



**The Institute of
Chartered Accountants
in Australia**

2 June 2011

Mr Philip Weickhardt
Presiding Commissioner
Retail Industry Enquiry
Productivity Commission
GPO Box 1428
Canberra City ACT 2601

By email: retail@pc.gov.au

Dear Mr Weickhardt

Submission on Performance of Australian Retail Industry Issues paper

The Institute of Chartered Accountants in Australia (the Institute) welcomes the opportunity to make a submission to the Productivity Commission (the Commission) on its Issues Paper, March 2011 (the Issues paper) in relation to the Economic Structure and Performance of the Australian Retail Industry.

Specifically, our submission addresses the matters raised in section 4 of the Issues paper which concerns the appropriateness of current arrangements relating to indirect taxes and duty on imported goods.

The Institute is the professional body representing Chartered Accountants in Australia. Our reach extends to more than 67,000 of today's and tomorrow's business leaders, representing more than 55,000 Chartered Accountants and 12,000 of Australia's best accounting graduates currently enrolled in our world-class Chartered Accountants postgraduate program.

Our members work in diverse roles across commerce and industry, academia, government and public practice throughout Australia and in 109 countries around the world.

This submission focuses on providing high-level comments and observations on the revenue and tax base aspects of the low value importation threshold, rather than providing empirical evidence or other data on the way in which the Australian retail businesses are impacted by the threshold.

Background

The Commission has been asked to undertake an inquiry into the implications of globalisation for the retail industry and the appropriateness of current policy settings in this environment. Relevant to this submission, the Commission is requested to examine:

“the sustainability and appropriateness of the current indirect tax arrangements in this environment, including the impact on Commonwealth and state and territory budgets, and the extent to which technology could reduce the administrative costs of collecting indirect taxes and duty on imported goods.”

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More broadly, the Commission is charged with reviewing the current structure, performance and efficiency of the retail sector, and with identifying any impediments to its contribution to the Australian economy.

This involves consideration of a variety of broader issues such as drivers of structural change in the retail industry, including growing household and business access to the digital economy. Factors contributing to increases in online purchasing by Australian consumers, and the role of online purchasing in providing consumers with greater choice, access and convenience are also relevant to the inquiry.

Key comments

General comments

The Institute is in favour of the government's decision to adopt the recommendation of the Board of Taxation not to lift or reduce the low value threshold on imported goods for the time being.

We support the principle that the Australian retail sector should seek to grow in a way that is globally competitive on prices and provides consumers with the choice and sophisticated product offerings they deserve. We do not see that a short-term reaction is required at this point in response to recent views that the low value threshold is causing or resulting in slow retail sales by Australian retailers, and that this is being exacerbated by the growth in internet shopping.

Our sense of the issue at present is consistent with the government's rationale for the decision, as revealed in Treasury's Executive Minutes,¹ that the increase in online purchases by Australian consumers is most likely due to a combination of other factors, driven in particular by the strengthening Australian dollar over recent years, better access to and familiarity with the internet more generally, and greater confidence in its security, reliability and convenience.

The Treasury Minutes also make another important observation that "the fact that a high exchange rate shifts spending from domestic to foreign sources, and increases competitive pressures on businesses that face foreign competition, is an integral part of its role in dampening inflationary pressures in support of monetary policy".² Government intervention to protect domestic businesses from these effects may transfer more of the burden to other businesses in the economy.

On the basis that the increase in e-commerce appears to be due to other prevailing market factors, and is not driven by the lack of GST and customs duty on imported goods, we believe that reducing or removing the low value import threshold is an unwarranted policy response in the circumstances. In fact, it appears that the existing policy is apt to encourage competition in the current environment which is good for consumers. In this respect, Treasury's Minutes indicate that Australian retailers have also had the benefit of the strong Australian dollar for their imports, but may not have reduced their retail prices to pass on the exchange rate savings to consumers. The Issues paper also notes that Australian retailers have invested relatively little in e-commerce business models to date, suggesting that there may be market share opportunities to be gained by establishing a greater presence in the online market.

Going forward, given the forecast growth in online trading, we believe it will be prudent and necessary however for Treasury to monitor and reassess in the medium to longer-term whether all relevant policy parameters remain appropriate since the issue of growth in e-commerce is one much bigger than indirect taxes, having the potential to bear upon broader economic issues such as Gross Domestic Product (GDP), and international trade and commerce, and the income tax base.

¹ Issued on 20 May 2011 under a Freedom of Information (FOI) request. The documents were prepared by Treasury to analyse the effect of the low value import threshold on the retail industry.

² Treasury Executive Minute, *The Low Value Import Threshold: Options*, 2 November 2010, released under FOI



As a fluid variable, it will be a matter of striking the right balance on an ongoing basis between revenue base, revenue collection and administrative efficiency.

Specific issues

Our high-level comments and observations in response to selected focus questions are set out below:

1. Potential impact on integrity of the tax system and revenue of sustained growth in low value imports

The Issues paper states that the GST revenue foregone on low value imports is an estimated \$460 million in 2010/11. Australia's total taxation revenue was \$332.6 billion (or \$332,602 million) in 2009/10,³ of which GST revenue was approximately \$45 billion.⁴ Therefore, the GST foregone on overseas internet purchases relative to total taxation revenue currently represents a negligible 0.14%, and around 1% of GST revenue.

The data relating to online sales also indicates, in our view, that the issue is not yet of a magnitude that would warrant a policy response such as reducing the low value threshold for imported goods or other legislative amendment to capture these transactions in the tax base. Online sales currently account for only 3% of all retail sales in Australia. Of those online sales, only around 20% to 50% are from overseas vendors.⁵

We note that Treasury has done a 'rough estimate' (low reliability) which indicates that foregone GST revenue on untaxed foreign imports is expected to rise to \$610 million by 2013/14. This reflects the expected increase in the number of low value parcels as online shopping becomes more prevalent.⁶ Even at this level, the Institute is not convinced that e-commerce presents a material risk to the integrity of the tax system.

Having said this, we recommend that the government monitor the trend in internet purchases closely in the medium term to understand the evolving structure of the retail sector, with a view to assessing the appropriateness of all relevant policy parameters over the medium to longer-term. Indirect taxes are only one part of a much broader issue for the Australian economy around the future implications of e-commerce. The current trial being undertaken by Customs should provide some more specific and reliable data on the trends which can inform Treasury and the government on any policy responses that may be appropriate in the longer-term.

2. How might continued growth of overseas online shopping affect existing border control and cost recovery arrangements?

Continued growth of overseas online shopping will result in an increased volume of small parcels that come through the clearance process. We expect that these parcels will require screening to establish their estimated value to ensure that it is below the low value threshold. The additional parcels may require incremental increases in personnel to conduct the screening process, however it may be more cost effective if existing systems can be optimised or new technologies can be planned for and adopted in a timely manner to manage the forecast growth in small parcel volume over time.

³ Australian Bureau of Statistics: 5506.0 - Taxation Revenue, Australia, 2009-10

⁴ Australian Taxation Office: Taxation statistics 2008-09, *A summary of tax returns for the 2008-09 income year and other reported tax information for the 2009-10 financial year*

⁵ Treasury paper, *Low value import threshold – talking points*, released under FOI

⁶ Productivity Commission, Issues paper, at p. 24



3. Overseas experience – how do other countries strike a balance? Are their thresholds being effectively enforced?

Observations from our members regarding overseas experience suggests that in countries where there is a lower low value threshold compared with Australia, such as Canada (\$20) or New Zealand (NZ) (\$400) it is more difficult to balance compliance with the threshold and administrative efficiency. In NZ, we understand from informal feedback from our members that:

- screening by Customs tends to be done on a sampling basis
- in practice, the low value threshold seems to be monitored by freight forwarders who clear the goods for Customs (including parcels)
- enforcement seems to be patchy and on an exception basis – unless it is an item that stands out (e.g. due to its size), many higher value items may be passing through the mail without GST.

NZ Customs has recently reviewed NZ's de minimis level for imported goods, with the retail industry submitting that no de minimis is required, while importers and the airfreight sector asserted that the costs of revenue collection support having a de minimis.⁷

NZ Customs concluded that “[a] lower de minimis would not produce worthwhile net gains in Crown revenue and would increase compliance costs for importers.”⁸ However it was noted that “[l]onger term work with Inland Revenue will take place to explore other methods of collecting GST revenue on imported goods.”⁹

NZ is undertaking work over the next one to two years on the Joint Border Management System which will impact revenue collection processes including the administration of the de minimis (e.g. revised data standards for reporting low value express airfreight), and a further review of the de minimis level will be undertaken at that point once the flow on impacts on revenue collection processes and costs become apparent.¹⁰

4. Would a lower or higher threshold be more appropriate? How might people receiving gifts from overseas be affected?

For the reasons discussed in our general comments above, the Institute does not consider that it is appropriate to lower the threshold, nor is there any apparent case for lifting the threshold at this point in time.

Another reason that we support maintaining the threshold as it stands is that lowering the threshold to any extent may provide greater incentive for importers to artificially split consignments into several parcels, each with a value lower than the threshold, to seek to ensure the goods are able to pass Customs clearance without being stopped and withheld until GST and customs duty is paid. This would only add to the already growing volume of parcels coming through Customs, which in turn would augment the amount of the screening and administrative work required to be done by Customs.

A further concern in lowering the threshold (in a meaningful way as sought by the retailers) is that it would be more likely to create practical problems for the logistics of gifts received by Australians from family and friends overseas. We consider that a \$1,000 limit is a reasonable threshold to allow gifts to be given without causing undue inconvenience or hardship for the gift recipient. If the threshold was reduced in a material way, we believe that many gifts may be need to be stopped and subjected to GST, customs duty and an administrative fee, at the expense of the

⁷ New Zealand Customs (2011), *Review of De Minimis: Report and Summary of Submissions*, OR 11/022, at p. 1

⁸ New Zealand Customs, OR 11/022, at p. 1

⁹ New Zealand Customs, OR 11/022, at p. 1

¹⁰ New Zealand Customs, OR 11/022, at p.p. 2-3



recipient, who did not actively procure the goods, and in most cases will not have even been aware that the goods were coming into Australia. Many gift recipients who are requested to pay the tax may simply choose to refuse the goods, which would then need to be destroyed at the expense of Australian Customs.

On balance, therefore, we do not believe that any benefits to revenue would justify the likely additional administrative costs that would be incurred as a result of a materially lower threshold.

5. Would there be any merit in having a higher threshold for duty collection and a lower threshold for GST?

As noted above, the Institute is of the view that the \$1,000 low value imports threshold is reasonable and we believe that a connection between the low value threshold and the customs duty rules is desirable. We do not favour the introduction of layers of complexity such as different thresholds for different indirect taxes.

6. Should imported intangible goods be brought into the Australian tax base? If so, how could this be accomplished?

Similar to imported goods, the Institute recommends that the Government continue to assess and monitor the trends in online overseas purchases to determine if and when the level of imported intangibles becomes material to the Australian tax base.

As a taxing mechanism for imported intangibles, we do not favour the application of a compulsory reverse charge to consumers, with or without a threshold, unless 'enforceability' issues can be addressed. It is important that the law be able to be applied with reasonable certainty and administered with consistency and efficiency. At present, we consider that such a 'tax on honesty' would be difficult to administer and enforce and may necessarily be applied only on an ad hoc basis.

In jurisdictions where there is a self-assessment obligation imposed on individuals, such as in the US where purchasers may have an obligation to self-report use tax, we understand that compliance is extremely low for individuals. Recipient businesses have slightly better compliance as many are required to be registered and are frequently audited. We understand there are two main pushes to increase the compliance in this area – both would result in the sellers becoming responsible for the tax obligation.

In terms of the NZ experience, we understand that private consumers who are not registered for a self-employed business are unlikely to be required to remit GST on overseas purchases of intangibles. This is because to breach the threshold of the compulsory reverse charge, a gamer/internet downloader would need to be accessing a significant amount of internet services before tax would need to be collected on the purchases, i.e. NZ\$60,000.

The Institute's preferred approach to capture online supplies, as we recommended to the Board of Taxation, would be to include e-commerce in Division 85 of the GST Act and leave it to the Commissioner to determine if and when the power is applied, and to what extent. While such a tax would itself also be a 'tax on honesty', it is the Institute's view that a tax on the honesty of large multi-national e-commerce suppliers is likely to be more fairly and effectively administered than a reverse charge on consumers. It would also be in keeping with the OECD Ottawa Framework recommendations and the EC VAT Directive. It is noted, however, the ATO has not to date made any serious attempt to apply the Division 85 mechanism to telecommunications supplies.



If you have any queries regarding the contents of this submission, or would like to discuss any aspect in further detail, please contact Donna Bagnall in the first instance or me.

Yours sincerely

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The Institute of Chartered Accountants in Australia

