST not charged on sub-\$1000 imports means fewer hospital beds, a diminished national educational curriculum or fewer dollars for needed infrastructure. Government should not arbitrarily permit overseas traders to trade in goods or services "connected with Australia" to have a tax advantage of 10% over Australian companies trading within Australia.

For the government to continue to ignore the Internet's dynamic change within retail segmentation, where some 20% of consumption may ultimately occur in the Online space and potentially much of it to be free from GST, is to completely distort the playing field. Under that argument an Australian retailer with a New Zealand business unit should encourage online purchases to be transacted with their NZ entity, and charter planes for daily delivery to Australia. Exports from NZ would be non-taxable or subject to tax drawback for the supplying entity under the *Closer Economic Relations* code operated between Australia and New Zealand. Clearly such a course would impose massive extra administrative workload on Customs.

The simple issue should be that consumption of goods and services associated with Australian consumption should have the same rules applied, regardless of whether supply is from an Australian entity or a foreign one. If the mantra of Government (and Opposition) is to be consistent it is clearly inequitable for overseas suppliers to be allowed to supply goods valued under \$1000 free from duty and GST, while Australian retailers and importers must pay Payroll Tax, Worker's Compensation premiums, Super entitlements, State Taxes, Company Tax, FBT and Capital Gains Tax on their business, as well as imposing GST on all transactions and having to cope with higher input costs caused by nation-scale.

Australians may not like to admit it, but it simply costs more to do business in this country. Australia is the size of the USA. Australia has just 22 million inhabitants, compared to 310 million in the USA. Marginal transaction costs are simply higher. Yes, if overseas manufacturers provided their subsidiaries and agents identical prices to those offered to the US, Australian retailers would have one less obstacle to globally competitive prices. But in many cases, differences in electrical standards, State and Federal safety laws, radiation compliance tests, environmental standards and other factors, contribute significantly to short-run production cost differences. There really is a difference in manufacturing 10,000 power chargers for an Australian customer, versus 130,000 for the USA.

It's bad policy to distort the economy through discriminatory taxation on only parts of the consumption chain. That's why Europe has scrapped "Duty-Free" sales for residents of member countries of the EU. It is inequitable to discriminate against a nation's own taxpayers in favour of foreign entities. Is it administratively complex? No! Not in a day of automated, computerised lodgements. If User-pays applies to roads and so many other previously 'free' government-provided services, then privately imported goods should pay their fair share, and the cost of collection be born by the user or consumer. Is such a change likely to be popular? No! But the role of government is often about doing the right thing, and taking into account the long term interests of all Australians, not just those that can afford to buy goods from overseas. If, as has been suggested in the media by some commentators, that up to \$2B of GST revenue is being foregone in these early days of Internet retailing, then many more billions of dollars will be foregone if current policy is allowed to continue. To achieve balanced budgets and provide needed services, the community must be more evenly taxed when it comes to payment of GST.

At the start of this submission I cited multiple factors that militate against continued adherence to a \$1,000 tax-free threshold and the unequal imposition of GST on Australian consumers. I summarise the points I have tried to cover within this submission.

- Exchange Rates – major long-term variance to historic US\$0.75c 10-year average exchange rates in the past 12 months. This has exacerbated an underlying imbalance in competitiveness.
- Technology Impacts on Retail Business – Overseas and in Australia – new products with declining inherent cost, as well as consumer information to world's lowest price comparison engines on the Internet.
- Equity: Where is the natural justice of discriminating against Australian corporates in favour of overseas entities, by administrative practice?
- Costs of doing business in Australia: Government and Society imposes those standards – there is a price to pay for that that should apply to all.
- Relative profitability: Australian businesses, through smaller scale, have greater relative vulnerability to marginal changes in volume on their basic viability.
- Warranty obligations imposed on Australian businesses under the *Competition & Consumer Act (2010)* – The new law is not imposed equally as a result of the GST-free import threshold, and “normal importers” bear an undue burden of compliance and negative PR from this inequity.
- Employment consequences from a ‘do-nothing’ approach – Do nothing and employment and diversity of consumer choice, especially in bricks and mortar businesses on a regional level, will be diminished.
- Intellectual property and Trade Marks – there are thousands of breaches of Intellectual property law and Trade mark usage by unauthorised traders who appear to be allowed to operate with impunity, or at undue cost to the Trade Mark or IP owner to protect.

See over for final recommendations.

RECOMMENDATIONS

1. That the Commission consider the basic inequity in Government agencies taxing Australian businesses for all goods and services transacting business “connected with Australia” but that it chooses, for reasons of administrative efficiency, not to tax similar goods and services supplied by entities outside of Australia, to Australian residents, and as a result of such consideration, to establish a system of fairness and equity to enable the GST element of price disparity to be removed from Retail competitiveness within Australia.
2. That a User-Pays principle be established on all personal imports, or commercial imports, such that such imports incur charges from the transacting instrumentalities (Customs,. Australia Post, Private Courier Companies etc...), based on the actual cost of processing such imports and born by the consumer making that import.
3. That the Commission, in reviewing the various impacts on the Australian Retail Trade, consider the safety issues to which Australian residents buying goods from overseas are exposed, when the personally-imported goods do not bear the safety approvals demanded by law of Australian Retailers, for the sale of similar (but not necessarily identical) goods, such as N-numbers or C-Tick registration numbers, when supplied through Australian businesses.
4. That the Commission duly note the sensitivity to marginal profitability of smaller Australian specialist suppliers of imported goods requiring service provision under Consumer & Competition Law, and that should such firms may be marginalised or fail without a more level GST tax treatment,. Australian consumers might no longer have access to local repair facilities to effect warranty cover as required by law for “reasonable” periods after local purchase.
5. That the Commission consider the imposition of some limits to the frequency with which any individual may import goods “of a personal nature” sub-\$1,000, that evidently are in fact related to commercial activity, and at the same time, ensure that such entities are registered for GST, Quarterly BAS returns and the like and provide evidence at the time of import to authorities.
6. That the Commission duly consider the capability of modern online revenue capture tools, that Customs set up such a revenue capture website for Australian consumers. Such a site could potentially enable individuals to be contacted electronically by the overseas vendor, go to the Government revenue site, securely key in themselves all the details of the import, its value and nature, pay any taxes or duties due, and effectively enable Customs to view whether an item has paid its dues for import, and then pass it for random security screening and then ultimately goods release to the consumer or carrier, at the cost of the importing individual.

I submit these comments for the Commission to deliberate.

John Swainston

May 2011.

John Swainston has been involved in the Australian Photo Industry since 1979. He first joined the industry in the UK in 1971. He has worked for US-based multi-national enterprises in the Imaging Industry, as well as running a privately-

held import distribution business for 24 of those years. He is currently Senior Vice President for the DayMen Group of Companies (Lowepro & Acme Made photo and IT bags), as well as Managing Director of Australian subsidiary, Maxwell International Australia Pty. Limited. He served as President of the PIC (Photo Industry Council) in 1982-1983, and twice as President of PICA (Photo Imaging Council of Australia., in the 1990's and again in 2008-9. He served as Deputy Chair of the Australian Centre for Photography from 2003 - 2005. He has lectured on Photographic Retailing in the USA, Canada, Australia, New Zealand and China.