



Productivity Commission Inquiry: The
Economic Structure and Performance of
the Australian Retail Industry

Response to the Issues Paper by the Direct
Selling Association of Australia

May 2011

Introduction

The Direct Selling Association of Australia (DSAA) thanks the Commission for the opportunity to comment on issues raised in the Commission's Issues Paper dated March 2011.

DSAA is the national trade association and voice of major players in Australia's direct selling industry. DSAA was established in 1967. It has seventy members with combined annual retail sales of the order of \$1.6 billion. For the most part the business focus of its members is to distribute products in the retail channel. This is achieved by the unique strategy of member companies selling to independent sales people (ISP) through arm's length contracting arrangements with these ISPs.

The major areas of retail sales achieved by ISPs are in the consumer product markets for cosmetics, skin care and personal care; nutritional and therapeutic products; and kitchenware and other household products. In the first two categories members are major wholesaling suppliers to the Australian market for those products through the sales activities of their ISPs.

The DSAA has made submissions to the Productivity Commission (*Review of Cost Recovery by Government Agencies, 2002*) and to State and Federal Government bodies over the past twenty years. Depending upon circumstances in the Australian economy, the sales force of ISPs has fluctuated between 400,000 and 600,000 people. Women comprise more than eighty percent of that substantial element of the Australian population. They seek an occupation that rewards them for their effort but does not impose either a floor or ceiling on their enterprise and input.

Observations regarding the future direction and channels for retail trade

Retail trade is often characterised by government and the media as comprising major shopping centres, chain stores, high street strip shopping, service stations increasingly functioning as outlets for the major retailers and a dwindling number of corner shops. Despite its long and substantial history the direct selling industry has only interacted with Federal and State Governments in relation to regulatory matters.

Before the Goods and Services Tax (GST) was introduced, Commonwealth Treasury was unaware of the size and scope of the direct selling industry. Specific representations to include the industry in the Government's information and training initiatives with major industry organisations were made to Treasury, and resulted in the Industry receiving Government assistance for the GST education of the independent contractors comprising its sales force.

The Australian Bureau of Statistics still does not provide a disaggregation in Division Five '*non store retailing and retail commission-based buying and/or selling*'. A major structural change in the Division is required that recognises forms of marketing and selling by retail that were simply not contemplated when the Division was first established by the ABS. It is not possible to improve what is unknown. At the present time Division Five does not enable an accurate disaggregation of data received by the ABS from very disparate retailing groups.

The ABS definition has been moribund and obsolete since the seventies. DSAA members have a significant share of the retail market for cosmetics, therapeutic goods, wellness products and other household consumer goods. Some direct selling organisations have operated in the Australian market since the 1950s.

Historically, the retailing industry was started by peddlers who moved from household to household and hamlet to hamlet. As towns grew into cities the peddlers started shops and eventually created a chain of shops. Shopping centres were created in the early sixties and ultimately became major shopping malls consisting of hundreds of shops. With that consolidation came problems of parking, distance from residential areas, high operating costs and space rentals. Shop fit outs are also a major and regular additional charge imposed by the property owning landlords.

It is commercially simplistic to believe that the evolution of retailing to the present stage of city based major retail conglomerations is the end of the evolutionary process. This Inquiry is about the structure, performance and future of the Australian Retail Industry. It is not about finding ways and means of preserving the hegemony of major retailers and stifling or delaying innovation in the industry.

The present retailing paradigm has been under siege for the past fifteen years or more. The Productivity Commission Inquiry into the *Market for Retail Tenancy Leases* published in 2008 received a substantial amount of evidence from smaller retailers regarding the financial pressure created by constantly increasing store lease costs, rentals rising as shop takings increased and the constant insistence by the landlord on regular new shop fit outs to meet changing centre designs and formats to attract new tenants.

The Internet is the medium and Social Networking is the message for the present massive revolution in communication and personal participation in a global market that promotes, communicates, advertises, explains and ultimately sells products to consumers in any place and at any time. The goods and services are generally transportable and the buyers are computer literate and commercially savvy. This is a form of peddling that returns to the personal interaction of five hundred years ago, but has a technology twist that only started in the last two decades.

The new markets on the Internet attract all generations but largely belong to Generations X and Y. These generations are technologically literate and expect to receive product that meets the sales specifications. They are part of a generation that regards product quality as a given and that global products are supported by service and warranty.

Generations X and Y will use the Internet to search for different products across a range of quality and performance and will then focus on relative prices, after sales service and warranty at home and overseas. Delivery of product has been virtually homogenised by DHL and is not a significant factor in purchasing decisions that may involve offshore supply.

Business Models

The rise and rise of Internet marketing on both a global and national basis is, in the DSAA's view, a demonstration of the continual potency of the evolution of retailing. The direct selling concept of retailing by independent sales people is ideally suited to that constantly evolving and changing process. These people are not bound by their employment to a retailing approach that is unable to change because of the level of previous investment by the retail owners in processes and bricks and mortar.

The Internet, direct selling and retail stores of various sizes and configurations constitute the three major retailing pathways to the consumer market.

These channels are constantly evolving, merging in particular retail market segments and strategies and using a combination of measures to obtain the consumer dollar. It is not true to talk about specific processes as the only strategy for a retailer. In our own industry companies that were Party Plan, so called Multi-level Marketing (it is not really a marketing process but an ISP payment structure) and door to door sellers are now using combinations of all these selling strategies. All direct selling organisations use the Internet and social media is integral at member and distributor levels to establishing and maintaining sales relationships.

The convergence of what were distinctly different retailing mechanisms and strategies has been hastened by the Internet. Selling involves direct consumer contact either in person, by phone, or increasingly, via the Internet.

The fundamental driver of our industry is that direct selling organisations supply through relationships that are personally negotiated between an independent sales person and a consumer. That negotiation does not take place in a fixed retail location. It generally occurs in a home or workplace or, increasingly, on the Internet. In a recent study for the DSAA (*DSAA Industry Metrics 2010*) Monash University estimated that a significant portion of ISP selling occurred on, or with the assistance of, the Internet.

The essential elements in direct selling are product knowledge, trust and the provision of service. DSAA believes that these attributes and the requisite knowledge are increasingly absent from major retailers. Internet sales by ISPs who are personally known to the consumer have a major marketing advantage in the world of virtual product display and electronic consumer choice.

A consumer strategy is to research products on the Internet, use retail outlets to physically examine the products and then purchase them on the Internet. The online environment is starting to erode the instant gratification gap between product selection and product purchase which has favoured mainstream retailers.

The Internet actually offers a much wider range of consumer choice, purchase mechanisms and sales avenues. Products are available that are not present in the limited ranges of the retailers who are constrained by floor space and driven by supplier discounts for quantity.

In conclusion, DSAA regards the evolution of the Internet and the exponentially increasing ease of online purchasing and purchaser trust in sources of supply, product quality and after sales service as the “already here” next wave of retailing development. Our focus is on sales by ISPs who live in Australia because they possess the on-site advantage necessary to create the social networks that are capturing the attention of younger generations.

There is a level of systemic confidence in the networks of *Facebook* and other social networks that generates a cellular development of consumer groups who all have a fundamental connection to the social network at a particular level through an established and active member and a willingness to buy and sell through that network. They connect upwards to a person that sponsored them in the network and downwards to a person that they have sponsored. This structure is capable of infinite growth or at least growth that ultimately includes everyone on Earth.

The “friends concept” in social networks such as *Facebook* creates the value of being vouched for by an existing member of a social group. It is an extension of the long established idea of being sponsored to become a member of a club. As with clubs there is also the opportunity to ban someone from a club or to refuse their membership application. This principle creates strong bonds of common interest and loyalty between members.

The Internet’s social and personal interaction is not just about *Facebook*. There is a growing number and wide range of social and commercial networks attracting different demographic groups and addressing a range of increasingly specific market demands for social and personal, individual interaction and both tangible and intangible goods.

Internet sellers are direct sellers. Some sell major brand name products, so do our members. The evolution of retail is an evolution that has moved from a travelling peddler who knows their product and their customers and visits them in their home or place of work to an electronic peddler doing the same thing but utilising far more efficient and cost effective means of marketing and distribution.

Our members have been refining and promoting the mantra of product knowledge, trust and service for fifty years. During that time we have had to struggle against unjustified Government intervention and ignorance in the market at both the State and Federal levels.

The new Australian Consumer Law (ACL) is an example where the governments of Australia have, admirably, banded together to create a federal environment on national consumer issues but have not fully understood the market dynamics and consumer issues in direct selling.

Direct sellers are the vanguard of New Age global marketing. They must be considered as a part of government policy concerning the market place for consumers.

RESPONSES TO PARTICULAR ISSUES RAISED IN THE ISSUES PAPER

Page 3, Paragraphs 1 and 2, states inter alia

“Division G of the Australian Bureau of Statistics (ABS) Australian and New Zealand Standard Industrial Classification (ANZSIC)... Defines a retail business

The fifth industry subdivision is “non-store retailing and retail commission-based buying and/or selling...”

There has been no accurate Government measure of any of the characteristics or metrics of the Direct Selling industry which is a dynamic and rapidly growing aspect of the retail market. This includes revenues, number of people in its sales force and number of people employed in direct selling companies. For the past twenty years, the absence of any relevant statistics has created difficulties for both the industry and State and Federal Governments.

As previously mentioned, the size of the ISP group has varied over time from between 400,000 to 600,000 people. These are people who are contracted to our members in distributing their products. This substantial fluctuation is a consequence of the condition of the Australian economy and the amount of part-time work for which fixed wages and hours are available, particularly for women. These numbers have been derived from a number of studies for the DSAA since 1992.

The absence of any specific ABS measurement posed a problem for the Federal Government prior to the implementation of the Goods and Services Tax in 2000. At various times the industry has been involved in substantial interactions with the Australian Taxation Office because there has been insufficient publicly available data regarding relevant metrics and characteristics of the industry.

Given the size of the Direct Selling industry and its sales force, the DSAA believes the Federal Government should ask the Australian Bureau of Statistics to undertake a project in conjunction with the Association designed to provide some clarity and precision regarding industry statistics. This project would undoubtedly clarify many of the misconceptions that have resulted in substantial and onerous one-off projects by the industry to satisfy individual requirements of State and Federal Governments. Internet sales are an obvious example of direct selling. A majority of Internet sales are made by locally based companies and individuals. From our research, we consider that Internet sales are now a major retail channel of the Direct Selling industry.

Page 14: Change in the next twenty years

How is the structure of the industry likely to change in the next twenty years? What factors are likely to drive changes? Which retail models are likely to survive and which are likely to struggle?

Further improvement in security of financial transactions will increase consumer confidence in buying products and services on the Internet. Banks already facilitate limits to customers' financial exposure and *PayPal* provides a filter to enable a \$500 limit.

We believe that the retail sector will recover from its present slump. However, there will be an increase in the size and number of major shopping centres and, during the period, high street shopping and strip shops will reduce significantly. The reasons for these changes will be the growth of Internet retailing and further concentration of the retail industry.

Page 17: How significant is the impact of online trading on domestic retail businesses?

What factors explain Australian consumers' willingness or reluctance to purchase online from overseas suppliers? What is the significance of these factors? Will the Australian online share grow at the rates of the USA and Europe? What retail sectors are likely to be impacted the most? What new business models may be created by online trading?

The questions posed here would, if answered in detail, fill a very large book. DSAA will attempt to provide some responses of a general nature but would like to provide more information in responses to the Commission's draft Report.

At the outset it is noted that our members are not, like many mainstream retailers, at the planning stage of an Internet presence. A significant proportion of their sales are facilitated through the Internet (Monash Study 2010). We have previously expressed the secret of this success. It is product knowledge, consumer trust and after sales service. The overriding driver is personal relationships.

Retail globalisation is an issue for direct selling. Retailers require a local presence to resolve issues and to recruit either staff or ISPs. The direct selling model will continue to evolve through technology improvements. It will increasingly cater to rural and regional areas. Most direct selling organisations (approximately 60%) cannot take their products to market through the major retailers or the bricks and mortar investment necessary in a large shopping centre.

There is also a shift in the present transfer of knowledge and skills in the major retail sector. Sales people are not provided with individual development opportunities in the major retail chains.

The large retailers have enjoyed a great period of growth and prosperity. They have become monolithic and their fixed costs are a substantial drag on their profitability and competitiveness. The general public has no idea of the size of unit profit margins for many of the products sold. The Internet is starting to expose those margins to the discipline of market competition.

Counterfeiting can be a cross border issue. The fundamental future problems for imported goods purchased via the Internet will be ensuring that goods meet Australian Standards, can be serviced or repaired, are not pirated or stolen, are not past their use

by date, cannot be seized by Customs because they breach copyright or trade mark legislation and are not spoilt or defective. In 2010 the Australian Communications and Media Authority (ACMA) noted that “One of the reasons for consumers preferring to purchase from Australian sites was a lack of trust in overseas websites.”

This is where local Internet purchases from sellers who are domiciled and conduct business in Australia, and are bound for the most part by progressive consumer protection laws are able to meet the future nature of consumer needs. The global Internet can be a source of *caveat emptor*. The solution is in personal knowledge of the seller, trust and service. As major retailers have grown, their sales people on the floor have either not refreshed the original product knowledge and training they once received as new products become available, or have not received training at all. The latter may occur because sales incentives move from a product and price emphasis to “price leaders”, strategic shelf placement and interest-free financing for consumer durables.

Isolation and market size are the major reasons why Australia will not reach the Internet sales levels of Europe and the USA. Internet’s percentage of Australian retail sales will still increase substantially. Small consumer products, cosmetics, sporting goods, electronic goods and almost anything without a high retail ticket price will be bought on the Internet. Freight costs for large items or capital equipment will not be offset. The obvious major new retail model will be online selling by major retailers with, possibly, viewing and sales pick up centres.

Consumer Protection & Regulatory Impacts

DSAA’s experience is that Government insistence of business impacts being properly considered in developing and expressing regulatory policy at transactional and product levels is sometimes unrealised.

The unsolicited selling provisions of the recently enacted Australian Consumer Law are instructive for transactional regulation. In terms of the Commission’s Issues Paper these provisions, in contrast with the principles based approach elsewhere in the ACL are:

- (a) Poorly designed and impose unnecessary cost in attempting to achieve underlying consumer protection objectives;
- (b) Replicate generic provisions of the ACL;
- (c) Unduly prescriptive, uncertain, biased and ill targeted; and
- (d) Restrict competition and consumer choice, and are
- (e) Non-compliant with regulatory development standards.

Among others these criticisms detract from an otherwise outstanding achievement by Australian governments in delivering on a recommendation from an earlier Commission inquiry for a single Australian consumer law with benefits to consumers and business alike. DSAA believes the unsatisfactory outcome of unsolicited selling regulation lies in the grossly unreasonable timetable for the introduction of the new law. This has meant the application of so called “best practice” in the form of highly prescriptive, dated and efficacy questionable regulation to “unsolicited” sales in effectively all non-store environments. Some understanding of these issues may be gained from the Association’s submission to the Senate Economics Legislation

Committee Inquiry into the ACL, and the attached case study showing the effect of these provisions on three retail channels. A Senate Inquiry recommendation for discussion about the existing monetary exemption threshold for direct selling is unanswered.

At a product level the regulation of complementary healthcare products is also instructive. More than a third of DSAA members are active in this growing and direct selling conducive market. The regulatory environment has become unnecessarily complex and costly for members trying to improve community health outcomes.

The entire cost of regulating this \$3.5 billion market is borne by industry. The national regulator operates on a 100% cost recovery basis. This contrasts with the industry's contribution of approximately \$350 million annually in GST receipts. Moreover compliance costs are increasingly burdening members without any benefit/cost analysis or obvious betterment in consumer health and safety. These costs raise competition issues and deny consumers access to a full range of cost effective, low-risk health care products. One member reports that compliance costs have now reached thirteen percent of sales, a 360% increase in just eight years with no discernible change in product or consumer benefit.

Against this level of domestic regulation consumers are able to import substances for personal use under the Personal Import Scheme. Online shopping allows the purchase of complementary healthcare products ineligible for supply within Australia with obvious competitive issues for domestic suppliers and potential health and safety issues for Australian consumers

DSAA MEMBERS

4 Life Research Pty Ltd
A Better Chance Pty Ltd
ACN Pacific Pty Ltd
AGEL Australia Pty Ltd
Amway of Australia
Arbonne Australia Pty Ltd
Atise Pty Ltd
Avon Products Pty Ltd
Become International Pty Ltd
Bessemer Sales
Bevilles Party Plan Pty Ltd
Creative Memories Australia Pty Ltd
Digital Crown Holdings Pte Ltd
Do You Have a Card
Dominant Homecare Products
Emma Page Pty Ltd
Enjo Pty Ltd
Envy Jewellery Pty Ltd
Essential Additions
Esteem Jewellery
Fifth Avenue Collection Pty Ltd
Foodie Parties
FreeLife International Australia Pty Ltd
Furlong Wines
GNLD International Pty Ltd
Guthy-Renker Australia Pty Ltd
Herbalife Australasia Pty Ltd
Homecare Direct Shopping Pty Ltd
Intimo Lingerie
Isagenix (Asia/Pacific) Australia Pty Ltd
Just One Village Pty Ltd
Kampai Pty Ltd
Kaszazz Pty Ltd
Le Reve Pty Ltd
Life Force Australasia Pty Ltd
Lorraine Lea Linen Pty Ltd
Mannatech Australia (Mannatech Swiss International)
Mary Kay Cosmetics Pty Ltd
Nature's Sunshine Products of Australia Pty Ltd
New Image International
Neways International (Australia) Pty Ltd
Niagara Therapy Mfg. Aust P/L (CT Healthcare Pty Ltd

Nikken Wellness Pty Ltd
Norwex Australia Pty Ltd
NSA (Australia) Pty Ltd
Nu Skin Australia Inc.
Nutrimetics Australia Pty Ltd
Oasis Homewares
PartyLite Pty Ltd
Pash Australia Pty Ltd
Penny Miller Pty Ltd
Phoenix Trading (Aust) Pty Ltd
Postie Fashions Pty Ltd
Pro-Ma Systems (Aust) Pty Ltd
Reliv Australia Pty Ltd
SPTM International Pty Ltd
Stampin' Up! Australia Pty Ltd
Sunrider International Australia
Swipe (Australia) Pty Ltd
Synergy WorldWide Australia Pty Ltd
Tahitian Noni International
The Body Shop At Home
The Chef's Toolbox Pty Ltd
The Commonwealth Key & Property Register
The Learning Ladder Pty Ltd
Thermomix in Australia
Tupperware Australia Pty Ltd
UnderCoverWear Ltd
USANA Australia Pty Ltd
Wicked Wix
Your Inspiration at Home Pty Ltd

CASE STUDY

Sarah is an independent contractor selling the products of a renowned company in the direct sales channel. It supplements her family income. The company's products are also sold in stores and online.

On a Sunday Sarah uses a social tennis gathering to promote the company's products to a number of persons, individually and in small groups. Jane decides to purchase \$110 worth of products. She knows Sarah, her business, and considers her a friend. Six months earlier she purchased products in similar circumstances. Jane makes a deposit with Sarah's assurance the products would be sent to her the next day.

In this transaction the company is a wholesaler; although it handles delivery and other logistics it is Sarah who is selling the products to Jane.

Under the Australian Consumer Law

- Sarah can't promote the products on a Sunday.
- If she could and Jane wanted to purchase the products, Sarah couldn't start her promotion of the products before she
 - tells Jane she wants to sell her products
 - advises Jane that if she requests, Sarah must immediately leave
 - tells Jane her name and address
- If Jane asks Sarah to leave, she must leave and not approach Jane about the products for at least 30 days, but she can contact Jane about another company's products during that period
- Jane can cancel her purchase within 10 clear business days.
- Jane must be informed of this right, how to cancel the agreement and told that products can't be supplied nor payment accepted for 10 clear business days, and she must also be given this information in writing. This information has to be
 - "attached" to the purchase agreement
 - transparent
 - in the most prominent text except for Sarah's name or logo
- Jane can't be supplied the products or pay for them for at least ten clear business days
- Sarah and Jane must each sign the purchase agreement and Jane immediately given a copy, and both also have to sign any alteration
- Sarah must be sure the purchase agreement
 - conspicuously, prominently and transparently sets out her name, her ABN or ACN, business (her residential) address, email address and fax number
 - sets out the "full terms" of the agreement
 - and any postal or delivery charges

- on its front page conspicuously and prominently informs Jane of her right to cancel (the agreement), and includes this text:

Important Notice to Consumer

You have a right to cancel this agreement within 10 business days from and including the day after you signed or received this agreement.

Details about your additional rights to cancel this agreement are set out in the information attached to this agreement.

- On its front page is signed by Jane and dated
- Sarah must also ensure Jane gets a notice
 - that she can use to cancel the agreement
 - that is in a form approved by the Minister
- If Jane decides to cancel the agreement she doesn't have to use the approved notice and can otherwise cancel the agreement in writing or orally.

Observations

If Jane had purchased similar products from Sarah within three months before the tennis gathering the transaction would be unregulated.

If the products cost \$100 or less the transaction would be unregulated.

If the sale circumstances could be construed as a party plan event the transaction would be unregulated.

Sarah is exposed to \$10,000 penalties (possibly \$50,000) for individual breaches of these requirements.

Breach of requirements could extend cooling off rights to 3 or 6 months.

If Jane purchased the Company's products

Online – she would have received an e-receipt and the goods would have been despatched the following day;

In a store – she would have immediately received the products and a cash register generated receipt.