



Fair Imports Alliance

Submission to the Productivity Commission Inquiry:

The Economic Structure and Performance of the Australian Retail Industry



About the Fair Imports Alliance

The Fair Imports Alliance (FIA) is a coalition of retail and wholesale industry associations providing a united voice on issues relating to the low value importation threshold and its effects on retail trade in Australia. The FIA was formed to campaign for a fair and equitable regulatory framework and the group strongly believes that the low value importation threshold and its associated compliance and enforcement regimes require further examination and reform.

The FIA consists of: Australian Retailers Association (Secretariat), Australian Sporting Goods Association (Secretariat), Australian Booksellers Association, Australian Fishing Trade Association, Australian Music Association, Australian Toy Association, Bicycle Industries Australia, Photo Marketing Association, and the Retail Cycle Traders Association.

Whilst individual member associations of the Fair Imports Alliance may provide submissions to the Commission about a broad range of issues, this submission will primarily focus on the need for reform to the low value importation threshold.

Introduction

The retail sector in Australia is currently undergoing massive change as a direct result of globalisation and its effects on domestic retail trade. Specifically, consumer acceptance of global online shopping has meant that Australian retailers are increasingly competing with overseas retailers and, as the Australian dollar strengthens and consumer confidence in shopping online grows, Australian retailers are exposed to significant pressure.

Of course, the globalisation of shopping is a logical corollary of market forces at play in the 21st century economy and it is something which is both inevitable and unstoppable particularly with the growth of the Internet and technology in general. Many Australian retailers are embracing global trading opportunities; however, they are also facing several obstacles at both a macro and micro level, and it is these which need to be explored further, in order to understand how the retail sector will fare in the future. Indeed, it is a primary aim of this submission to outline the challenges faced by Australian retailers in the current and global environment.

In addition, this submission will also explore a de facto set of impediments which exist alongside the globalisation of shopping, and which are principally felt by small and medium retailers: the misapplication of certain aspects of government taxation policy. The differentially applied rate of taxation regulation upon all retail businesses trading domestically as against online, pack-and-send, offshore businesses, exacerbates an effect best categorised as an impediment to trade. At the most basic level, overseas retailers automatically have a 15-20% advantage over Australian retailers selling the same product, as a result of the Australian Government's policy to waive indirect tax applications and customs duty at the import stage for packages under the \$1,000 low value threshold. This, coupled with the increasing propensity for Australian consumers to shop overseas, is greatly impacting on the ability of Australian retailers to drive their businesses forward within a competition neutral market-place.

Further to this, there is a measurable loss to the economy of taxation revenue as a result of the volume of goods imported both GST and duty free when under the \$1,000 low value threshold. This lost revenue has implications for the States and their respective economic and social policy goals, and it is an issue which will be further explored in this submission.

The broader social effects of a globalised shopping world will also be examined within the context of the Australian economy. One of these is the very real concern that retail jobs are at risk if the domestic taxation environment continues to penalise domestically-based retailers and acts as a catalyst for retail trade to shift online and overseas. This is something which needs serious consideration given its impacts on both the economy and the social welfare of all Australians.

Indeed, the traditional retail business model is changing and it is a key aim of this submission to highlight the importance of embracing new business models within an equitable environment which allows Australian retailers and e-tailers to compete with offshore online sites. How this can be achieved is something which will be discussed later in this submission.

Finally, this submission will look at other policy and regulatory issues inherent in the globalised shopping economy. Matters such as consumer risk, counterfeit products and

warranty assurances are all brought into question when consumers shop globally, and these are elements which need clarification.

In summary, it is clear that the retail market, and indeed all sections of the economy, is undergoing enormous change due principally to the effects of globalisation. In Australia, the Government's intentions for a National Broadband Network (NBN) will unleash enormous levels of innovation and productivity, as well as bring about certain challenges for Australian businesses. The rise of online shopping in a globalised world stands to greatly benefit both consumers and businesses; however, regulation in this space must ensure that it does not, in turn, detrimentally affect the businesses and consumers which it purports to support.

1. The current structure, performance and efficiency of the retail sector and impediments to its contribution to the Australian economy.

The Australian retail sector (both bricks and mortar retailers and domestic online e-tailers) contributes to the strength of the Australian economy as well as providing quality goods, services and consumer safeguards to Australians. Particularly across rural and regional Australia, retailers add significant value within their local economies, through direct employment, community support and providing a local retail service in communities that may not necessarily have access to a variety of stores. However, as this submission demonstrates, the performance, structure and efficiency of the Australian retail sector is currently being challenged and its ability to add to the economy may be compromised as a result of domestic taxation policy, globalisation, competition which is skewed to one side, and other market forces.

Performance

Throughout the 2010-11 period, the \$240 billion retail sector in Australia demonstrated limited growth across all categories. According to the Australian Bureau of Statistics (ABS), retail has grown by 2.5% as compared to the same time in 2010¹. While the retail sector in Australia is, at a macro level, not symptomatic of a failing market, this growth is below the current rate of inflation, and furthermore, does not accurately depict the struggles felt across all non-food retail categories during 2010, and in particular, the Christmas period.

Retailers faced a tough period in December 2010 with many traders reporting a decline in sales as a result of intense competition². Sales did, however, pick up in January but growth in these areas was only 1.8% higher than January 2010 demonstrating continued poor trading conditions. Additionally, there were several retail categories which posted declining growth in January 2011 when compared to the same time in 2010: department store sales declined by 4.1%, clothing and footwear saw a decline of 3.3%, and household goods were sitting at 1.9% less than the previous year³. This decline in growth was felt particularly in small and medium retailers who generally have smaller profit margins and greater risk factors.

The Southern Cross Equities report into retail⁴ identifies several reasons for the downturn in retail spending, and general retail performance, of the previous months, including:

- Unseasonal weather patterns particularly on the East Coast have driven consumers away from seasonal trends in clothing and also affected spend in food and beverage categories.
- Rising interest rates have placed strain on consumers who are restricting their spending on non-essential consumer goods.
- The strong Australian dollar has driven consumers to shop online with overseas e-tailers rather than with local retailers and domestic e-tailers. In addition, the strong

¹ Australian Bureau of Statistics from Australian Retailers Association, 'Submission to Fair Work Australia', 18th March 2011.

² Southern Cross Equities, 'Retail: Where did Santa Shop?', 24th January 2011.

³ Australian Retailers Association, 'Submission to Fair Work Australia', 18th March 2011.

⁴ Southern Cross Equities, 'Retail: Where did Santa Shop?', 24th January 2011.

Australian dollar has meant a decrease in the number of tourists visiting Australia with an increasing number of Australians choosing to travel overseas.

- The rising cost of living has seen an increase in essential household expenses, which have overtaken wages growth and, as a result, consumers are curbing their discretionary spending. Indeed, the cuts to family tax benefits in the recent Federal Budget are likely to continue this trend of low discretionary spending. This is another example of an unintended consequence of Government policy negatively impacting on domestic retailers.

All of these factors are continuing to impact on the current performance of the retail sector in Australia with recent ABS figures showing that there was a 0.5% drop in trading across all retail categories in March 2011 as compared to March 2010⁵. This decline in spending is undoubtedly affecting all retailers, from large department stores to medium, small and micro businesses. In recent months, SMEs have been hit the hardest. Analysis of data sourced from the parliamentary library suggests that prior to the 2010 election, small businesses employing up to four staff fell to approximately 497,000 down from nearly 529,000⁶.

Structure and impediments

The current structure of the retail industry as a whole can best be described as fragmented. Leaving aside the role of manufacturers, wholesalers and distributors, the Australian retail sector in terms of active traders comprises department stores, small and medium businesses, micro sellers, e-tailers, high-street stores, sellers at local markets, auction-site sellers, and so on. This fragmentation of the sector has been exacerbated by new technologies and innovative uses of the Internet which allow new retailers to enter into the market with ease (for example, with lower overheads and start-up costs) and with wider access to consumers. Now, more than ever, there is a proliferation of traders all looking for a share in the market, and for the consumer, this means a wider variety of places to shop, greater product choice, competitive prices and access to products without necessarily having to rely on high street or department stores.

Further to its already fragmented nature, the structure of the retail industry in Australia has expanded to include offshore sellers via the burgeoning use of the Internet. Australian consumers can shop overseas from the comfort of their homes, and Australian retailers of all sizes are forced to share the market with their overseas counterparts. Thus, competition for consumers is at an all-time high, and with a dispersal of consumer spend across all retailers (both domestic and offshore), the structure of the retail sector in Australia is understandably undergoing massive change. While the Internet provides exposure for Australian retailers to potential overseas consumers, it also hinders the ability of these same retailers to contribute to the Australian economy particularly if Australian consumers are being driven to online, offshore sellers. Along with the opportunity it brings, a globalised shopping economy is still felt by small and medium retail businesses in Australia as one of the very real impediments to domestic trade. This is not to say that Australian retailers are not in favour of online shopping; simply, that it is affecting the Australian retail sector in a significant way.

⁵ Australian Bureau of Statistics, Retail Trade, 5th May 2011.

⁶ Malcom Farr, News Limited, 'Australia Shuts Up Shop: the Effect the GFC has had on your Local Stores,' May 16th 2011.

In addition, as online shopping grows it is becoming more apparent that the Australian Government's application of taxes and duty at the importation stage is creating a significant disadvantage to Australian retailers as compared to their international counterparts. Simply, if an Australian retailer is selling the same product as an offshore seller, and the consumer chooses to shop offshore, why is it that the imported product does not attract GST or duties if it is under \$1,000? By waiving this tax and duty, the Government is preferencing international traders over Australian businesses and giving them a price discount advantage of 15-20%; that is, 10% GST and between 5-10% duties. This is extremely concerning to Australian retailers as they cannot compete on an equitable basis in an otherwise competitive market.

While retailers realise that the price differential will still exist between products sold in Australia and those sold overseas even with the removal of this GST-free threshold, they believe it will create a tax neutral setting; one where domestic retailers will be able to compete by providing exceptional customer service standards and in-store experiences. In short, the Government's taxation policy creates a profound impediment to Australian retailers' business models and thus affects their ongoing contribution to, and viability within, the economy.

Key points

1. The retail sector is experiencing limited growth across all categories, with the most recent ABS figures showing a decrease in retail trade, year-on-year.
2. Reasons for the downturn in retail spending include: unseasonal weather patterns, rising interest rates, the strong Australian dollar, and the rising cost of living.
3. The retail sector in Australia is fragmented with a variety of different traders.
4. A globalised shopping economy is now the norm with Australian retailers and e-tailers sharing the marketplace with their overseas counterparts.
5. The Government's taxation policy at the importation stage is creating a profound disadvantage to Australian retailers in terms of equitable competition with offshore sellers.

2. The drivers of structural change in the retail industry, including globalisation, increasing household and business access to the digital economy, cost structures of the domestic retail industry, employment structure, the exchange rate and structural change driven by the resources boom

Over many years, the retail sector has undergone significant structural changes caused by both domestic and global factors. From the diminishing level of high-street retail in favour of mall-shopping; to the rising value of the Australian dollar and the various, and sometimes contradictory, changes to employment frameworks, retail has been in a semi constant state of flux.

As already discussed in the previous section, the Australian marketplace sits within a globalised world which is constantly evolving, and where the maturation of distribution channels globally has further expanded market growth. The proliferation of both on and offshore e-tailers has driven an unprecedented level of competition for the consumer dollar. It is likely that online shopping will grow even more within Australia with the roll-out of the National Broadband Network (NBN).

The NBN and its take-up will provide a quantum shift in the way all facets of the economy are accessed by consumers. Indeed, even without the NBN, online shopping has skyrocketed over the past ten years with a study undertaken by the Department of Broadband, Communications and the Digital Economy showing that the percentage of individuals in Australia aged fourteen years and over who are buying and selling goods online has increased from 41 per cent in 2001 to 64 per cent in 2006⁷.

In addition, a recent study put together by Forrester Research and commissioned by PayPal has found that the Australian online sector alone was worth over \$24 billion in 2009 with growth predicted to reach over \$36.5 billion by 2013⁸. These figures demonstrate that retail is clearly moving into the online space, and traditional bricks and mortar businesses that do not already have an online presence will be impacted by the surge in online shopping.

Clearly, globalisation and Internet growth are major drivers of structural change in the retail industry and, as stipulated in the previous section, existing retailers in Australia must find ways to utilise this increased connectivity to the digital economy in addition to their existing service offerings. Indeed, the FIA strongly supports multi-channel selling strategies and believes that Australian retailers should embrace the opportunities that are made possible by the Internet.

Aside from globalisation being the principal driver of structural change in the retail sector, there are several other factors which are impacting on the way the retail industry functions currently. The present reliance of bricks and mortar domestic retailers upon securing tenancies within shopping centres poses a significant structural challenge to the ongoing viability of the sector. The oligopolistic nature of shopping centre ownership and a retail tenancy regime which is skewed in favour of these large-scale landlords presents an inherent disadvantage to Australian domestic bricks and mortar retailers in terms of equitable competition. In addition, the award harmonisation process and the rising cost of

⁷Department of Broadband, Communications and the Digital Economy, 'Australia's Digital Economy: Future Directions,' 2009.

⁸ Forrester Research and PayPal, 'The Business of Australian Online Retail', 2010.

labour required within this process does act as a disincentive to retailers in retaining their relatively low-skilled workforce in a time when trading conditions are still lagging.

Structural changes to the Australian retail sector are also being felt as a result of Australia's position in the supply chain as the proportion of the international market for imports into Australia is not significant. This often results in the orders of Australian retailers and wholesalers, particularly for specialist consumer goods being placed at the end of the queue by overseas manufacturer suppliers. Australia's access to the supply chain is often limited by the size and scale of our domestic retail industry and also results in increased wholesale prices imposed by suppliers in the country of manufacture which is an additional price point which needs to be factored in for the Australian consumer, compared to a product exported to a larger economy, such as the United States.

Australian retail is also being detrimentally impacted by natural disasters around the world. Most recently, Japan has experienced economic instability as a result of the earthquake and tsunami. Consequently, this has resulted in a price spike for consumer products manufactured there and this has had a pronounced effect on supply chain reliability with Australian retailers facing delays in obtaining products. Larger markets are able to secure products sooner than Australia leaving domestic consumers with no option but to source these particular products from offshore online sellers.

As a corollary to these issues, the Australian dollar has been rising steadily and is now exceeding parity with the U.S. dollar. This acts as a push factor to potential online consumers of domestic goods wanting to look to the U.S. market to source the same product. However, it is noted that over many years other comparable economies' currencies have retained a ratio of difference that has not caused this push factor (for example, the British pound). Although a high dollar strongly indicates that retailers may be able to import more goods from overseas at a better rate, the cost of doing business with manufacturing countries is on the rise. Therefore, the benefits to retailers are not as clear or simplistic as consumers may think.

Finally, the mineral boom and its associated high disposable income and low cost of living in labour centres in the resource states, has also impacted on the rise of online shopping, simply to the extent that these remote communities are unlikely to ever be serviced by certain sections of retail (such as electrical goods and consumables). While the retail sector as a whole certainly does benefit from these increasingly affluent cohorts within the market, it could be argued that although being driven to online domestic consumption by necessity, residents in these remote yet relatively affluent communities will likely expand their online shopping as their confidence grows to include offshore purchases; thus negatively impacting on Australian retailers.

Clearly, the retail sector in Australia is constantly faced with new obstacles which threaten to destabilise traditional retail business models. At the forefront of structural change for the retail sector is globalisation which, while it provides great opportunity, also fractures the industry into smaller segments, creating much greater competition both on a domestic and international scale. As a result, Australian retailers are having to rapidly re-define both what they offer their consumers and the ways in which they offer them, in order to remain competitive.

Key points

1. Globalisation and online shopping are the principal drivers of structural change in the retail sector in Australia. It is estimated that online shopping will grow to over \$36.5 billion by 2013.
2. Other drivers of structural change to the retail sector include: rising shipping and transport costs, complex retail tenancies and work cover issues, changing employment frameworks, supply chain issues, and the effect of natural disasters on Australian retail trade.
3. Australian retailers are having to radically re-define what they offer consumers and the manner in which they do so.

3. The broader issues which are contributing to an increase in online purchasing by Australian consumers and the role of online purchasing in providing consumers with greater choice, access and convenience

As the previous section demonstrated, in the last few years there has been a surge in online purchasing by Australian consumers, and it has been estimated that this will increase even further in the coming years. There are several reasons why consumers may be more attracted to online purchasing as an alternative to, or even in addition to, visiting bricks and mortar stores. These include greater choice, access, information, competitive prices and convenience. In addition, it is widely understood that economic issues may drive consumers online, particularly with living pressures becoming a greater issue for many Australians.

The rising cost of living has been a growing factor in Australia for several years and it is an issue which is affecting the Australian economy. Recent ABS statistics of the 2010-11 period reveal that the cost of living has risen well above wages growth, particularly in healthcare, housing and utility costs⁹. Understandably, the cost of living pressures have created a more austere consumer who has less money to spend on discretionary items and who is more likely to shop for 'bargains'. As a corollary, retail businesses have themselves matched the new frugality of consumers with trends such as heavy and constant discounting, which is now the norm rather than a twice yearly occurrence. This, in turn, has affected consumer perception of retail whereby consumers are no longer happy to pay full price for products when they know that discounts or more competitive offers can be found elsewhere. For consumers, this 'elsewhere' is most likely found on the Internet with its myriad of online shopping options.

Consumers can use the vast online resources available to them to research their purchase and choose the channel which best suits their needs. Online shopping also exposes consumers to a breadth of products which they may not be able to find in domestic bricks and mortar outlets. In addition to this, in a country such as Australia, online commerce provides a greater quality of life to individuals in rural and remote areas who may not necessarily have physical access to retail stores. This latter driver – convenience – has also been responsible for the uptake of online commerce by increasingly time-poor consumers.

While choice, access and convenience are the clear benefits of shopping online, the trade-offs for consumers are, of course, the inability to interact with the commodity before purchasing, obtain contextual information from informed staff, and readily re-engage with the retailer should they need post-purchase service or replacement. Interestingly, an Access Economics report points out that these downsides of purchasing online support the notion that 'many Australian households use the Internet as a research tool but still choose to make the final purchase in person'¹⁰.

Clearly there are both benefits and downsides to purchasing online and these will evolve and solidify as technology moves forward. The role of online purchasing, however, needs to be further clarified by the Government in order to inform consumers, and make them better aware, of the implications of their online purchasing decision. While price may be a major factor in a consumer's decision to purchase products offshore and online, it is important to inform them of the greater consequences of this. Namely, when a product is purchased from

⁹ Southern Cross Equities, 'Retail: Where did Santa Shop?' 2011.

¹⁰ Access Economics, 'Household E-commerce Activity and Trends in Australia,' 2010.

an offshore online site, it strips value from the Australian economy and puts added pressure on working Australians in the sector. On the other hand, if consumers purchase products from a domestic online seller, a contribution is made to the Australian economy.

It is clear that online purchasing has a role to play within the Australian retail sector – it provides consumers with greater convenience, access and choice of products. However, a clearer distinction needs to be made for consumers on the benefits of purchasing from domestic online e-tailers rather than from offshore online e-tailers where the products are essentially the same. Just as the Government supports locally made products and retailers, they should also promote Australian e-tailers and support them over their overseas counterparts.

Key points

1. Australian consumers are 'bargain hunters' and retail businesses are responding to this with more frequent discounting and sales.
2. The Internet provides a source of information for consumers
3. Online shopping gives time-poor consumers and those in remote or rural areas access to a wide variety of products when it is convenient for them.
4. There are certain downsides to online shopping including: physical interaction with products, knowledgeable staff and post-purchase service.
5. Consumers are often unaware that by shopping offshore, added pressure is placed on the Australian economy.

4. 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

As it stands, the current indirect tax arrangements are perceived to be unsustainable and inappropriate by members of the Fair Imports Alliance (FIA) who are making this submission. FIA members – which include Associations representing the toy, music, sporting goods, books, cycling, photographic, and fishing industries – have concerns relating to the administration of the low value importation threshold which is currently set at \$1,000. The FIA strongly believes that the indirect tax arrangements relating to this threshold are unintentionally disadvantaging the Australian retail industry and Government revenue collection. These two areas will be examined in more detail in the following sub-sections.

Lost Revenue

In Treasury's Tax Expenditure Statement in January 2011, it was found that online shoppers are costing the federal government approximately \$1.26 million per day through the purchase of tax free imports over the internet which, individually, are valued beneath the tax-free threshold of \$1000¹¹. The net effect of this legitimised form of tax avoidance will deprive \$460 million from government funds which, in turn, poses a real risk to Government service delivery in critical areas such as disaster reconstruction and the health and hospital reform, and a self-imposed imperative to return to surplus. Moreover, this loss in funds is projected to increase by Treasury and will be in excess of half a billion dollars lost revenue in the very short term.

Such a gaping hole in the Government's taxation regime is cause for grave concern as the total spending throughout the domestic economy is also made vulnerable through the drive to online offshore markets. Decreased spend results in a greater risk to government as it ultimately drives lower employment, lower incomes and, thus, further reduces spending in the domestic retail and e-tail marketplace. In addition, the Treasury figures do not take into account revenue loss from unpaid duties. This can account for 5-10% of the total import amount which represents a substantial amount of lost revenue to the Government in addition to acting as an incentive to consumers actively seeking offshore online retail outlets.

While Treasury has estimated the loss of revenue due to tax-free imports being at \$460 million per annum, Australian Customs has quoted a different figure. Customs' own figures demonstrate that imports made between July 2010 and March 2011 which were under the \$1,000 threshold totalled \$932,493,422. If this figure is correct, it suggests that the total loss of GST revenue to the Australian economy would be approximately \$93,249,342 as opposed to the \$460 million estimated by Treasury. Certainly, the Customs data only takes into account eight months of the year and also only includes air cargo (to the exclusion of other methods); however the disparity between the two figures is still quite substantial notwithstanding these vagaries. This disparity is extremely concerning to the FIA as it is presumed that this data dictates, to some extent, the dollar value of the low value importation threshold.

¹¹Commonwealth of Australia, 'Tax Expenditures Statement: 2010', January 2011.

Clearly, the low value importation threshold has been set at \$1,000 without clear justification or modelling by the Australian Government. This was confirmed in correspondence from the Minister for Home Affairs where he stated that Customs had not undertaken an analysis of the economic feasibility of the low value importation threshold at different levels. Moreover, the lack of empirical data on the relative merits of the policy is exacerbated by the fact that records around the total value of packages are not kept. This poor administration of the threshold, and Customs' lack of transparency regarding data, indicates to the FIA that there is little rationale behind setting the threshold at the value of \$1,000. Given that the low value importation threshold is a significant taxation policy, and indeed, one which is having a sizable effect on the retail industry currently, the Government needs to make transparent the reasons behind setting the low value importation threshold at \$1,000.

Disadvantage to the Australian retail and e-tail sector

The role of Government in an increasing free market environment should be to reduce regulations and barriers to trade. However, the impost of a low value importation threshold can be seen as a reverse form of protectionism disadvantaging Australian retailers and in turn advantaging offshore retailers and e-tailers selling direct to Australian consumers.

Indeed, there is a certain inequity which exists between Australian retailers/e-tailers and offshore online e-tailers, particularly those who sell the same product to a similar set of consumers. As stated earlier in this submission, when an Australian consumer purchases a product from an Australian retailer/e-tailer, they must pay GST of 10%; however, if they purchase the same product from an offshore seller, provided that the product is under \$1,000, the consumer can import this and avoid paying any added GST or duties, saving between 15-20% on the purchased item. Effectively, the offshore online seller has an immediate and distinct advantage over domestic retailers/e-tailers selling the same product simply because of a misapplication of Government's taxation policy, one which, while it benefits the consumer, has unintended consequences for Australian businesses.

While the FIA encourages healthy competition between all sellers regardless of whether they are based in Australia or overseas, this competition is taking place on an uneven playing field given the current indirect tax and customs regime which is ultimately gifting a 'tax break' to the foreign retailer. In order to remedy this situation and create equity between all sellers, taxation and duty neutrality should be a primary goal for government.

One way of addressing this issue is by removing the low value importation threshold which will create a tax neutral, level playing field for all sellers regardless of their location. In the context of competition, the Government's role should not necessarily be to act; rather, the situation would be better remedied if the Government simply 'got out of the way'. Retailing is a trade primarily dictated by free market forces and should, in the first instance, be left to flourish or flounder on its own terms without Government intervention. At the moment, the Government's policy on low value imports acts, in principle, as a 'reverse tariff' which penalises domestic retailers.

The unintended and negative consequences of the low value importation threshold on businesses is something which cannot be addressed by simply using technology to make the collection of tax more efficient. As this section has demonstrated, the threshold is having a far wider reach and effect on Australian businesses and thus a broader approach needs to

be taken. Indeed, the Government should have a view to creating equality and neutrality in the marketplace so that it can ensure a healthier budget and vibrant future for the retail sector to the benefit of Australian workers and consumers.

Other side effects of the low value importation threshold

Because of the advantage given to offshore online sellers through the low value importation threshold, Australian businesses are being squeezed at every corner to compete with foreign retailers. As more Australian consumers shop with offshore online e-tailers, a greater strain is placed on Australian businesses. With less consumers shopping in Australian stores, there is a decreased need for employees, causing a long-term problem which ultimately results in employment pressures for both the retail sector and the Australian Government. Employment is already a significant issue in Australia and the increase in offshore, online shopping is only compounding this issue.

Currently, the retail sector in Australia employs over 1.2 million people. Indeed, retail employment plays an important role in Australia, and according to Martin Feil, a prominent tax and industry policy consultant, 'services sector employment is supposed to be [Australia's] economic salvation now that manufacturing is meaningless'¹². However, given that many Australian retailers are losing business to offshore online e-tailers, will retail employment still continue to be as strong as it once was? This is an issue which FIA members foresee as growing given the recent drive to offshore online shopping.

The FIA believes that the Government needs to take a comprehensive analysis of retail employment given the globalisation of the retail sector and the associated issues of the low value importation threshold. While the FIA strongly supports online shopping and recognises the need to transition the Australia retail industry into an online economy, they also recognise the importance of retaining employment in the retail sector.

Key points

1. The Australia Government is losing a substantial amount of revenue due to tax-free imports.
2. Revenue loss estimated by Treasury is vastly different to the figures quoted by Australian Customs. This calls into question the rationale behind setting the low value importation threshold at \$1,000.
3. A foreign retailer immediately has a 15-20% advantage over Australian retailers and e-tailers selling the same product. If a consumer purchases the product in Australia, they must pay GST of 10%; if they import the product from overseas, and it is under \$1,000 there is no additional GST (10%) or duties (5-10%) to pay.
4. An uneven playing field exists because of the low value importation threshold and it is one which penalises domestic retailers and e-tailers.
5. Removal of the low value importation threshold will enable a tax neutral, level playing field.

¹² Martin Feil, Sydney Morning Herald, 'Retail is just the Thin End of the Online Trade Wedge,' April 8th, 2011.

5. Any other regulatory or policy issues which impact on structural change in the sector

The shift to online retail has certainly seen some consumer choice factors at play such as convenience, price, access, and ability to research products. In addition, an increasingly confident consumer has emerged, one who is fully immersed and well versed in the digital economy. However, along with the benefits of domestic and international online shopping options, there are certain risks for consumers. Chief amongst these concerns is compliance with Australian Standards and matters related to consumer rights and warranties which may be voided in some instances. Indeed, the following situations may occur:

- a. Warranty may be voided for certain products. There may be ambiguity surrounding warranty policies when purchasing items from offshore online sellers and there is also no guarantee that stated warranty policies will even be upheld, depending on where the item was purchased. Indeed, many of FIA's members reported that consumers who had purchased goods from offshore sellers were bringing them back to retail stores in order to place warranty claims. This became problematic as certain products only had international warranties which were not recognised in Australia.
- b. The quality of the goods is not assured and if a consumer purchases a product not made to the highest standards, this could result in personal health and safety risks.
- c. There is an increase in the probability of purchasing goods which are counterfeit. This is often the case where prices are too good to be true and the avenues for consumer redress are poor.

Ultimately, it could be argued that by shopping online, consumers themselves accept these risks; however, evidence suggests that this is becoming a real and growing issue for Australian retailers. As stipulated above, many Australian consumers are bringing products purchased offshore and online to Australian retail stores expecting warranty and statutory rights to be honoured. Most of the time, this is simply not feasible and Australian retailers are having to turn away these consumers which is having the effect of creating a negative experience for the consumer with the Australian retailer. This, in turn, acts as further incentive for consumers to transact online, just as for others it may be the 'shock' to drive them back to Australian stores. The trend, however, is that reputational credibility is being lost to the offshore online market.

As online shopping grows, there will inevitably be further structural changes to the Australian retail sector. A primary concern for many retailers is the notion that, for them, engaging online is a daunting process, one which is costly and unpredictable. This is particularly the case for small and medium retailers who, rather than seeing online as an opportunity to a broadened marketplace, feel very uncomfortable exploring something they perceive as a 'high-risk' venture.

Government could play a role in this through leveraging its investment in the NBN and assisting to develop digital economy strategies to provide the best ecosystem for Australian business growth, rather than simply funding broadband infrastructure. In doing so, the Government could realise the greatest return on the multi-billion dollar investment of the

NBN. In this vein, Government should also seek to engage with all levels of Australian industry to make clear how it envisages businesses transacting in the online world. If such a dialogue were opened up, it would be of mutual benefit to helping Australians realise the full potential of our ability to innovate and adapt by leading the drive toward an online economy without causing unnecessary and unintended disadvantages to the existing retail business model.

Key points

1. Consumers face certain risks when purchasing from offshore online sellers. There may be warranty issues, products which do not comply with Australian Standards and counterfeit items which may cause personal harm to the consumer.
2. A further issue is the notion that many Australian retailers may feel that transitioning their stores from a bricks-and-mortar outlet to an online store is a daunting and costly process. Government could play a role in providing strategies for retailers to engage with the digital economy.

Additional Issues related to the Inquiry Process

The Fair Imports Alliance was formed in late 2010 to crystallise the issues faced by smaller scale Australian domestic retailers. At all times, the FIA has attempted to positively and proactively engage with government to identify and address key challenges facing the retail market in an increasingly connected and globalised world.

Given the positive motivations for pursuing the Government on these issues, the FIA, and indeed other non-government participants within this debate, have become frustrated by administrative and bureaucratic inefficiencies which have prevented a robust disclosure of data and a fully informed public policy debate.

Principally, the FIA has faced pronounced difficulties in further testing or evaluating the extent of the leakage of taxation from the Australian economy as a result of the failure of the Customs and Border Protection Service in releasing the finalised data of their Enhanced Enforcement Campaign, in a workable deadline ahead of the close of submissions to the Productivity Commission.

Indeed, Customs and Border Protection has operated very much at arm's length to key industry stakeholders and has not meaningfully engaged. Whilst the actual parameters of the low value importation threshold rightfully rests with the Board of Taxation and ultimately Treasury, Customs and Border Protection enforced the policy and played an important role in its administration. Their failure to properly engage with industry and comply with the Government's stated commitments outlined in its announcement of December 18th 2010 regarding the establishment of the Inquiry (which this submission addresses), deserves serious public scrutiny and has earned the strong criticism of the industry.

The Fair Imports Alliance met with officials from the Customs and Border Protection Service and the Minister's Office in November and presented them with a paper on some of its concerns around the enforcement of the low value importation threshold. Based on the actual delivery of the Enhanced Enforcement Campaign, it seems obvious that despite meetings with senior personnel and the Minister with executive responsibility, none of these matters were taken into account when developing the campaign. Industry feels strongly, and this is supported across the plethora of interested stakeholders from market dominant players that Customs did not consult or engage with the industries which are most deleteriously impacted.

The agency did belatedly attempt to salvage this exclusion of relevant industry voices by organising a forum, however, squandered this opportunity by only giving invitees a few days' notice and failing to invite key representatives of industry associations to the preference of multiple bureaucrats from Government departments or Government Business Enterprises. When further forums were arranged, questions were placed on notice in advance to allow Customs personnel time to obtain information which is key to industry concerns ahead of the forum. However, at the event itself, this information was yet again not available, not researched, not even peripherally discussed, and had to be taken on notice. The FIA then wrote directly to the Customs Minister seeking answers to specific questions relating to the enforcement of the threshold having exhausted all other options including being obstructed by unreasonably high-cost Freedom of Information requests..

During the submissions window, the Fair Imports Alliance had not received answers to many of these questions and had been deprived of access to key data and information. At an administrative level, the actions of the Customs and Border Protection Service in failing to engage with industry and their complete lack of cooperation and transparency deserves criticism. Moreover, the failure of the Minister to take adequate proactive steps to require that the engagement of industry was secured throughout the process has ensured that a key component of the Government's response to industry concerns has failed.

The Fair Imports Alliance further notes, a substantial challenge in sourcing accurate data to build into what is essentially an economic argument. It is the contention of the FIA, and indeed the gamut of other respondents to this inquiry, that their businesses are disproportionately struggling due to the misapplication and unintended consequences of taxation policy. However, the available data in the argument provided by both Customs and Border Protection through the Enhanced Enforcement Campaign results and Treasury figures outlined in the most recent Taxation Expenditure Statement, indicates an enormous lack of reliability of data. As indeed disclaimed by Treasury, the estimates they provided had a 'low reliability'¹³. Both as participants to this inquiry and as affected industry stakeholders, the FIA is disappointed that such inconsistent data is tacitly accepted by Government, especially the Board of Taxation and key agencies, yet data from industry (such as surveys and member statistics) is discounted out of hand.

The FIA believes that an analysis of credit card transactions from Australia's major banks would provide a greater data set of transactions in the retail space being lost to offshore economies. This data is not available for industry to access; however, it is imperative that the Productivity Commission attempt to source this data. The Fair Imports Alliance strongly believes that the data provided by Government agencies is not an accurate reflection of the market. We are of the view that an analysis of actual consumer transactions will demonstrate that the average purchase size of online transactions in retail is much larger and that the market share of online purchases in several categories of consumer goods is much higher than statistics quoted by the Government.

¹³ Commonwealth of Australia, 'Tax Expenditures Statement: 2010,' January 2011.

Policy recommendations

Throughout this submission, the FIA has advocated for a position of competitive neutrality across all retailers regardless of their location. Australian retailers and e-tailers should be given the opportunity to compete with their overseas counterparts on an even playing field. In order to achieve this, the FIA would like to see consideration given to the following policy positions:

1. Removal of the low value importation threshold

As discussed throughout this submission, the low value importation threshold is having the unwanted effect of 'gifting' foreign retailers with a price reduction of 15-20% on products. Removal of this threshold will ensure that Australian retailers can compete on an even ground with offshore online sellers.

2. Ensure tax neutrality by removing GST and duties from all domestic retail if the transactional value is less than \$1,000.

One possible way of ensuring tax neutrality if the low value importation is to remain as it is, is to remove GST and duties from all categories of domestic retail if their value is below \$1,000. Certainly, this would provide Australian retailers the opportunity to compete with offshore online sellers.

3. Transition funding for domestic retailers to better engage in the digital economy

Many Australian retailers (particularly small and medium businesses) may find the transition to an online economy rather daunting. Given that retailing affects a range of people within the Australian community, Government may wish to invest further funding or provide education to give the retail trade the best possible environment to prosper. This is particularly critical in a globalised world where online economies are becoming the norm rather than the exception. The FIA is concerned that the AusIndustry 'Small Business Online' program expires on 30th June 2011 and that there are no plans for a continuation or similar proposal in the public domain.

4. Tariff reductions

The FIA believe, that although such a move would not entirely redress the overwhelming price differential between domestic retailers and offshore online retailers, the Alliance believes that some relief could be provided by accelerating the removal of the textile, clothing and footwear tariff and thus provide consumers access to cheaper consumer products. Without the application of tariffs and duties Australian wholesale distributors and retailers can import product more cheaply from their place of manufacturer and sell to Australian consumers at a cheaper price.

5. A dedicated Minister in the Commonwealth Government with responsibility for the Retail Sector, and the creation of retail advisory structures.

The Australian retail sector lacks a dedicated representative and voice in the Commonwealth Government. The appointment of a dedicated Minister for the retail sector would provide the retail industry with a focal point to address concerns. In addition, establishing a representative structure such as a Ministerial Advisory

Council on retail will provide government a forum to engage with industry and consider policy options to address industry concerns and the changing marketplace.

6. Branding of domestic e-tailers as 'Australian'

The FIA strongly supports e-tailing and believes the Government has a role to play in supporting domestic e-tailers, particularly as consumers may not necessarily recognise the potential consequences of their purchases (for example, purchasing a product from an offshore online seller is a loss to the Australian economy). Government may wish to examine an online version of the 'Australian Made' logo to readily show consumers whether their product is a value add to the economy or an export of wealth. While this may not discourage Australian consumers from shopping offshore and online, it may encourage them to think before they purchase and allow them to make an informed decision.

Conclusion

The FIA understand and embrace the opportunities and evolution that online retailing presents, both to retailers and consumers. For the reasons stated in this submission, however, the FIA believes that current government taxation policy has failed to adapt to the changing marketplace and has created an inherent imbalance to the detriment of Australian retailers and the Australian economy as a whole.

Contacts

The Fair Imports Alliance is a coalition of nine industry Associations. The Australian Retailers Association and the Australian Sporting Goods Association act as co-secretariat and spokespeople and administer the Fair Imports Alliance.

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