



**COMMONWEALTH OF AUSTRALIA**

# **JOINT COMMITTEE**

of

**PUBLIC ACCOUNTS**

**Reference: Internet commerce**

**SYDNEY**

**Wednesday, 5 November 1997**

**OFFICIAL HANSARD REPORT**

**CANBERRA**

## JOINT COMMITTEE OF PUBLIC ACCOUNTS

### Members

Mr Charles (Chairman)

Mr Griffin (Vice-Chairman)

Senator Coonan  
Senator Faulkner  
Senator Gibson  
Senator Hogg  
Senator Watson

Mr Anthony  
Mr Peter Baldwin  
Mr Beddall  
Mr Broadbent  
Mr Fitzgibbon  
Mr Georgiou  
Mrs Stone  
Mr Vaile

The terms of reference for this inquiry are:

The Committee shall inquire into and report on the impact of internet commerce on:

- (1) the administration of the Australian taxation system and the implications for Australia's tax base;
- (2) the international competitiveness of Australian businesses, particularly small and medium enterprises, with the emergence of the internet as a retailing medium; and
- (3) government industry assistance programs, Customs administration, and the quality and accuracy of Australia's economic and trade statistics.

In conducting its inquiry the Committee will consider:

- (a) the expected growth in internet commerce;
- (b) the findings of and solutions proposed by the Task Force on Electronic Commerce established by the Commissioner of Taxation;
- (c) the quantity, value and type of goods entering Australia under the duty and sales tax free limit, and the commercial entry thresholds, administered by the Australian Customs Service;

- (d) the appropriateness of the existing duty and sales tax free limit, and the commercial entry thresholds, referred to in paragraph (c) and the implications, costs and benefits of any alteration to these limits and thresholds;
- (e) the commercial opportunities (both domestic and export opportunities) afforded to Australian firms by the growth in internet commerce;
- (f) the current frameworks for consumer protection and the protection of intellectual property;
- (g) the opportunities for Commonwealth agencies to improve services to the business sector and to the general public arising from growth in internet commerce;
- (h) the extent to which the Government's potential responses to the growth in internet commerce are affected by international agreements or conventions; and
- (i) the policy approaches being taken by other countries and the scope for international cooperation.

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JOINT COMMITTEE OF PUBLIC ACCOUNTS

*Internet commerce*

SYDNEY

Wednesday, 5 November 1997

Present

Mr Charles (Chair)

Senator Coonan

Mr Anthony

Senator Gibson

Mr Beddall

Senator Watson

Mr Griffin

The committee met at 9.34 a.m.

Mr Charles took the chair.

**CHAIR**—The Joint Committee of Public Accounts will now take evidence as provided for by the Public Accounts Act 1951 for its inquiry into Internet commerce. I declare open this public hearing of the Joint Committee of Public Accounts inquiry into Internet commerce. The JCPA has conducted two public hearings on this matter in Canberra during October.

The inquiry will focus on the international competitiveness of Australia's small and medium sized enterprises, the administration of the taxation system and the implications for Australia's tax base arising from the dramatic increase in the volume of commercial transactions now occurring on the Internet.

The JCPA inquiry and report will form a vital part of our country's challenge to be a leader in the worldwide Internet revolution. The implications, challenges and opportunities created by Internet commerce are only just beginning to be realised. Australia must be at the forefront of these growth opportunities and be a world player.

Currently, the global value of goods and services transacted over the Internet is estimated at \$US3 billion. By 2000, this is expected to grow to around \$100 billion to \$150 billion. The inquiry will explore some of the key issues that are beginning to emerge as Internet commerce expands. For example, Australian small and medium sized enterprises will be exposed to greater competition from overseas retailers in advertising their goods and services on the Internet. At the same time, Australia's SMEs will be able to expand their market share in the same way.

A growing trend exists for Australian consumers to purchase goods and services from overseas retailers via the Internet and avoid duty and sales tax. Currently, goods entering Australia are not subject to sales tax if they are below a \$50 duty and sales tax free limit and the value of the goods is below \$1,000 for goods imported by post and \$250 if other than by post.

An increase in the volume of imported goods not subject to duty and sales tax will have implications for customs administration and for Australia's tax base if there is excessive revenue leakage. In addition, there is a potential impact on the trading environment for locally based companies trying to compete against international traders able to avoid sales tax liabilities.

In addition to investigating and making recommendations on these issues, the JCPA will also consider the current frameworks for consumer protection and the protection of intellectual property; government industry assistance programs; and the opportunity for Commonwealth agencies to improve services to the business sector and to the general public arising from growth in Internet commerce.

The JCPA will conduct further public hearings in Melbourne next week and Canberra during December. Today, the JCPA will take evidence from the Australian

Fishing Tackle Association, the Australian Federation of International Forwarders and the Customs Brokers Council of Australia, the Australian Retailers Association, CAPEC Pty Ltd, Mr Hugh Pattinson, the Internet Industry Association and Mr Paul McNab.

Before swearing in the witnesses, I refer members of the media who may be present at this hearing to a committee statement about the broadcasting of proceedings. In particular, I draw the media's attention to the need to fairly and accurately report proceedings of the committee. Copies of the statement are available from the secretariat staff present at this hearing.

[9.38 a.m.]

**DUNPHY, Mr John Maurice, Vice President, Australian Fishing Tackle Association, PO Box 2082, Taren Point, New South Wales 2229**

**HALE, Mr Brian Derek, Secretary, Australian Fishing Tackle Association, PO Box 2082, Taren Point, New South Wales 2229**

**WEBB, Mr Lawrence Frank, President, Australian Fishing Tackle Association, PO Box 2082, Taren Point, New South Wales 2229**

**CHAIR**—Thank you for coming to talk to us today. We thank you for your submission. I am sure that members of the committee will have a number and a range of questions but, before we start, would you like to make a brief statement, without covering everything that your submission says.

**Mr Webb**—Thank you. Mr Chairman, I would like the opportunity to make a few opening comments and then to answer any questions from you and the committee. As we outlined in our submission, the Australian Fishing Tackle Association represents the Australian wholesalers and retailers of the fishing tackle industry. While our members do include some of the major retail outlets, such as Coles Myer and Big W, we are predominantly small business.

As you will appreciate, as small business operators we do not have the luxury of large secretariats nor the funding to undertake detailed analysis of information collected from our members. But the absence of detailed statistical analysis has not limited our ability to assess the risks and challenges of our businesses. We work with our members and are well aware of the trends in the marketplace and implications for businesses. For instance, around this table we have over 75 years of direct experience in the tackle association.

For our industry, Internet trade represents a serious risk. AFTA has been at the forefront in bringing this issue to the attention of the government in Canberra. For several months, we have sought to convince officials of the risk of this trade and its inherent unfairness to our industry. For the Australian fishing tackle industry, the issue is not whether the Internet is good or bad, nor the conditions or controls on access by consumers to the Internet. Rather, it is the way the Australian taxation system seriously disadvantages Australian retailers. The real point for a retailer is that he cannot compete with his competitors on the Internet where those competitors have an effective price advantage of around 26 to 33 per cent.

We will today show you first-hand how this is happening. We will also show you how our competitors on the Internet are deliberately promoting the avoidance of tax in Australia and are using the discretionary allowance by Customs as a marketing tool. We



will also be able to give you examples where shippers are deliberately undervaluing. The result is that we and the Australian taxation revenue base lose. We see the issue to be considered by the committee as to how the Internet as a marketing medium is forcing the government to address a taxation system in Australia in the context of a borderless society. Our competitors operate in a different taxation environment and we cannot compete. We have submitted to you a number of recommendations. These are serious proposals. We hope the committee can give them due consideration.

**CHAIR**—Thank you for that, Lawrie. One of the things the committee ought to first ask is, in your submission you have stated serious concerns about what is happening to your industry because of the so-called ability to avoid tax, both customs duty and wholesale sales tax. But how competitive are you against suppliers operating through the Internet if those taxes were removed? Are you still competitive or not?

**Mr Webb**—Yes, we are very competitive. I think Mr Dunphy would probably be better equipped to handle those questions.

**Mr Dunphy**—What we have done is gone through the major products of importance in this country, that is, the biggest sellers from fishing reels, whether it be a Shimano, whether it be an Abu, whether it be a Penn, whether it be anything. We have shown you the FOB price that either Bass Pro, Melton's or whatever offer. We have shown you what the landed cost would be to the consumer if it included the freight as detailed in Bass Pro shops' catalogue. Then we have shown you what the best competitive retail price in Australia is. So they are the columns.

You can see that in all cases, except for minor variations, we are very competitive, but if you put the import duty and the sales tax on we are actually cheaper. Australian retailers in the major product lines are very competitive. This is a very much smaller market than America. There are 280 million people or 260 million or something there and there are 17 million people here. If someone wants to buy six game reels, they will shop from Broome, they will shop from Coffs Harbour, and they will check the price and make sure they are getting the best deal.

What I have done also is prepared the documentation from which we actually have got these prices, which I can leave so you can check it. I have also included Bass Pro shops' catalogue and Melton's catalogue. We have simply taken the prices out of these catalogues for your reference. We can leave them, as long as, if you don't mind, we can get them back when the inquiry is finished. I have prepared 10 copies of these.

I am going to give you some examples of how it works. Basically, I have listed every Shimano product that is in demand. These are the biggest selling products we have. I have listed lures. I have listed Abu's best selling products, Penn's best selling products, Silstar, Daiwa, plus some electronic trolling motors, some fishing line—probably the two most important brands—and tackle boxes. I am certain that, if I went through the entire

range of Bass Pro's catalogue or overseas dealers and compared them to retailers in this country, you would find, because the number of SKUs is so large, that in some instances they are more competitive than we are, but in most cases, on items of real importance, if you studied these notes you can see it is very clear cut: FOB price, Australian landed cost to the consumer, if the tax and duty is paid, what the price would be, and also what the current retail price is in this country. I cannot be any more specific than that in terms of answering your question, because we are very competitive.

**Senator GIBSON**—There is a great push around the world for freeing up commerce on the net. I see in this week's *Economist* the perils of electronic shopping, but basically saying we need fewer consumer protection laws, not more, in order to encourage greater commerce and interchange and trade around the world. What is your view of that?

**Mr Dunphy**—My view of that is, fine. I think this situation has brought to a head what is actually happening in this country. I do not mind the freeing up of anything; I think that is wonderful. But what we have got to face is that we have a totally different tax regime in this country to what we are competing against in, for example, Singapore. Singapore is going to be more of a problem for this industry anyway than America because Americans trade quite fairly, but in Singapore we can produce you evidence of what actually happens—maybe it is the way they do business, but everything is undervaluing. We have got the evidence which we can produce and give to you here. But they have different fringe benefits tax, that is, none; sales tax, quite different; free port; free everything. What we are faced with is living in this country, which we love, and paying the correct amount of taxes that we have to pay.

In essence, all we are saying is, give us an even playing field. We do not care how it is freed up or what the rules are. The government decides what the rules are. If people want to compete in this country, like Americans, we welcome it, that is fine, not a problem—as long as they pay the same taxes as we pay, no more and no less. We are not asking for anything brilliant.

**Senator GIBSON**—Please explain more what you mean about unfair competition from Singapore. What is actually happening? I do not mean their internal tax rates. Can I buy from Singapore cheaper products than I can from the Australian retail market?

**Mr Dunphy**—Well, you can if you do not pay any of the taxes. And what the people in Singapore say quite strongly, and I can detail—it is probably an opportune time to give it to you—is simply this:

As for the duty fees, we would lower the prices of the order by declaring a false invoice.

And this letter was sent to most of the retailers in Western Australia because of the proximity of trade between Perth and Singapore. That is unfair, is it not?

**Senator GIBSON**—Sure. Are they trading on the net currently?

**Mr Dunphy**—Yes, certainly.

**Mr BEDDALL**—That is a trade that is happening now—apart from the Internet, isn't it? I mean, it is not happening with the Internet. What I am trying to get at is that that is a current business practice.

**Mr Webb**—Yes, they are going to do that anyway.

**Mr BEDDALL**—And you see that is exacerbated by the fact that the Internet will run—

**Mr Dunphy**—It is, because the first contact is the net. They get on the net and ask for a catalogue. Once they get the catalogue, then they get the follow-up.

**Senator WATSON**—Can't you get these cheaper prices as importers? Why is it that you cannot get it on a wholesale differential, whereas the retails seem to get the greatest benefit? There seems to be some missing link here.

**Mr Dunphy**—I am sorry, I do not understand your question.

**Senator WATSON**—If it is fishing tackle importers, you buy the goods wholesale. Surely you are going to get the same sort of margin?

**Mr Dunphy**—We import the goods and we pay factory price—not wholesale. When we come out here, when the goods arrive here, we sell them at a wholesale price. Is that what you mean?

**Senator WATSON**—You maintain there is a differential of about 25 to 30 per cent. But surely you should be able to buy your goods and apply the same sort of principle to your factory price or the price which you pay for them and still maintain that differential margin?

**Mr Dunphy**—We are saying that there is a difference of 26.4 per cent to 32.7 per cent between if goods come into this country and they are non-dutiable, where the sales tax levy equates to a factor of 26.4 per cent, and if the goods are dutiable, where the sales tax and duty factor is 32.7 per cent. That is the difference we are talking about. We are not talking about a difference in margin that we make.

**Senator WATSON**—But as importers you would still be able to reap that sort of benefit if there is a problem in the way the wholesale tax is applied. I cannot see how you are going to be disadvantaged. If you import goods in your own right as a wholesaler, don't you get the same sort of duty concession as people who import them direct?

**Mr Hale**—No. We must pay sales tax and duty when we import the products.

**Senator WATSON**—How does that anomaly arise?

**Mr Dunphy**—How do they not pay it?

**Senator WATSON**—That's right. How is it that as importers you have a different tax regime or a different method of application of your sales tax than if somebody gets it indirect? That is the core question.

**Mr Dunphy**—The answer is fairly simple. When we as importers bring the goods in in volume, as we get them in we pay the import duty before we actually get the goods. So that is done. When we sell the goods, we have to declare a sales tax declaration at the end of each month and remit that money to the government in terms of the sales tax department. So that is that system. When the customer gets the goods, one of the key problems is that the volume of goods coming into the country is such that not everything can be checked, because Customs at the moment I believe do not have the manpower to be physically able to do it.

So we have these concessions in place, and this is where I am sort of confused about the issue. What Bass Pro Shop have said in print—and they have just dropped a quarter of a million of these around this country—quite clearly is that, if the consumer places an order for \$US200 or less, there is no import duty and there is no sales tax. That is a guarantee. They say if the goods are more than \$US200 then they will collect sales tax at a rate of 35 or 40 per cent. They say 35 here and 40 there; I do not know what they mean. But, if they collect it as an American company, where are they going to send it to?

**Senator WATSON**—So their benefit comes under the exemption provisions?

**Mr Dunphy**—The exemption provision does not say \$250, that is the top limit, and a thousand, but the letter of the law, as I understand it, says that, if the sum total of the money to be collected in terms of duty and tax is \$50 or more, the goods should be declared and the money should be collected. That is not what this says. That is where I am confused. They are saying, 'All of this stuff will come in.' We placed orders on this company last week. We ordered \$243 worth of lures and they said, 'It is too much.' We said, 'What do you mean?' 'It is more than \$200, so we will ship it for you in two cartons so you won't pay any duty or tax. The goods will arrive here tomorrow.' And we said, 'What if we want to order \$2,000 worth?' They said, 'We will ship 10 cartons for you, 10 cartons of \$200.' That is what we are up against.

**Mr BEDDALL**—Can you take me through an exercise on your products and price comparisons, say, the ones at the top, the Tiagra 50? Can we just go through the cost thing so I can get it clear. \$US529.99 converts to \$A777.13?

**Mr Dunphy**—Yes, we have used an exchange rate factor of 70, which is what it currently is.

**Mr BEDDALL**—Yes. Does that give you a price of \$A982.29 if duty and tax are added to the \$A777? What is the \$A982?

**Mr Dunphy**—I am sorry, let us just go back to the start: \$529.99 is US dollars. Converted in Australian dollars and with, I think, whatever their cost factor is here, whatever it says, if it is between X number of dollars it is X. We have used exactly that.

**Mr BEDDALL**—Okay.

**Mr Dunphy**—There is a little star next to that which shows you that this product is duty free, so the next column is with sales tax alone. If you put onto this rate, onto the \$777, 22 per cent sales tax, it brings it up to \$982.29.

**Mr BEDDALL**—Then you have got a price here of \$800, which you say is Australian retail?

**Mr Dunphy**—That is correct.

**Mr BEDDALL**—You are selling at \$800?

**Mr Dunphy**—Yes. Our retailers are currently selling that at \$800 or in fact sometimes a little cheaper.

**Mr BEDDALL**—So, on the Internet, they would not be able to compete?

**Mr Dunphy**—Not if they paid tax.

**Mr BEDDALL**—Okay. But, even with the cost of conversion and postage and all that, you are pretty competitive?

**Mr Dunphy**—Very much so. In certain instances a lot cheaper, but there are several cases where it is line ball or what we are saying is that it really is not worth going through ordering stuff from overseas and then running warranties, sending them back there.

**Mr ANTHONY**—There is only \$23 difference between the Internet and—

**Mr Dunphy**—Correct. There are examples with a wider disparity further on on electric troll motors, where there is—

**Mr ANTHONY**—What price would you be getting the wholesale price at, then?

**Mr Dunphy**—I am sorry?

**Mr ANTHONY**—The retailer is paying \$800?

**Mr Dunphy**—No, the retailer is selling it at \$800. We sell it to them, I think, at a new price of somewhere in the order of \$560. If you need our price list, I do not have one here but I can certainly get one to you.

**Mr BEDDALL**—Can we take a quantum leap, then? These are prices you are taking out of US magazines, et cetera. Is there an Internet site which sells this particular type of gear?

**Mr Dunphy**—There are several.

**Mr BEDDALL**—Are these about the same prices still?

**Mr Dunphy**—Sure.

**Mr BEDDALL**—Because what we have found in other industries, for example in the book industry, is that the prices are so different because they do need a warehouse, they do not need anything.

**Mr Dunphy**—Yes, that is true.

**Mr BEDDALL**—They just need an electronic mail box and they are off and running. But that is not the case with this?

**Mr Dunphy**—Not at all. These two companies, Melton International and Bass Pro shops, are probably the two strongest in terms of Internet and certainly the strongest in terms of mail order. They are also the biggest and they are very, very competitive. I mean, there are numerous other ones or examples we could have used from America: Capellas; we could have gone through them all. But these two traditionally have been the cheapest, and that is why we have used them.

**Mr BEDDALL**—I also assume, and I think fairly correctly, that you have always had competition from mail order firms. This is an industry where mail order has always been a big player.

**Mr Dunphy**—Not so much in Australia.

**Mr BEDDALL**—Not so much in Australia, but a lot of the other small businesses are now facing this type of competition for the first time.

**Mr Dunphy**—We have had it for years.

**Mr BEDDALL**—Yes. Which probably means that is why you are competitive. You have to face market forces.

**Mr Dunphy**—Most of these products, if you talk Abu, if you talk Shimano, if you talk Penn, Daiwa or Silstar, they are from international companies, and we must keep prices very similar within different countries, especially ones that use a similar product, that is, Australia and certainly America. In Europe it tends to be different because the product they use is very much different to the product they use in this country.

**Mr ANTHONY**—Just on products within the fishing industry, this might be a difficult figure, but how much of that product would be manufactured in this country?

**Mr Dunphy**—Very little.

**Mr ANTHONY**—Okay. The second point is, how many Australian retailers, fishing shops, that is the tackle shops, are actually ordering direct over the Internet and stocking their shelves?

**Mr Dunphy**—Not too many.

**Mr ANTHONY**—But they could be doing that, couldn't they?

**Mr Dunphy**—Well, they could, but they would not be competitive at these prices. We can sell the product to them much cheaper than they can buy on the Internet, that is for sure.

**Mr ANTHONY**—Yes, because on some of these prices I noticed even your price is cheaper than the Internet price.

**Mr Dunphy**—Certainly, yes. As I said, we are very competitive, but it is a month's job to go through this entire catalogue. In American made lures, we are not competitive at all, but the upsurge in manufacturing of Australian lures more than makes up for that. The Australian lure manufacturing business at the moment is very big and I see some very good opportunities for those people on the Internet anyway.

**Senator GIBSON**—Have they started to do that yet?

**Mr Dunphy**—Yes, certainly.

**CHAIR**—So on one hand you are proposing to your members that they become involved in Internet commerce, and on the other hand you are saying to us that you are at a huge competitive disadvantage because some individuals are using the Internet to purchase from overseas.

**Mr Dunphy**—We are not actually saying just that. We are saying that we are competitive, but we are saying one of the major problems we have with the Internet as a catalyst to get more mail order magazines out there on the Internet itself is that the only problem we have is an inequity in the sales tax rate. For example, the average purchase in a fishing tackle shop is \$60 to \$65. That is the average purchase, and we get these figures all the time. Can you imagine what it does to those shops when we are talking here the average purchase \$US200, which is \$A285? That is the average purchase here. We are talking about a loss to the government revenue on every one of these transactions of \$94.35, because that is what it equates to. We are not talking \$50. It is \$285, and sales tax import duty on that figure is \$94.60. We have an American company saying, 'Here, buy it.' We are entitled to ask how they can put this in print without any prior consultation. Or did they have prior consultation with the government agencies that represent this? How can they do that? This is a fair question.

**Senator WATSON**—You are recommending an elimination of the tax-free threshold in relation to small quantities of goods. That is the only way to solve your problem at the moment.

**Mr Hale**—It makes it more equitable.

**Mr Dunphy**—Or make sure that it is not totally eliminated but it is reduced or it is properly policed.

**Senator COONAN**—You have said in your submission that your retail sales have declined about 15 per cent on average. What do you think that is due to? You have said you are competitive. Is it entirely due to these particular sorts of problems with the Internet and wholesale tax? What do you put it down to? Have there been some real shifts in the industry?

**Mr Hale**—We are going through a downturn in the industry. I think that is partly due to the economy in Australia at the moment. It is very difficult to actually measure the effects of the Internet on this industry. We believe it is pretty substantial but we are a small industry and we do not have the people or the money and finances to do the research to find out. When we are talking to most of our members they are all saying they are having customers coming in saying and skiting, 'I bought this on the Net. I saved \$50,' or \$100, or whatever. We are getting a lot of information from our members that this is happening. I really think that the Internet trade is bigger than we think. This is having an effect on industry too.

**Senator COONAN**—Why do you say it is bigger than you think?

**Mr Hale**—It is very hard to judge. We cannot get definite statistics on what is going on. The information that we are getting from our members is that it is a major problem. In my company alone we are being told that Manns lures, which we represent in



Australia, are being bought over the Net because there is about a \$4 or \$5 difference on each lure. They only retail for \$13 anyway. If they buy a bagful like this they can get \$200 or \$300 worth of lures in a bag like that and save quite a lot of money. If they were being charged the duty and the sales tax on it then it becomes more even and we are in a better competitive situation.

**Senator COONAN**—What happens with warranties? Have you had any problems with people who have bought goods over the Net—perhaps more expensive items than lures—coming to you and saying, ‘Can you fix this up for us?’

**Mr Hale**—Yes. We have evidence where customers have brought in models that we do not actually sell in Australia and asked for repairs. When we say, ‘We are sorry, we can’t help you because we do not have the spare parts to repair this reel,’ they get quite upset. There is just nothing we can do. We do sell models in Australia that are different to some of the models in the States. Quite often, the consumer buys a product from the States that is not really applicable to this market. They buy it out of a catalogue without seeing the product and when they get it out here they find it does not work or it is not suitable for this market.

**Mr Dunphy**—It is a common problem.

**Senator COONAN**—Do you carry out repairs for lines you sell if people buy them over the Net?

**Mr Hale**—Yes. We cannot do anything but repair them.

**Senator COONAN**—Is that to protect your own brands and protect your own lines?

**Mr Dunphy**—Yes, it is our responsibility.

**Mr BEDDALL**—Given that any reform in these areas is a zero sum game—if the government of the day accepts the fact that the tax regime is making you uncompetitive—what is your ideal solution to ensuring that the tax regime is fair and equitable to your members and applies to those people who are importing?

**Mr Hale**—I think we would all agree that a GST or a similar type of tax would make it a lot fairer across the board, and these taxes should be charged on Internet purchases.

**Mr BEDDALL**—How do you charge a GST on an item imported through the post?

**Mr Hale**—Couldn’t Customs do this? I am sure they must do it in America.

**Mr Dunphy**—I think you use technology to fix the problem—like everything we do these days. The government expects us to be internationally competitive, and we are. But I think the government has to be internationally competitive itself. For example, for all goods that we send out of our warehouse we use bar code systems to track them and to do everything. I know that you can use a bar code system for price but what I am suggesting is that—and I have read Customs' submission, too, and they say this as well—a great many of these products that come into this country do not have any declaration or any paperwork on them. In relation to a further great many, the declaration is illegible. Surely that is unacceptable. Everything should have a declaration. One of the problems we face is that, when the Australian orders it on the Internet, he does not instruct the shipper to do anything wrong; he just places the order. If the goods come in and the guy has undervalued, which is a common thing, if he does not charge or put a declaration or if he does like this, the Australian consumer has not done anything wrong at all. The Australian government is losing. The overseas people know how to work this system, believe me. I should give you the copies of this. There are a lot of other things.

**Mr BEDDALL**—The country that is pushing this more than anyone is the United States government. It sees a huge advantage for the US, because it is the biggest Internet site, and it is not really interested in collecting Australian taxes at all.

**Mr Hale**—No. It has to be collected at this side.

**CHAIR**—One of the problems I have with what you have told us is that we have received information from ABS that indicates that between 1993-94 and 1996-97, for instance, fishing rods imported have gone up in value from \$8 million to \$10½ million, fishhooks from \$4 million to \$5 million and fishing reels from \$13½ million to \$21½ million; but you tell me the industry is going down.

**Mr Dunphy**—But you are talking dollars and not units. Did you compare the units? What you have there is dollars. Does that mean there are more units or the price is higher?

**CHAIR**—Yes, there is more quantity, too. Fishing reel quantity went up from 797,000 to 1,289,000 between 1993-94 and 1996-97—a substantial increase in the number of units and in dollars.

**Mr Dunphy**—I cannot answer exactly, but 1993-94, 1994-95 and 1995-96 for my company were quite good years.

**Mr Hale**—They were good years in the industry.

**Mr Dunphy**—This year is nowhere near the same. I think there were more people in it. We had a lot more people come into the business. You have people like K-Mart, who are importing directly. A lot of people came into the business; but, unfortunately, a

lot of those people are no longer here.

**Mr Hale**—They are going out.

**Senator WATSON**—There must be a statistical aberration in 1996-97 in relation to fishhooks, because your average price bears no relationship to your quantities.

**Mr Dunphy**—Some of that information is incorrect, too. For example, if you look at fishing rods, you see that radio antennas and aerials are in there, too. That is one of the problems. Of this item, 180,000 come into the country and they are 75c each. You cannot make a fishing rod for that. When I checked the information regarding fishing rods in particular, not reels, I saw that there is a lot of other stuff in there that you do not know what it is, and radio antennas are part of it.

**CHAIR**—You said:

The numbers of dissatisfied customers is growing daily, and the complaints against equipment, for which a . . . lot of effort and money has been invested to promote and develop a place in the market, is being undermined . . .

You say that is because equipment is coming in which is not suited to our marketplace and is not used to the high salt content of our water. But you say that, if somebody imports it through the Internet and does not pay the duty and the wholesale sales tax but there is something wrong with it, you still have to fix it. I do not understand why.

**Mr Dunphy**—We have to. I will give you my example on it—the Tiagra fishing reels that we spoke about before. In America you have a different drag radiant—I will not be too technical. The difference in cost between what they have and what we do is something like \$70. For us to put that reel right to make it fishable in this country, it costs us \$70. We cannot have that customer out there with a reel that does not work properly. That is what we pay for. That is what we spend our money in advertising on, and we probably spend more than anyone else. We protect our image. We will charge them the \$70. They are not very happy with it either, but we will charge them. It is not like a warranty repair, because—

**CHAIR**—I thought you were saying that you do this for free.

**Mr Dunphy**—Not at all. Sometimes we will if it is the same reel; but not if it is a different reel that we do not import. That is why we get people who are not very happy.

**Mr Hale**—But we do do repairs on a product that is bought on the Internet. If it is the same product we are selling, we have the spare parts, we can repair the reel and we quite often do that under warranty. You cannot tell whether it has been bought here, in America or anywhere else in the world because it is the same product. There are no serial

numbers on fishing tackle in general except for the more expensive game reels and that type of thing.

**CHAIR**—And does the manufacturer reimburse you?

**Mr Hale**—No.

**Mr BEDDALL**—Do you envisage a situation where if Internet purchases take place then you actually say, ‘Well, in order to have a warranty undertaken, you must produce your receipt and show that it was bought from an accredited retailer’? This happens in Hong Kong now with watches, for example. There is an accredited retailer—and most people do not know that there is usually only one in a city—and you have to go to that retailer. So if you bought it somewhere else, it is too bad. Do you envisage a situation, down the track, if this trade grows, where you have to say, ‘Look, in order for us to commercially do warranties we need to actually do warranties on products purchased in Australia’?

**Mr Hale**—I think that is going to have to happen, because as this grows it is going to be a major problem for us. We are going to have to employ extra people to do these repairs if it gets big. But the biggest problem is that we have got to be competitive in this country. At the moment we are just not competitive.

**Mr Webb**—From my company’s point of view we certainly do that. We have warranty certificates on our rods. The rods we have built here have the same name as those available from America, but they are two totally different products. If you cannot produce your warranty certificate, and we have not got it registered, we will not give you any warranty on an imported rod whatsoever.

**Mr ANTHONY**—In your submission the fundamental question you are addressing is the level of sales tax. What level should it be at? What would your association advocate?

**Mr Dunphy**—Zero.

**Mr ANTHONY**—Well, you are not going to get zero. But in the other breath you talked about a GST so—

**Mr Dunphy**—Whatever level you put it at, it is going to change within a year, isn’t it? It does mean you have got a starting point—that is what governments do.

**Mr ANTHONY**—They are indexed now, so you have not been getting very large change at all, recently.

**Mr Dunphy**—Ten or 12½ per cent, or thereabouts.

**CHAIR**—Are you willing for company tax to go up if the sales tax comes down?

**Mr Dunphy**—I knew you would get me one way or another.

**Mr Webb**—From our point of view, we would probably all like to see some form of GST. That is where we are coming from. It is a fairer tax and we would certainly like to see it applied on all imports, whether it is for \$50—I am not talking about grandma who sends you down a Christmas card again as a gift—or whether we are talking about imports from mail order houses. I think there should be a GST applied on the declared value at the point of entry.

**Mr BEDDALL**—A GST or something like a retail tax.

**Mr Hale**—A consumption tax.

**Mr Dunphy**—There is a difference.

**Mr BEDDALL**—I had the privilege, at one stage, of being the minister for customs and of talking to my British counterpart who told me how great it was because they employed 23,000 extra customs officials when they brought the VAT in, in order to police it.

**Mr Hale**—Think of the jobs you would gain.

**Mr BEDDALL**—I do not think this government is about to create 23,000 new public service jobs. Sometimes people get caught up with a consumption tax which I think has a great deal of merit—

**Mr Dunphy**—I like a consumption tax. It is simpler.

**Mr BEDDALL**—Rather than a VAT which is through the system, and the paperwork, for you, would double.

**Mr Dunphy**—I prefer a consumption tax like the one they have in America. The consumption tax thing appeals to us because of its simplicity and its ease of operation. What I think really galls this industry at the moment—and not just this industry—is that not only do we collect the tax, but we also have to fund it. It was, I guess, a fair call when taxation systems started and it was 2½ per cent and you got low interest rates, but these days when we are talking 22 per cent sales tax and we have to pay that money some 35 or 40 days before our debts have come in, I do not think that is fair at all.

**CHAIR**—You are talking about trying to tax all this stuff as it comes in, and yet you tell us and you gave us one piece of paper that implies that people are willing to send goods to Australia and provide non-valid invoices, or fraudulent invoices—

**Mr Dunphy**—May I just give you this one?

**CHAIR**—If they do that or if, for instance, the wholesaler in Kansas City or wherever sends out a fishing reel to an individual in Australia and puts a birthday card on top of the box that says, ‘Gift of no commercial value,’ then how does Customs ever police that?

**Mr Webb**—There is no way of policing it as such, per se. You could not possibly expect Customs to pick up on all of those things. However, if there was a trend arising that there were a lot of parcels coming out of that city that you mentioned, certainly Customs would be obliged to look at that, I would feel.

**Senator GIBSON**—On the customs matter, you made a recommendation ‘seek removal of discretion to exempt imported goods’—the \$50 limit, in other words. We have had evidence from Customs that going any lower in value than \$50 would cost the taxpayer nearly as much; in other words, to break even for chasing sales tax and/or duty is roundabout the \$50 mark. So there is no point in going any lower, because we are just churning taxpayers dollars around. What is your response to that?

**Mr Webb**—My personal response to that is that I believe it would be quite simple just to apply a flat fee, an entry fee, right across the board on anything that comes into the country. It would be a very simple collection procedure. That is my own personal viewpoint.

**Senator GIBSON**—A fee per item?

**Mr Webb**—Per item, irrespective of what the item is. If it is a packet of seeds, a fishing rod or a reel, or whatever, you just have a flat entry fee. The user pays. We are really in a user-pays situation right now anyway. So, if the user or the consumer wants a by-product overseas, if he wants to import it down through Australia Post or any other way he chooses, at the point of entry—whether it is coming through a commercial airline, freight forwarding company or whatever—there should be a collection fee paid, whether it is \$50 or \$60. It is that simple. On the other hand, as I said earlier, if my grandmother wants to send me a jumper for Christmas there should be some way around that as a gift.

**CHAIR**—One of the things you said bothered me a little. You said:

Furthermore, Internet trade has been also identified by the ATO as leading to structural changes in the distribution and delivery of certain products. Internet is a threat to current ‘wholesalers, brokers, agents, consolidators, advisers, franchisers, multilevel markets and retailers.

What do you want us to do about that?

**Mr Dunphy**—We were just making the point, and we were quoting from their

report, that there is nothing you can do about it. We are not asking you to. I do not think anything can happen there. If you look at the back of that piece of paper it will show you the real value of the goods; the customs declaration is on the front.

**Mr ANTHONY**—Back to some of the pricing comparisons, which is where we started.

**CHAIR**—You have some declarations that it was worth \$65?

**Mr Dunphy**—Yes.

**CHAIR**—And the real invoice, including freight?

**Mr Dunphy**—\$US987.

**Mr BEDDALL**—That is the problem: this is a fraud case, isn't it?

**Mr Hale**—Yes.

**Mr Dunphy**—It is the same company, that we gave the evidence to Customs on when we went there in April.

**Senator COONAN**—As Mr Beddall says, it is really more an enforcement issue than a real fiscal issue that we are trying to deal with, with normal commerce and trade and imports.

**Mr Dunphy**—I understand.

**Mr Webb**—I think we want to make it quite clear that we do not fear the Internet. We just want it made, somehow, a level playing field.

**Mr BEDDALL**—Are many of your members utilising the Internet domestically for your customer base?

**Mr Hale**—Yes, there is quite a number of them.

**Mr Dunphy**—Very many.

**Mr BEDDALL**—Rather than fear it, you have embraced it.

**Mr Dunphy**—Certainly. If you get into the Internet on fishing, the number of Australian tackle shops on it is just never ending.

**Mr BEDDALL**—This is a good inquiry for me. I cannot get into it. I open it up,

but I cannot find anything on it.

**CHAIR**—I found earrings the other night.

**Mr BEDDALL**—I hope they suit you!

**CHAIR**—Thanks very much, David.

**Mr Webb**—You certainly need plenty of time if you are going to go searching on the Net, that is for sure.

**Mr BEDDALL**—It seems to me that you really have to know the actual address rather than search. I did one the other day. There were 798,000 finds or something.

**Mr Hale**—You have to have a good search engine, and they are around. If you put Bass Pro into a good search engine, it will come up very quickly.

**CHAIR**—Thank you very much, gentlemen. We certainly appreciate your taking the time and trouble to write a submission and come talk to us. You have helped enlighten us. I am not sure what we are going to do about all that. Is it the wish of the committee that the document entitled 'After comparison pricelist' of FANTEC Enterprise correspondence, correspondence from Bluefin Fishing Tackle, AFTA statistics and Bass Pro order form B be taken as evidence and included in the record as exhibits? There being no objection, it is so ordered. Thank you very much.



[10.40 a.m.]

**FRASER, Mr Robert Lawrence, Board Director, Customs Brokers Council of Australia Inc., PO Box 303, Hamilton, Queensland 4007**

**HEAZLETT, Mr Kent Gordon, Past Chairman, Customs Brokers Council of Australia Inc., PO Box 303, Hamilton, Queensland 4007**

**MORRIS, Mr Stephen John, Executive Director, Customs Brokers Council of Australia, PO Box 303, Hamilton, Queensland 4007**

**LOVELL, Mr Brian Paul, Chief Executive Officer, Australian Federation of International Forwarders, Suite 403, Level 4, Westfield Office Tower, 152 Bunnerong Road, Pagewood, New South Wales 2035**

**CHAIR**—I now welcome representatives from the Australian Federation of International Forwarders and the Customs Brokers Council of Australia to today's hearing. We have received and digested your submission. Would you like to make a brief opening statement before we start to ask you questions?

**Mr Morris**—If I may, Mr Chairman. In terms of our position as regards the terms of reference, we would take our submission as forwarded to the committee as being our opening statement. As the second paragraph states:

It is also the CBCA's opinion that few individuals currently using the Internet as a means of making overseas purchases have any understanding of the application of the '*customs duty and sales tax free*' limit or commercial entry thresholds for customs entry purposes. While individuals may not understand the advantage of 'screen free', commercial operators clearly do, such facts being exemplified by the increase of 'screen free' consignments.

I think it is fair to say that, in relation to the issues that are in the terms of reference, the main aspects that we keep coming back to are the issues of equity as to the treatment of goods imported, and we abase the statement that there is a benefit or any other type of accrual to the customs broking and freight forwarding industry. We would see no revenue flowing to us in terms of any changes in government philosophy in relation to screen free. It is all about the equity issue, prohibitive imports and the non-leakage of government revenue.

**CHAIR**—Do you see that the mechanisms at the airports and on the wharves causing us big problems now are likely to be exacerbated? Do you think the volume of goods coming is going to increase, or are they just going to come in in a different manner, if we are talking about goods?

**Mr Morris**—I think if we go across the table and ask for various comments, and I may just start on this particular issue. I think the screen free concept—you mentioned sea

freight—is really not an issue in relation to sea freight. It is more in relation to airfreight and in terms of the express carriers industry, where the majority of the screen free takes place. We do see that there will be a change in the amount of goods coming into this country as a result of Internet trading. In the main, these goods will be carried by the express carriers industry due to the fact that opportunities exist for retailers, sellers or whoever to take rates with the express carriers industry that allow their goods to be delivered with certainty and within time to those people who wish to purchase on the Internet. Australia Post I do not think has that same level of confidence in terms of its ability to meet those service demands, but the express carriers industry certainly has.

Looking at the figures that have come forward from the Australian Customs Service out of their own customs figures, and I quote issue No. 7, which is data to the June quarter 1997, in 1996-97 there were 1.062 million sea cargo manifest lines. In the same period, there were 3.66 million house airway bills reported Australia wide. That gives a total population of about 4.7 million consignments into this country, of which only 2.4 million are entered for home consumption by way of a formal customs entry.

On the basis that there are something like 2.4 million to 2.6 million still sitting out there, we would suggest that a large percentage of those are trans-shipment items. So, if we take about 30 per cent of those as being trans-shipment, we might have about 1.4 to 1.6 million consignments coming into this country by airfreight that are screen free and for which no record is held as to the value of the goods in question in terms of statistics. Therefore, we do see a problem in the process—an increasing problem.

**Senator GIBSON**—Those ones coming in are under the limit of the \$50—

**Mr Morris**—No, not necessarily so. Some are. I think the Australian Customs Service statistics suggest that below the threshold limit is something like 50 per cent of those consignments.

**Mr Heazlett**—If I can just add to Steve's comment. The first part of your question really related to whether there are problems currently with the volumes that are being handled through Australian ports and airports now. I do not think there are at all. The days when you could blame or put blame on either Customs or any other area that your shipment was held up have certainly gone. All of us have probably heard when we want something in a shop or whatever, 'Sorry, mate. It's held up with Customs.' That is not the case.

In the majority of cases cargo is cleared prior to its arrival or prior to its availability for physical delivery. So that argument certainly has gone. The electronic systems that are in place currently with the ACS areas or whatever it might be certainly can accommodate that, especially in respect of the screen free. We are not proposing that everything should be entered formally in the same way as it is today. Certainly there needs to be a simplified method of handling smaller consignments, because we know the

numbers that are there. These can be looked after by a modified entry processing system. The electronic systems that are employed by the freight forwarding and customs broking industry as well as with Customs are certainly at the leading edge of what is available throughout the world, and I think that has been acknowledged for some time.

Electronic commerce has been employed throughout our industry for a long time, and the rest of commerce is probably starting to catch up now. The Internet certainly will be used by our industries for communications and all that sort of thing. But certainly there should not be that barrier of saying, 'Everything has to be formally entered'—as is the case currently—'on this date.' It certainly can be modified and handled quite well.

**Mr Lovell**—I would just like to add one more point on the question you raised. This is not totally relevant to this inquiry but I think the committee should know the physical barrier at the airport primarily, which is what we are talking about, is still there. The cargo handling facilities are not equipped to deliver the goods as quickly as they are being cleared electronically. If we sped up the system to the nth degree and had goods cleared electronically immediately, the goods would not move from the airport any more quickly. Those comments were made to Mark Vaile at the airfreight inquiry last year. That is just additional information.

**CHAIR**—The Fishing Tackle Association told us this morning that, because of the import limits with respect to duty and sales tax free that are set now, overseas companies might, if they are sending 10 items that would breach the \$50 limit, simply send 10 packages.

**Mr Fraser**—That is correct. In fact, it can amount to thousands of packages from a single supplier.

**CHAIR**—Is a lot of that happening?

**Mr Lovell**—Yes. I made reference to that in my article which I put with the submission. Fishing tackle, compact discs and in fact jeans are a big problem. Single pairs of jeans are being sent by organisations which are set up to do that in the States, for example, to individual importers in Australia.

**CHAIR**—How about goods of a greater value coming through the system in a package marked 'Gift of no commercial value'?

**Mr Heazlett**—I think that does happen, certainly; and the smarties in the industry have had that worked out for a long time. But Customs, I think, in that particular case would be aware of that and would be on the lookout for that happening. Going back more than 10 years ago, I was working for one of the multinational forwarders. Our overseas operations were structuring the shipments so that they came in—this is normal commercial cargo—under the \$250. There was a flat rate of freight charged, so they were not

penalised for any number of consignments that there might have been.

In those days—and this was part of the reason why the ‘screen free’ scenario came into play—Customs were taking four days to process an air freight entry through Sydney airport. It would take you a day to get it here and four days while it went through a manual process within Customs. Those days have totally disappeared. You are gaining release of cargo within seconds, not days. If we started from scratch on a very simple entry here today, I would think that within three or four minutes we would have the release, the Customs duty paid and it on its way. I do not want to do myself out of a job here, but it is that straightforward because a lot of the work is done prior to the arrival of the cargo and that is where the saving is achieved.

**Mr Morris**—In addressing your comment, Mr Chairman, as to whether the consignments are over the threshold, that is a question that only the Australian Customs Service, in terms of a review or check at the time of importation, would be able to verify or not. In a study they had done for them on the screening position on commercial cargo, the consultants suggested that there was only a plus or minus five per cent variation as to the figures shown on air cargo automation values as against the formal Customs entry system under COMPILE.

COMPILE provides an opportunity for all the commercial documents to be provided in terms of the formal entry being created. Therefore, there is an opportunity to determine what actually is the price paid for the goods, as against a consignment note that comes with the express carriers industry. In many cases there is not an invoice, so it is just a comparison of what is shown on the consignment note as to what the ‘screen free’ details will be. It is not a case of going back to the recipient in Australia and saying, ‘Can you now show me through your records actually how much you paid for these goods?’

The ACS did carry out a project on it called Operation Helium, where they tried to determine this. But their review process was flawed because they were checking the documents which were carried with the goods as against the goods themselves, rather than checking the documents with the goods with the importers’ record of payment, because that is the only way you could have verified it in any type of post-entry audit process. Is it occurring? Yes. To what level? Who knows.

**CHAIR**—But, if the payment systems take place out in cyberspace, how are they going to check?

**Mr Morris**—I suppose, at the end of the day, that is the difficulty of the process.

**CHAIR**—Is there a case to be made for worldwide free trade?

**Mr Morris**—There is. If you have that wand, I suggest you wave it, because I will not see it in my lifetime.

**Mr BEDDALL**—Worldwide trade is a great motivator for the US government.

**Mr ANTHONY**—Except if you want to export there.

**Mr Lovell**—I think Mr Clinton's comments were referring to freedom of trade, not free per se.

**Mr BEDDALL**—Freedom for the United States to trade with anyone they want to.

**Senator GIBSON**—The fishing tackle people were here earlier this morning. One of the suggestions was that, because of this threshold problem, and a lot of goods are coming in and not paying any sales tax or duty, perhaps there ought to be a user-pays fee on every item coming in, apart from gifts that are declared as such. Would you care to comment?

**Mr Fraser**—I think the point that Kent Heazlett made before is valid in that the systems we have at the moment allow for efficient processing of those sorts of transactions anyway. So you do not need to implement or impose any user charges as such to try to resolve that problem. It may be that, for example, if the population of consignments that are currently 'screen free' were to be entered in some other way or reported in some other way, you would then increase the population of consignments that are reported to Customs and therefore would also be able to reduce the per unit cost recovery charge that is currently imposed on entries.

**Mr Morris**—Were they suggesting a levy across the board, then the government would accrue a certain amount of money, or were they looking at a user charge?

**Senator GIBSON**—They were basically suggesting a user charge for everything coming in. So it is basically a transaction fee to be considered.

**Mr Heazlett**—There currently is a very small per consignment fee that is levied. It is only \$2.40 on what is termed 'screen free'. Whereas a formal customs entry is attracting on average \$26 or \$28 per entry. It is collected by Customs. It is broken up into a couple of components. Certainly that would be a real opportunity to bring down that user fee.

I cannot think of the figures for customs cost recovery, but I was at a meeting last week and there were eight major importers around the table. In that group \$1 million was collected in user fees from just eight importers. There is certainly some fairly substantial cost recovery going on within that customs area.

**Mr ANTHONY**—You mentioned earlier the simplified entry procedures and minimum value. It has been raised here before. Previous speakers here at our public hearings were talking about many things not being declared and that is why they are coming in. How would you classify minimum value? How do you go about having a

simplified entry procedure and even monitoring that?

**Mr Morris**—In terms of looking at minimum value threshold, the question is that it is excluding out of the system those types of things that should not be in the system. Screen free is fine in terms of commercial documents, contracts, papers and those types of issues. So they would automatically be screened out of the system and not part of an entry processing system.

Other things would be in the system, depending on the value threshold that you might wish to determine. The Canadian threshold is \$20. That is in effect because of the trading relationships with the United States. We would suggest that some sort of a minimum value like that would be acceptable and anything over and above that would go into an entry processing system. A minimalist approach of such data requirements as the name of the owner, the supplier, tariff classification of the goods, the value of the goods and the country of origin would allow the Australian Customs Service to do their profiling against those types of importations in terms of commodities, not only for duty and sales tax, but also for prohibited imports.

It could be done electronically through a very minimalist arrangement. The cost would be borne by industry. It would not be borne by the regulatory authority or government and, as such, the industry would fund the process. It might be \$2 for an informal style of entry. But it is a case of just screening out those which should be screened out and minimalists valued items and the rest go into the system or into the process.

We would suggest—and we have said in our submission there—that the revenue leakage could be anywhere. This is like the question: how long is a piece of string? We have done some statistics on it. It can be anywhere from \$18 million right through to \$35 million or \$50 million, depending on what the permutations and combinations are on duty and sales tax arrangements. At the end of the day, in terms of government revenue, that might not be a lot, but when it is going to cost the government little if anything to collect \$35 million to maintain equity in the process, it is a rather simple process.

One would suggest that people who are the suppliers of service in terms of the delivery of goods into Australia would say it is commercially not acceptable to go through that type of process and that it would create a impost on them to undertake that process. That might be correct, but we are continually told by various sectors of industry that they are at the forefront of electronic technology. Most, if not all, of the information provided on goods that are brought into this country by express carriers is downloaded from one country to another and is available to be translated in the country of importation at least—for example, for things that might come in from New Zealand—six to 10 hours before the aircraft arrives in this country.

So there is a screening process that could be undertaken. There is an entry process

that could be undertaken. But it would be a cost to that sector of the industry and that is a cost that probably that sector of industry does not wish to absorb.

**Mr Heazlett**—If I can just add to those comments, I guess the question you ask there is: how would we structure a system to handle a simplified method of processing? There are moves already under way to go to an EDI based entry processing system. We already have an EDI based system in place in Australia called EDIFICE, which is one of the customs entry processing methods. I think there is probably room to simplify the current system that we have for all customs entries. There is a lot of information there that is collected for other than customs purposes certainly, and a lot of those are for the ABS, for quarantine and a whole range of other instrumentalities that get in there.

There is room to simplify that for starters, and I am not here to speak for Customs, but there are already moves to do that. There are moves to talk about moving to a periodic reporting scenario with Customs and periodic payment—heaven forbid the Treasury guys getting their knickers in a knot, but that is what is being planned. That would accommodate all this. We would not have a problem because, basically, everything would be reported at the end of the day. There would be a mechanism to release the cargo up-front and report it and account for it at a monthly period or whatever it might be. So there are areas within that.

Remembering that most of the changes within the Customs' electronic systems have been funded externally by the importing and exporting community—and that would continue to be the case—there would be no impost upon government to have to do that. So there are methods there already, firstly, to accommodate it and, secondly, to simplify it.

**CHAIR**—What do you do about a grandmother who wants to send her grandchildren a book or any kind of present from Italy to Sydney? How does she electronically describe her goods, who she is and where they are going?

**Mr Heazlett**—I do not want to be trite but the books are not a problem because they are duty and sales tax free. Whatever it might be—a pair of pyjamas or whatever they might send them—

**CHAIR**—Let's say that it ends up being a laptop instead.

**Mr Morris**—That is the question that was asked before: would there be a threshold? I think if you threshold it at a certain value, you would be able to accommodate those types of issues.

**Mr ANTHONY**—What is the value you are proposing?

**Mr Morris**—We would propose that it would be a minimalist value, and I would suggest that it probably would not be more than at or about that type of figure.

**Mr ANTHONY**—Back to our piece of string.

**Mr Morris**—\$20 or \$50.

**Senator GIBSON**—But Customs have told us that chasing the stuff that is worth less than \$50 costs the taxpayer more than what we get back in.

**Mr Morris**—I would agree with them, and that is why you would look at something like that. What you are screening out of the system is a large percentage of items that you would not need in the system. In their surveys they found that something like five per cent of what was screened was out of the textile, clothing and footwear industry sector, which has a very high duty rate component on it. That has a market effect on the marketability of retailers and wholesalers in this country. Not only is there a revenue issue; there is also an issue here that relates to the ongoing ability of those people to supply employment in a certain industry. It is a complex equation.

We have numerous examples that we can support where things have been screened out of the process when, in fact, the value of the goods should maintain them being screened into the process. I can give you an example of \$US270,000 worth of aircraft parts and equipment being 'screen free'. That is not a real problem because there is no leakage to the Crown because they are free of customs duty and exempt sales tax. But, certainly, there is something like \$400,000 worth of statistical information that the ABS does not have on aircraft parts being imported from the United States.

**CHAIR**—Perhaps you did not understand my question. I was not as much concerned about the dollar value limit as about how grandmother gets access to the electronic system to get her stuff cleared?

**Mr Heazlett**—In our submission we actually stated that there should be public access to whatever the system is—whether that be Internet access, which is quite on the cards, whether that be that there be terminals available at airports, parcels posts, mail exchanges and all that sort of thing.

**CHAIR**—All over the world?

**Mr Heazlett**—We are talking about Australia, but that would be quite open. Certainly, I personally think there should be a by-law to cover that gift scenario; that, if grandma is sending something from England to Australia, from Lebanon to Australia or from wherever it might be—again, you would have to apply some formal limit—that be available.

**CHAIR**—Yes, but little Sophie does not know that her grandmother is going to send her anything anyway, and her grandmother has no access to any electronic means to describe what is in that parcel. She simply takes it to her post office and says, 'I want this



to go to Australia.' It arrives off the aircraft, goes through the mail exchange and there are no electronics anywhere.

**Mr Morris**—There is a bit of a difference there. I would try to distinguish between the express carriers industry and the parcels post industry. Where people send things by post there is a requirement for them to fill out a douane sticker to go on the goods to show the description and the value of the goods. That is a requirement under the postal agreements. At the end of the day, when gifts arrive in Australia, Customs have the opportunity to screen them free if they wish—to just roll them free, as they call it—or they can say, 'An assessment will be made on this,' and a Customs officer will assess the goods in terms of a PPC1, a PPC2 or a PPC6. If it is a PPC1 or a PPC2, you will pay the money at a post office; if it is a PPC6, it will be delivered to you at your front door by a person from Australia Post who says, 'Here are the goods. Give me \$5.60 which will go back to the Crown.'

It is not that type of process that you really need to attack. Some thought needs to be given to gifts and they could be screened out of the process. But there is a huge impact on the industry in Australia where a consignment of 900 shirts is brought into this country in one consolidation and each shirt is worth \$45 and falls under the threshold but, because they are separate contracts at law, they are sent out, they arrive and then they are broken down and distributed to all the people in Australia through a mailing process.

**Mr ANTHONY**—Is this one consignment coming in?

**Mr Morris**—It is one consolidation made up of 150, 300 or 600 separate contracts at law. Because I am buying from you on the Internet, under the Customs Act that is a separate contract. It is not a consolidated contract; it is a distributional process.

**Mr ANTHONY**—So there are 400 contracts for 400 shirts?

**Mr Morris**—Yes, on one consolidation.

**Mr ANTHONY**—So it is screen free?

**Mr Morris**—It would be screen free because each one is a separate contract that falls below the value of the goods.

**Mr Heazlett**—Those sorts of numbers are startling, but in a single consolidation into Sydney in recent months there were 5,000 house airway bills on the consolidation, so 5,000 consignments were screen free.

**Mr BEDDALL**—At what value?

**Mr Heazlett**—It was mail order stuff under the threshold, but all from one

supplier. Basically, the mail order house imported them into Australia. Who the owner is at that time is a question that Customs would need to sort out, but they are all consigned to you and me—all of us, 5,000 of us—in various parts of Australia.

**Mr BEDDALL**—They come in and they are distributed to individual addresses from here, not from overseas?

**Mr Lovell**—They are distributive of one freight forwarder. It took Customs 32 hours to screen those documents because they had to screen each line of that shipment.

**Mr Heazlett**—But that was set up. That was a commercial utilisation of the current system and they have not broken the law.

**Mr Morris**—We should be quite specific here so that we do not give you the wrong impression. It is done by freight forwarding consolidations; it has nothing to do with the express carriers industry, who may or may not go through the same process. It is certainly happening in terms of freight forwarding consolidations and deconsolidations in Australia from New Zealand and from elsewhere.

**Mr ANTHONY**—Can you distinguish between freight forwarders and express carriers?

**Mr Morris**—We probably do not, because they all carry cargo.

**Mr ANTHONY**—I do not understand the difference. You are making a difference but there is no difference.

**Mr Heazlett**—There has been an intentional perception that there is a difference, but there isn't. Whether we are a customs broker, a freight forwarder or an integrator, we all carry organised freight into and out of Australia. I guess the integrators and the express couriers are the one thing. Let us be frank: we are talking about the DHLs, the UPs and the FedExes of this world—and there is a myriad of others.

**Mr ANTHONY**—As the freight forwarders?

**Mr Heazlett**—As the integrators or the express couriers. If you just want examples of freight forwarders, you are talking about the Air Express Internationals, the Burlingtons, the Circles, the Emerys and a myriad of others. From where we sit there is no damn difference. There has been a worldwide push by the express courier and integrator industry to have a perception that they are different. They are in no way different. In some cases, they own their aircraft; in some cases, the freight forwarders own their own aircraft. But, whether they are using external carriers or their own devices to bring their cargo into Australia, they are pretty much of a muchness. There is no difference.

They seek to differentiate for their own purposes, and they have done it exceptionally well. They have marketed it well. They have done it on the world stage and they are doing it here in Australia—especially with the likes of the screen-free system which facilitates their business. If they do not have to enter the cargo then it is very easy; if they do, then it is an impost upon them to do it, but every other importer in Australia is having to do the same thing. The differentiation, as we pointed out in our equity scenario in the submission, is the difference between the \$250 piece of equipment coming in by itself and 10 of them coming in in a normal consignment.

**Mr BEDDALL**—This probably goes to the core of the whole inquiry. Now that commerce will expand on the Internet, the growth of that particular industry will come. Rather than a manufacturer exporting 1,000 shirts to Australia to be sold in David Jones, they will sell them on the Internet. Therefore, the whole system of tariff just does not exist any more, and that is really the core element of what the inquiry is about: how you address the drain on revenue that will come from that. That is a very legal thing to address, too. Is it being addressed in any other country? We are obviously not the only country in the world that is worried about a revenue drain.

**Mr Lovell**—No, all customs organisations are well aware of this problem. Just to add to Kent's statement, because I think it is important, there is a difference, without disagreeing with my colleague. The integrated operator normally would have their own truck, their own aircraft, their own tracking system and they offer a price for a product from one origin to one destination. The freight forwarder would normally consolidate goods from many different suppliers, send them to a destination and they are then distributed.

We have one difference and that is the example Kent gave of the freight forwarder who organised the bulk Internet shipment into Australia. They are not what you would call an express operator because those shipments were not express. The people they were going to did not want them urgently; they just wanted them cheaply. So the express operator would not normally target that sort of business. They will get it because of the service they provide: easy, one price, door-to-door. But we have a new animal coming into the system and that is the bulk Internet distributor.

**Mr Heazlett**—Senator Gibson raised a point before about the statement by Customs—I have heard it before and I am sure they have run it again—as to the perceived cost of recovering the revenue under the \$50 mark. Currently, any duties and sales tax that are paid on imports are funnelled through a group of customs brokers and freight forwarders that are numbered in the high hundreds. For Customs to collect \$30 million, I would think they might have to spend \$2 million per annum to fix their system to collect it. Once it is set up, the mechanism is in place, and I disagree with their statement that it is going to cost them too much to recover that sort of money. It is not they who are going to do the work.

**Senator GIBSON**—Just to follow on from that, it was interesting that you should raise that because—and Mr Morris mentioned the Canadian threshold of \$20—in this week's *Economist*, they pat Canada on the back. It says:

One of the few countries that has tried in a serious way to cut these costs—

duties and stuff—

. . . has set up a special scheme to allow recognised carriers to take responsibility for collecting taxes and duties themselves on packages worth less than \$1,600. An online merchant includes taxes and customs duties on the customer's bill, and passes them on to the carrier. Once a month, the carrier settles up with the government. Not only are orders now delivered three times as fast and much more cheaply, but this 'privatisation' has halved the cost to government of processing small shipments.

**Mr Heazlett**—If I could comment on that: you are right, the Australian Customs Service is certainly addressing that right now. We have a client who is involved in what they term their partnerships arrangements, whereby they are pretty well convinced that in scenarios where they have a high level of current compliance, have done an audit and have a pretty good understanding of their future compliance, they are going to say, 'Listen, guys. We don't want to collect that transaction by transaction. We don't want you to report the cargo transaction by transaction. We want you to say at the end of the month, "I've had 50 shipments in the month."'

**Senator GIBSON**—It is saying the same thing, basically.

**Mr Heazlett**—Yes, exactly, and pay all those on a given day of the month and balance it up.

**Senator GIBSON**—Can you see that system applying throughout your industry?

**Mr Heazlett**—It is certainly going to take some time, but, yes, it could. It is not going to apply to the mum or the grandmother who is sending one shipment, and it certainly will not apply across the board. But regular importers will certainly be able to avail themselves of that. That in itself will reduce the demand on customs resources.

**CHAIR**—With respect, that will not do anything about addressing the bookshop Web site in Cleveland, Ohio, or wherever it is, that sends 100,000 books a year to Australia in single packages.

**Mr Heazlett**—No, it will not. We are talking about resources and cutting costs as far as the importing process is concerned. It will not address that single importation scenario at all, because those persons importing them will not avail themselves of a periodic report. Certainly, there needs to be another mechanism to do that. The current system or an amended system on the current basis could accommodate that.

**Mr BEDDALL**—The books will all be coming by post, seairmail mostly, otherwise there is no comparison if you airfreight a book. The books come in a square box. It is fairly obvious what they are. The post system can pick that up. Customs can pick that up at the postal links, as they do with big packages. It is intercepted and they look for revenue loss. If you have 100,000 books coming in, it would be fairly obvious, I would imagine.

**Mr Morris**—I think also—as I was just discussing with my colleague here—it is a case of getting a category of items. There is no revenue problem for the Crown in terms of books. They are free of duty and exempt from sales tax. So you can put things in there and screen out. So it just brings you back to core issues that you need to keep addressing. There is the textile, clothing and footwear industry, computer parts, cassettes and software. There is a huge market. You can pick up Microsoft 97 from the States and have it sent to you basically for about \$150 cheaper than you can buy it in Australia.

**Mr BEDDALL**—Can you download it yet?

**Mr Lovell**—That is the new problem, downloading.

**Mr Morris**—But the statistics that came out cover what is in there, such as the textile clothing and footwear industry, photographic materials, motor vehicle parts, JIT parts for equipment, personal effects, toys, et cetera. People are not going to use a very expensive process to bring something into this country that has no value to it. Why would you pay, let us say, \$100 to use an express carrier to bring a parcel into Australia unless it is a document or a contract that you need to get here quickly?

Why would you use it to bring something over here that has no commercial value? I just cannot understand that process. Why would you use airfreight? You would use the post. You can get it here within a maximum of five or six weeks from wherever it is coming from. You can use express post and get it here quicker and cheaper. This is a service driven industry in terms of express carriers, but certain things can certainly be taken out of the process, which would leave us a core. Then in that core, you have people who are regular shippers into this country, like companies. Then you have got the people who ship irregularly to their friends or relatives, whatever the case may be, or maybe purchasers on the Internet.

When a DHL senior executive did a presentation of the DHL position at a New Zealand conference, they said in Malaysia they have 28,000 customers. You could bet that out of those 28,000 customers there would be only 1,000 who are regular users of the service, that is, weekly. Of the rest of them, they might use it once, twice, three or five times a year. You can differentiate. You can go through the process. It is just developing the process, if you wish to develop the process.

We have been involved with the Australian Customs Service on this issue for over

four years and have been trying to suggest to them the equity process and the revenue process. It is not a cost to the Crown. It will be picked up by industry. Is it an extra cost to small to medium enterprises? Perhaps not at the end of the day, because we could lower the cost structure in terms of going through the clearance process.

We come back to the express carriers and the question: how about the person in Italy who sends a parcel to their friends in Australia? If they use the express carriers, they have given them tacit authority to clear the goods in Australia anyhow. Therefore, when they sign the consignment note, that person could go through the clearance process here and charge them X dollars for the service fee to carry it from Italy to Australia. Inherent in that price would be a clearance cost in Australia which would then be transferred to the Crown.

If there is revenue in terms of customs duty and sale tax payable, that could be a separate payment. When the person goes out to deliver the parcel, they could say, 'You owe us \$16 because we paid that to the government on your behalf.' The enterprises would say, 'We do not want our delivery persons going out there collecting money. We are happy to write it off.' In that case, it is a commercial decision. What they should then do is work out what the write-offs are, add it back into their service charge, recover it that way and pay the government what is required in terms of duty or tax, and say, 'We will deliver it to the person in Australia, all cost charges included.'

**Mr Fraser**—We are talking too in terms of the existing duty and tax regimes. I think we also need to think about the possibility of some kind of broad-based consumption tax and what impact that would have in this area. Certainly, as far as commercial entities using these sorts of consignment arrangements are concerned, there probably would not be a problem with the GST because of the credit arrangements that need to flow through. But as far as individuals are concerned, it would be a problem and there would be perhaps significant revenue leakage at the time of entry because you would not know about those transactions; there is no database.

**CHAIR**—So you are really suggesting that we lower the screen free limit, not raise it?

**Mr Morris**—For those that are screened into the process and not screened out.

**Senator GIBSON**—And be much more selective in who to tackle and what to tackle?

**CHAIR**—The Fishing Tackle Association will love you!

**Mr Morris**—I am sure they would. But at the end of the day we are saying that is what we see in the equity process. It is interesting. If a parcel is worth \$300, I have to pay duty and tax on it. But if it is worth \$249, I probably do not. You know it is going to be

always \$249.

**Mr BEDDALL**—My suggestion was a gradual fee, but I could not get him to take it up.

**Senator GIBSON**—If we do bring in the broad-based consumption tax, from your perspective do you see it as an advantage for commerce in Australia, for your businesses?

**Mr Lovell**—No, not so much for our businesses.

**Mr Morris**—I suppose we could ask people who are employed in business. We do not necessarily see that there will be any more business opportunities flowing to us. Are the express carriers going to provide to us the customs clearance process? I do not think so. I think the express carriers have within their own organisations customs clearance facilities, licensed customs brokers, so they will maintain that in-house; that will be another service they provide. So we do not see it as a business opportunity. What we are saying is that it is a total equity process here.

**Mr Fraser**—It is an equity issue. The other issue is the integrity of the data that needs to be presented. We believe that there are shortcomings at the moment in the integrity of the data in relation to imports, particularly those that are being screen free. I have some examples here, if the committee wishes to see them. These examples illustrate that there are some goods which, on the face of it, should have been screen free and will require to be entered, and others that should have been entered but were in fact screen free.

**Mr Morris**—If I can make one point just on the side there. In the main, with customs duties coming down, it is not a leakage in terms of customs duty, except for the textiles, clothing and footwear industry; it is a tax issue. That is where the bulk of the revenue is leaking from: sales tax. With a GST, it will be even enhanced.

**Mr BEDDALL**—But it will be an incentive to purchase overseas if there is a GST domestic. So you actually exacerbate the problem.

**Mr Fraser**—Yes.

**Mr Morris**—If you look at it in terms of how large Australian retailers will react to this, I would suggest that large retailers in Australia will set up the same opportunities. You will go into their store. You will go through their catalogue. You will do it on the Internet. You will clock in, you will pay for it in the Internet. The goods will be sent to you from China—or wherever—to your home address. You will look at it and say, ‘I don’t like this one.’ So you will take it back to the store and say, ‘I don’t like this.’ Our refund policy is certainly money credited back to your account. The retailer then says, ‘I will sell this off at a bargain bin price.’ So no-one loses in terms of the sale opportunities.

The number of people who might be employed by those retailers, especially the part-time employees, will go down because they do not need to be there any more. The only thing to be lost is the sales tax and the revenue issue, and this will happen. They will respond to this Internet trading by providing their own Internet sites.

**Mr BEDDALL**—That is right, otherwise they would go broke.

**Mr Morris**—And so the large retailers will have no problems. The small retailers will because they will not be able to play in this game.

**Senator GIBSON**—Mr Fraser, I think those examples would be of interest to the committee.

**Mr Fraser**—Yes, I will just hand them up.

**Mr Heazlett**—We can hand them up later on. As to the examples, the way that the system currently works is that Customs has an officer sitting in front of a screen who has a look at some very, very basic information and makes a decision as to whether he screens that free. That is based on what may be on the manifest or on the face of the airway bill or whatever document you want to call it. In this particular instance, there is a currency shown as Indian rupees on the document and it shows a value of 2,000. In fact, it was \$US2,000—a simple mistake—and, because of that lack of information, a decision was made to screen it free. It could have been \$US200,000, for all intents and purposes. So those are the areas.

We have had a bone of contention with Customs for a long time. They say, ‘No, we accept the information that’s on there and that’s where we base our information.’ Quite to the contrary, AQIS have moved away from accepting manifests and shipping documentation as being the basis for their assessments. They want further information, and that usually flows from having profiles matched to a tariff classification. That is the only way they know what the goods are. What is the cargo—machine parts or books? A cargo of books is always a good one; you know it is duty free and sales tax exempt. A lot of books come into this country.

**CHAIR**—The Fishing Tackle Association gave us an example this morning of an invoice listing 38 separate items—from the United States to Australia—paid for by credit card with a total value of roughly \$685, but the consignment note—commercial invoice, air waybill—says it is one fishing tackle worth \$65.

**Mr Morris**—A clerical error!

**CHAIR**—That is a big clerical error.

**Mr Morris**—The little finger missed a digit.



**Mr Fraser**—That is an example of the point I was making about the integrity of the data.

**Mr Lovell**—It is also critical to understand who completes the shipping documentation.

**CHAIR**—What do you do about that?

**Mr Lovell**—Sometimes the shipping documentation is completed by the shipper, who may wish to deliberately defraud the customs department in the country of destination because they are sending it to a friend. Alternatively, the freight forwarder who completes this documentation has to be trained because they are looking not just for the value of the goods commercially, but also for what the goods are in terms of dangerous goods and also those that might breach the aviation security regulations. So we have two very different animals: we have the trained freight forwarder and we have the shipper who just fills out the con note, and the carrier goes in and picks up the goods and treats that declaration as gospel.

**Mr BEDDALL**—In the evidence that was given in this particular case, that was what they were saying they would do for you—that they will invoice you at a figure that does not attract duty, and that is the way they were selling.

**CHAIR**—They gave us another one about a company in Singapore. It says:

As for the duty fees, we would lower the prices of the order by declaring a false invoice.

**Mr Morris**—They put that in writing?

**CHAIR**—We have got it in writing; that is a fact!

**Mr Morris**—I do not think it is necessarily fair to tailor the whole of the screen free issue with those types of things. But, yes, it is there; it is relevant. There would not be a problem in, say, having a Web site and, if you were exporting goods to Australia, when you go in there to look for a purchase from Australia, saying, ‘Make sure that you put them under the \$250 threshold.’ It is just an information issue so that they do not attract duty and taxes. And the purchaser would say, ‘That’s fine. I’ll purchase under \$250.’ And that is correct at law and that process will continue.

**Mr BEDDALL**—The other one we got this morning which comes under that point is that for a \$2,000, order they will send 11 consignments.

**Mr Morris**—What is the cost of sending those consignments? People would have to do their homework to save. For instance, with sales tax at 22 per cent on \$1,000 I am looking at \$250. Each consignment will cost me \$20 extra. It is marginal as to whether I

make it. At the end of the day this process is going to move out further and further with Internet trading. If you are going to buy from Sears Roebuck or I Magnum in the United States—you just go into the catalogue and you buy—they have got a flat rate with service providers to carry this to Australia for X amount of dollars. If you and I went in and bought it off the street it might cost us \$55; for them it is only \$5. They can make it very competitive for people to buy on the Internet.

There was a large mail-order catalogue company in Australia called Lands End. They had very good products. They have just returned to the United States. I have looked at their catalogues. I know my size, fittings and all of those types of things and I see no reason why I should not be buying from their mail-order catalogue and having those goods sent into this country. This will exacerbate in years to come.

**Mr BEDDALL**—I think that rather than letting consignments be sent from the point of source, it is more likely, as the example you gave us, that as the Internet grows, it will be sent in bulk. It is non-time critical.

**Mr Morris**—You are right.

**Mr BEDDALL**—And distributed in Australia. That is the issue.

**Mr Morris**—Most people who purchase on the Internet do not expect it to be time critical.

**Mr BEDDALL**—No.

**Mr Morris**—If they know it will be delivered within 30 days, they are happy with that. People are using express carriers industry, and it is a service that they provide. We guarantee on-time delivery and that is what you pay for. As I said, it is not necessarily that we are picking on the express carriers industry, it is just that so much is carried by the express carriers industry at this time. It will continue to grow in terms of screen-free issues, but the consolidation issue will continue to grow also.

If you look at some of the information that was provided to you, on those waybills for example, and you look at the one that has the rupee issue on it—which is 2400—you would call into question, if you were screening this, that this consignment is 156 kilos. To carry 156 kilos by airfreight out of India, the best rate that you could get would probably be something like \$5 or \$6 a kilo. We are carrying \$600 or \$700 worth of airfreight here but it is shown as a value of 2,400 rupees. That just does not ring true in a commercial sense. Screeners should be able to go through this process but, when you consider the amount, we are talking about 1½ million of these and they are human beings trying to screen them—it is no good. You need an electronic process, where data is being put in, to screen it.

**Mr BEDDALL**—Has this change that is coming from the Internet forced a rethink amongst your members about whether they should actually be into acting as a distribution point as well as being a customs broker?

**Mr Morris**—I think, in terms of consolidation, they do act as a clearance point for airfreight forwarders who are freight forwarders and customs brokers. Even though there are two associations here, we are one association in real terms; in looking after the welfare of our members. They are customs brokers freight forwarders. Yes, there is a process there. They are part of that process. They can take on those clients who do those consolidations and deconsolidations.

There is no extra market for the express carriers industry. Express carriers operate in this country. They have their own customs clearance processes built into their business. So it is not going to be money that goes outside into the industry. This industry is subject to contraction and will be contracting up to the year 2000, and to changing processes, the way of doing business, in terms of intercontinental activity with partners overseas. All of this will have an effect on this industry.

**Mr Lovell**—I ought to add that the express carries and the customs brokers are also members of our association, as are the distribution forwarders, which Kent referred to earlier. We understand their concerns.

**Mr BEDDALL**—I just thought that some of your members might be trying to expand their businesses by going into some of these newer areas.

**Mr Lovell**—We are always looking for new areas.

**Mr ANTHONY**—Finally, and it was raised beforehand, what do you do with software that can be downloaded or CDs that can come across the Internet? Do we just give up on that area?

**Mr Lovell**—The music industry is very concerned about that, of course. That is a very good question. There is nothing we can do in the physical sense. The physical barrier is gone so I guess that is up to the government. It is out of our industry.

**Mr Fraser**—As far as software is concerned it is not really an issue in revenue terms at the moment because software is free of customs duty and sales tax exempt. Once again, if we get a broad-based consumption tax, it becomes an issue.

**Mr Morris**—There is also the issue that people make money out of selling software that provides tax arrangements for this country and provides employment for this country. The issue that we have at the moment in terms of the positions of small to medium enterprises will be exacerbated as this Internet trading moves on. If the government has decided that there should be a level of protection built into the process or

a level of revenue received from the process, that should be protected—in the most cost effective way—as long as it does not put a cost on industry. But most ways of doing business with government put a cost on industry. Industry absorbs the cost anyhow. The customs entry procedural process at the moment creates \$34 worth of cost just to create a customs entry before you do anything else. Therefore, that is just part of the process of doing business.

**Mr BEDDALL**—It is interesting that the Finance model for a GST has got to factor in that a whole lot of this stuff will now move away from ‘Australian bought’ to ‘Internet produced’ and the revenue drain that will come out of that.

**Mr Fraser**—Exactly.

**Mr BEDDALL**—I have not seen any economic models that do that.

**CHAIR**—All done, gentlemen? Thank you very much for both your submission and for talking to us today. It was fascinating. I can assure you that we have been enlightened. Is it the wish of the committee that the document entitled *Air Waybill—Concorde International—Mumbai* presented by the Customs Brokers Association of Australia be taken as evidence and included in the committee’s record as an exhibit? There being no objection, it is so ordered.

**Mr Morris**—Before I go, could I hand up a discussion paper on the air waybill. It just supports a submission in the past. It goes back to our workings with the Australian Customs Service in 1994 and references some of the issues that will come out of the discussion papers. It is more background to what we have put in there.

**CHAIR**—Terrific. Did we also agree to have that paper taken as evidence? It is so ordered. Thank you.

[11.44 a.m.]

**SHETLIFFE, Mr David Reginald, Director, Retail Business, Australian Retailers Association, 20 York St, Sydney, New South Wales 2000**

**CHAIR**—I now welcome the representative of the Australian Retailers Association to today's hearings. We have received your submission. We thank you for it. Would you like to make a brief opening statement before we start to ask questions?

**Mr Shetliffe**—Most of my submission and the interests of my members are about the increase in competition that could open up as a consequence of people being able to source product direct from overseas in the global marketplace. Most of our submission has focused on that, but there are a number of other issues that are also relevant to our constituency and to this inquiry.

The first thing that needs to be said—and this has certainly come up in all the discussions I have had on this issue in our association and elsewhere—is that in dealing with electronic commerce we are dealing with something that could totally change the way in which we think about doing business and the way in which business is done. It is not just a different form of doing existing business; it has the potential to totally change the way in which we do our business.

One of the major challenges we have is that we have no idea how big this is going to get in terms of consumers buying directly via the Internet, whether from Australian suppliers or from international suppliers. There are enormous differences in the amount estimated for that. The challenge is that, while imports of these products are relatively small, people can turn a bit of a blind eye to it and let it happen because the cost of policing it from a tax or other point of view tends to be too high in relation to the revenues to be sought. But it seems to me that, once it gets to be large, one really has to look at that very closely. Obviously, when you have a tax system and other regulatory systems in Australia that retailers within Australia have to comply with and they are competing in the global marketplace, where those things may or may not be relevant, it starts to raise some important competition issues for retailers, both large and small.

What we do know, though, is that it is going to increase. All the evidence that I have seen to date suggests that the amount of trading that is done on the Internet by consumers is going to increase—and increase substantially. This will be driven both by technology changes as well as by the population becoming more and more computer literate over the next few years.

Some products are more susceptible than others to Internet trading at the moment. There seem to be a number of characteristics that relate to those products. First of all, in terms of physical size, they tend to be relatively small because the cost of freight, therefore, is not a major factor. They tend to have a relatively high value in relation to

that size; they have a high regime of sales tax or duty imposed on them that is not paid on import because of the commercial thresholds that exist; or there is a very wide range of product.

That is why things like books, for example, even though there is not necessarily a sales tax issue, have been so successful as products on the Internet. People find they can access a very much wider range of books or rare books that they cannot buy locally. All the evidence we have suggests that one can have a book delivered to Australia from somebody like Amazon.com in the States more quickly and cheaply than if they had gone into an Australian book store and asked to have it ordered on their behalf. So those challenges are there and clearly retailers are going to have to learn to compete with that. But, where there are tax or regulatory disadvantages, we think that creates an unfair situation for retailers.

The other potential that could happen as a consequence of this is disintermediation of the retailer themselves; that is, manufacturers and major suppliers may supply direct to consumers and leave the retailer out of the distribution chain. At the moment, it appears that only manufacturers of very high global brand names, such as Levi Strauss, for example, are attempting to do this. They are imposing supply contracts on retailers that prevent them from being able to sell their products via the Internet. Levi Strauss wish to keep that market to themselves. So there is a whole range of different issues starting to emerge around that.

One of the major challenges when one starts getting into the question of regulation is that, on the advice we have had, the regulation that applies for these kinds of transactions is that in which the purchaser is acquiring the product. It raises issues, therefore, in terms of advertising. If you regard an Internet site as a form of advertising, as it clearly is, then there are all sorts of issues that flow from that, because around the world there is a whole raft of different advertising rules and regulations, and both Australian businesses and other businesses are subject to those rules. The challenge, however, is how you police and regulate it to ensure that you are complying when the company that is putting the site onto the Web is not based in the country where the purchase is being made. So there is a real challenge there.

There is a whole range of issues associated with the way in which business can be carried out. One is already reading in the press examples of scams that are emerging—of issues involving companies that do not really exist. Tax havens and all those kinds of things clearly are opened up with the global marketplace that Internet trading provides.

At the ARA we have been doing a lot of work in this area. We are very concerned with electronic commerce not only in terms of marketing consumers but also in the supply chain. One of the positive outcomes of this, of course, is that retailers—large and small—can more easily access the global marketplace for goods that they can, in turn, sell. There are opportunities for retailers in rural areas to be more competitive, to access supplies at

better rates and display product to local consumers better than they currently can. By the same token, there are opportunities for city retailers to sell directly into country areas. Country consumers are likely to be beneficiaries of this kind of trade, and it will greatly increase the range of goods that they can get.

We have developed our own Web site which is about to be launched. One of the things we have done is put a retailer directory into it. For a retailer to have their name incorporated in that directory they will have to comply with a code of practice that we are developing at the moment in relation to things like delivery time, breakages, returns, privacy issues, faulty goods, consumer education—all those kinds of things. So if somebody is wanting to buy a product on the Internet either from within Australia or elsewhere then the fact that the retailer is on that list is a check for them to ensure that it is a real, reputable trader they are dealing with that complies with a code of practice. We are doing a lot of work on that.

Finally, one of the things that strikes us is that, in regard to electronic commerce in its broadest sense, which is growing extremely rapidly around the world, government really needs to take, I think, a holistic and strategic view of the policy responses that are going to be needed. One is already starting to see reports come out from the Department of Foreign Affairs and Trade, the Taxation Office and the ACCC all dealing with the same kinds of issues, all repeating the same kinds of challenges. It seems to me that we have to get a much more strategic framework for dealing with this issue because it cuts across so many of the ways in which we historically do business. That would certainly be, and has been, one of our pleas to government—that there be some mechanism put in place where the whole issue of electronic commerce can be dealt with on a whole of government basis.

One of the challenges we also have as an association is to educate our members as to not only the threats but also the opportunities that electronic commerce opens up for them. The technology is becoming cheaper. Smaller and smaller retailers are able to start accessing this and we are setting up mechanisms within our association to try to assist that process and ensure that, to the extent that there are opportunities for retailers, they are able to take advantage of it. That is all that I wish to say by way opening statement.

**CHAIR**—Yes, thank you for that, David. Is Coles Myer a member of your association? As I recall, Myer Direct took over the operations of Lands End in Australia.

**Mr Shetliffe**—That is right.

**CHAIR**—A few months ago or a year ago or whatever it was. What is to stop Myer Direct from taking orders over the Internet from 5,000 customers for 5,000 shirts, sending an order to China, having them made and bringing them back in in one consolidated shipment as being for 5,000 individual Australian clients and bypassing the ‘screen free’ limits?

**Mr Shetliffe**—I suspect there is nothing to stop them doing that if they chose to do it. I am not sure that is how they would operate because the time from order to supply would probably be too long if you had to go down that path. But, sure, that is the kind of opportunity that could open up.

**Senator GIBSON**—As a matter of fact, you mention in the submission ‘quantity of businesses to grow from, say, 10 per cent of retail sales—\$1.2 billion per annum’. Was that the correct number? What is aggregate retail sales?

**Mr Shetliffe**—\$120 billion per year.

**Senator GIBSON**—\$120 billion?

**Mr Shetliffe**—So it is actually \$12 billion, isn’t it?

**Senator GIBSON**—So it should be \$12 billion.

**Mr BEDDALL**—The Chairman raised the issue about the Chinese shirts, and it is an issue that we have raised before. With the movement towards some form of tax reform and some form of a broader consumption based tax system, isn’t that going to be a further incentive for people to shop offshore because of the fact that, under current thresholds, these items will be under the limits? Doesn’t that present a further problem for your association?

**Mr Shetliffe**—If you assume, firstly, that no tax will be paid on those that are under those threshold limits and, secondly, that some goods that are currently not taxed will be taxed then, quite clearly, it opens up a broader range of incentive for people to buy offshore. Yes, you are correct.

**Mr BEDDALL**—There was also a proposition put forward that there would be an incentive in many ways for members of the association. For example, if I am going to buy a shirt on the Internet, then there is incentive for Coles Myers or Tony Barlow or anyone to have a Web site terminal in the shop so that, I as a customer can go into the shop and order that shirt and for it to be delivered offshore. Should it not be the right colour or whatever, it can be brought back, exchanged or credited to the account and the only person who misses in that whole loop is the tax office. You will all have to compete and your members will have to compete.

**Mr Shetliffe**—Absolutely. In fact, one of the advantages of this kind of trading is that a small trader can greatly increase the range of products it can offer by having a kiosk terminal within their store and being able to display a range of products that, financially, they would not be able to hold in stock. The systems that are going to flow in terms of the supply chain using electronic commerce and the capacity of retailers to know what is in stock in particular warehouses at any given point of time absolutely raises the



possibility for retailers to be able to access that.

The downside, of course, is that if it is coming in direct from China one has to be careful because people do want things immediately, and there is a delay in that. That is going to be a natural barrier to product coming in directly to the consumer. People have to wait for 10 days or so whereas, often, people want to go into a shop, buy something and walk out the door with it because it is mum's birthday tomorrow or they need the shirt for the dinner tomorrow night. So, to that extent, there is a natural barrier. But I agree that there is also a lot of opportunity for people to do that sort of thing, which could greatly affect the tax office in terms of those products that carry duty or sales tax.

**Mr BEDDALL**—Also, your association—and I will finish on this point—fought about the whole nature of retailing. You will virtually have a virtual reality shop. Basically all you have to provide is a screen and you can retail anything from clothing to jewellery through to basically one of these cybercaps.

**Mr Shetliffe**—Absolutely. As I said in my opening comment, the way in which we do business in the future need not necessarily be the way we do business at the moment. There are already shops in Sydney, as I understand it, where people are putting kiosks in. They are carrying a sample range of products and then most of the display is done by way of kiosk. This has the effect of greatly reducing the amount of space that they have to occupy and therefore the rent they have to pay, which as the honourable member knows is another issue of concern to our association. But people are finding that those kinds of models are being experimented with at the moment.

I guess, at the end of the day, it is going to be how much consumers will take it up, and that is the big unknown in this whole area. The highest figure I have seen quoted in overseas conferences and things that I have been to over the last 12 months is 30 per cent of retail sales. But 30 per cent of retail sales is still a very large number and would totally change the way in which retailing operates in Australia. You just contemplate taking 40 per cent of retail sales out of traditional shops and the investment in shopping centres and infrastructure that currently exists. The potential impact of that is huge.

I am not saying that it is going to be 30 per cent. I am not saying it is going to be five per cent. What I am saying is that it is going to be bigger than it is now and it is likely to continue to grow over the next few years. The kids coming out of schools and universities these days are much more sophisticated when it comes to this kind of technology and much more comfortable with it. The technology itself is improving in terms of the bandwidths and the speed with which you can work on the Internet and that kind of thing. It is inevitable that more and more people are going to start selling on the Internet.

Australian retailers have been quite slow to take it up. There is a bit of work going on now from a number of retailers, both large and small, but they really have not got

serious about it yet. What is also interesting in the United States is that a lot of the very successful businesses that are selling over the Internet have not had their origins as retailers. Amazon.com was not a retailer. It is a brand new business set up specifically to do the task it was doing. Peapod, which is the large supermarket group, was not a retailer. It has gone into partnership with a supermarket retailer, but in itself it was not historically a retailer.

The interesting challenge for retailers is to get their mind-set around this kind of merchandising as opposed to their traditional kind of merchandising. What I mean by that is that the thing the Internet allows people to do is to personalise the shopping. The offer that is made to you as a customer is very much about the sorts of things you are interested in and the sorts of things you have historically purchased. It will be an offer to David Shetliffe the individual in terms of the things he is interested in. So, if there is a special on golf clubs or golf balls or something like that and I happen to be a golfer, that is what will be presented to me as the offer—by name, to me. That kind of retailing is foreign to traditional retailers who tend to be, even though they may be in a niche market, still mass merchants.

The whole thinking of the way in which marketing people have to think about how this operates is very different from the way retailers have historically done their business and very different from the way in which suppliers have done their business—the sorts of examples of seamless limits between a supplier's catalogue and a kiosk in a store, or somebody's home computer being able to access a very much wider range of products, or the proposition that people will go into a traditional store, have a look at the range that is there, decide that a Van Heusen size 43 shirt is the appropriate shirt that they like and so on and then go home and shop around to buy it on the Internet. Those things are all going to happen; there is no question about that.

Inasmuch as product is coming in from overseas direct and avoiding taxes and duties that are applicable in Australia, it is going to put Australian retailers at a substantial disadvantage. It seems to me that, irrespective of what we do with tax reform, we are going to have to make sure that, in any tax reform process, this is recognised and mechanisms are put in place to try to capture those goods that come in. I do not think the commercial thresholds at their current level are sustainable in an Internet environment.

**CHAIR**—Up or down?

**Mr Shetliffe**—They have to go down.

**Mr GRIFFIN**—Could you expand on that and the reasons why?

**Mr Shetliffe**—It seems to me that the commercial thresholds were put in place on the proposition that a few people were occasionally buying stuff overseas or having it sent to them as gifts and so on and so forth, and it was a very minor part of our commercial

trade. Retailers, therefore, took the view, 'Look, it is only a very small amount of product and it is not really affecting the \$120 billion of retail sales that we are doing, so we will tolerate it.'

If you follow the logic of people seeing competitive advantage in being able to buy product offshore and becoming much more comfortable in doing that and we allow the commercial thresholds to continue—that is, sitting around \$200 or wherever they are—then, potentially, the number of those very small purchases is going to explode. That is going to cost jobs in Australia and it is going to hurt the retail industry for just the kinds of examples that I was giving to Mr Beddall. People will go and shop, have a look at what is there and then walk away and go and buy it cheaper on the Internet to avoid tax. We do not mind people buying things cheaper if the supply chain is cheaper—that is what competition is about—but we do object to people being able to buy things cheaper because they are suffering from an advantage in relation to a tax regime.

**Mr GRIFFIN**—How low would you go?

**Mr Shetliffe**—Ideally, zero.

**Senator WATSON**—How much trade do you think the retail sector will lose if nothing is done on the tax line over the next 10 years?

**Mr Shetliffe**—It is almost impossible to tell. But if, again taking up the scenario that Mr Beddall was putting—

**Senator WATSON**—There would be opportunities for some and downsides for others, of course.

**Mr Shetliffe**—The reason CDs have been so popular as a product that people have bought over the Internet—and all the evidence I have is that it is quite large—is because it is a very high sales tax product in Australia and it is a small product.

**CHAIR**—Does it have anything to do with choice and availability?

**Mr Shetliffe**—It has a little bit to do with choice and availability, but I would suggest it is primarily to do with price. If you are paying \$30 for something in Australia and you can get it over the Internet for 15 bucks, there is a pretty strong incentive to do that. My point is that the Internet opens up the chance for a very much greater number of small transactions to take place—to import product into Australia direct and bypass the traditional mechanisms of the way product comes in now, which is in a consolidated form. It is either brought in by a wholesaler-importer or it is brought in by a retailer direct, and it comes in by the container load. It is relatively easy to manage that, capture it into the system, and make sure that it is brought into the system.

I do not suspect that 30 per cent of product will be directly imported but, even if it is five per cent, it is a substantial disadvantage to Australian retailers. My plea would be that, in any review of the taxation system that is going to go on in Australia, people have a very close look at this issue. The fact that we have got a highly discriminatory sales tax system in Australia at the moment means that some products are going to be targeted much more than other products for this particular system. It is clearly going to be a factor in what people do. We are dealing with a lot of unknowns in this area, and I have already conceded that, but my point is that it is going to be a lot harder to fix it if it becomes big than it is to fix it while it is still relatively small.

I cannot say precisely how big it is, but I believe the threat is quite large and quite real, and we need to find a way. I floated an idea in my submission—which was really all it was, a floating of an idea—that I am trying to encourage the committee to think of different ways of dealing with product that is coming into Australia in these very small parcels. We ought to be able to find a way, using the same technology, to capture the stuff in some way. I do not know enough about how the system works in detail to see that, but I do know, and I am sure everybody on the committee knows, that when you go to countries that have value added taxes or GSTs you pay the tax at the time of purchase and then, if you are eligible for purchasing that product tax free, you get a refund.

What I floated in the submission, just to try and stimulate some thought, is that in fact every product that comes in you charge a tax on, whether it is a gift or whatever it is, and it is up to the recipient or the purchaser of that product to demonstrate that they should not have had to pay that. All I am saying is we have to think about things in a very different way from the way we traditionally do it; otherwise this thing is going to get right out of control.

**Mr BEDDALL**—The other problem, too, is that once you, say, buy a CD on the Internet it becomes user friendly for you and you can then start to look at all the other items.

**Mr Shetliffe**—That is precisely right.

**Mr BEDDALL**—And you tax shop.

**Mr Shetliffe**—Yes. If we are going to move towards a broad based consumption tax, your point is absolutely right. The amount of tax is possibly going to be less. If you have got a 22 per cent or 30 per cent sales tax item and you are talking about a GST of six or 10 or something like that, then quite clearly the price differential is not as great and the freight component that inevitably has to be applied may even the price out a little bit.

**Mr GRIFFIN**—The situation could be that those goods which at the moment are sales tax exempt, and therefore are not attractive for people to actually shop on the Internet for, potentially could become attractive.

**Mr Shetliffe**—Yes. That was the point I think Mr Beddall was making.

**Mr BEDDALL**—One of the issues we have talked a lot about is books. I am not sure of the current situation, because it is some years ago when I last looked at this. The publishers had broken the world up into basically United States and the UK camps and, where you had to buy books via the UK, therefore availability of books, say, that were published in the US could be a year or two down the track. Do you know if that is still the case?

**Mr Shetliffe**—I would not pretend to be an expert on it, but I believe there are still those kinds of situations that exist, that the release of books into Australia is often later than it is elsewhere around the world.

**Mr BEDDALL**—This may be an advantage to Australian booksellers in the sense that the pressure will now be on to get the books earlier, otherwise people will buy them from the US on the Internet.

**Mr Shetliffe**—Precisely.

**CHAIR**—On this idea of a uniform charge, is it hard to administer? How do we differentiate between grandmother who sends a parcel in and XYZ company?

**Mr Shetliffe**—I would be the first to acknowledge it may be hard to administer. I am putting it in there not as a firm recommendation but to say we really have to look very closely at those commercial threshold levels, because the reason that they were put there in the first place, I suspect, is no longer going to be a valid reason. The major reason is that they were relatively small, they were gifts and they were not dislocating the marketplace in Australia. Whether charging for everything that comes in is the mechanism to do it, I am not sure. I am just floating it to try to say to the committee that you have really got to look at other ways of doing things.

But the proposition that I am putting is that the onus goes onto the recipient of the gift from grandma in England and the person has to demonstrate the validity of that, either at a post office or some other appropriate distribution area, that the bona fides are established, some rules are established and a refund is then given. Or people just pay the tax anyway, except that they have got the goods and had to pay that, just as they had to pay for postage to send it out here.

**CHAIR**—I have to say to you that other respondents to this inquiry have suggested that limits that are there now should be raised, and quite substantially, in order to encourage Australians to become more involved in Internet commerce.

**Mr Shetliffe**—Well, that is fine, but what that is going to do is potentially raise huge problems for existing retailers, who are the largest private sector employer of people

around the country. I would have grave fears about that.

**CHAIR**—The Yanks have had mail order houses around for a long time. It is a long established business moderm in the United States. Australians have never particularly warmed to mail order business.

**Mr Shetliffe**—I think that if we make an assumption that Internet home shopping is mail order business in an electronic form we have totally missed the point of what the potential of this is all about. That is the message I get from everybody that I have spoken to around the world on this topic. Internet shopping is not catalogue shopping, mail order shopping, in an electronic form. It is a totally new way of shopping. I would counter the argument by saying, have a look at what Australians did with ATM machines when they came in—one of the highest take-ups of anywhere in the world; have a look at what Australians did when credit cards came in; have a look at what Australians did when mobile phones came in. There is a great capacity for Australians to do it: we have one of the best electronic infrastructures about to be in place anywhere in the world, and we have one of the best educated groups of citizens in the world that are increasingly going to take up shopping in this new format.

It is totally different from walking into a shop to buy. It is a totally different experience if it is done well, and it will be being done well. I would urge members of the committee who have not gone and visited an Amazon.com site or one of those sites to do so, and have a look at how different it is in terms of the services that are provided compared with what you would get in a hard copy catalogue. I just think that to argue that we should be encouraging people to use it, and that Australians are not going to take it up on the basis that they have not taken up catalogue shopping, would be a false premise to start your argument on.

**Mr ANTHONY**—We talked a bit earlier on about this being beneficial to very small retailers. Is that correct?

**Mr Shetliffe**—Yes.

**Mr ANTHONY**—I assume you would walk into a small retail outlet; if they have not got it they would look it up on their own Internet site in the store; yes, we can get this for you, we order it in. I assume at that point the small retailer puts on a margin?

**Mr Shetliffe**—He would have had a margin on the product in the first place. But his cost of holding stock, which is a very substantial cost in retailing, is reduced because he can provide the product there. The problem that a small retailer has is range of product that he or she can offer. What this has the potential to do is, first, to enable them to source supply from overseas so that they can get a more innovative range of stock into their store than is available through the current wholesaling system that they rely on at the moment; and, secondly, they can carry a wider range of stock as available to their

customers without having to have it take up floor space in their stores and therefore add to their costs. So it makes them a little bit more competitive.

**Mr ANTHONY**—If I am the consumer and I see that, okay, this small retailer can get it for that price, why can't I just wander back home and look up it up on my own page and buy it direct and not pay the margin?

**Mr Shetliffe**—You will still be paying a margin in the sense that—

**Mr ANTHONY**—But there has to be a margin for that retailer.

**Mr Shetliffe**—Yes. It depends on whether the person that is selling it on the Internet is selling it to the consumer at the same price that he will sell it to the retailer. That is a bit of an unknown at the moment. He will have his supply agreements and arrangements with his suppliers that are likely to result in potentially a different channel.

**Mr ANTHONY**—Do you think there is much of that happening now with small retailers?

**Mr Shetliffe**—No, it is not, because they have not taken it up yet. But the costs of the technology is coming down. One of our goals as an association is to try to provide—and we have already started—forums and exposure to these sorts of systems so that these people can take it up.

**Mr ANTHONY**—Aside from the Commonwealth losing out from a tax angle and I suppose big retailers—the DJs, the Coles and whatever—losing out, the wholesalers will be cut out of the whole process. But, then again, I suppose the wholesalers are taking advantage of this because that is where they are purchasing most of their items, is it?

**Mr Shetliffe**—Again, everybody is going to have to rethink the way they do business—that is the point that I keep coming back to—and it is potentially quite different. Whether the wholesaler will be 'disintermediated', which is the term that has evolved in this area and the retailers will buy direct from suppliers, I think there will be a drift in that direction.

But just bear in mind, though, that, even with the most optimistic or pessimistic, whichever side of the coin you are on, predictions about this, even if it is 30 per cent, there is still 70 per cent of business that is going to be done more along the traditional ways. The infrastructure is there. One of the major barriers that manufacturers have at the moment or one of the major reasons they are not rushing in to sell direct to customers is that they do not want to be cut out of the game by the rest of the retail industry in terms of purchasing their product to sell through the stores. So there is a bit of a natural commercial reason that a lot of suppliers are a bit loathe to go direct at this stage. So the wholesaling mechanisms and price structures, I suspect, are going to remain in place for a

fair while in Australia.

What the Australian retailers will be doing is still accessing product out of those warehouses and manufacturers, and still be part of the game. How that is going to unfold again is something that we just do not know, but it certainly has the potential to reduce the impact of the wholesalers. One could argue it has the potential to increase the power of large retailers. If small retailers are not encouraged to take it on and do something with it, then it will. If small retailers continue to just operate in a traditional mode and not take advantage of this technology, they will be overrun by global competitors because they are now competing with people in the States and all over the world, or shortly will be, as well as having to compete with larger retailers. So they really have to become part of the game. What we are trying to do as an association is facilitate that.

**Senator COONAN**—What is stopping the small retailers? Is it just the cost of technology, or is it just that they are set in their ways of doing business and everyone understands the infrastructure that is there? What are the main barriers?

**Mr Shetliffe**—I think there are probably three. First, most retailers really have not thought through the potential of this and regard it as really only a small thing that is going to happen and it really is not going to impact on them greatly. Secondly, a lot of them would not be comfortable with high technology and it is all a bit strange. That will change as younger people come into businesses. The third reason is cost in terms of investing in the technology. To get a trading web site up is not all that cheap. It is quite cheap to get something up that is just an advertisement for you, but to actually transact business over it and set that up is not all that cheap. That is why there are a number of businesses out there trying to establish electronic malls. We have been concerned to ensure that those controlling electronic malls do not become the same kind of people as people that control physical malls in terms of the charges that they—

**Mr BEDDALL**—They are trying very much to become the people who are.

**Mr Shetliffe**—We looked at trying to establish our own mall as an association, but that ran into a whole lot of competitive issues. Associations really get themselves into trouble if they start getting into the front line competition of their members. So we had to pull our head in on that. But we are encouraging other people to form malls, because the main advantage of the mall is that it enables you to get into the market at a much lower entry cost than it would be if you went in entirely on your own. They are the three major reasons.

**CHAIR**—One firm, [www.consult](http://www.consult), commented in its submission:

. . . the only limitation Australian firms face is their own products, capabilities and management skills—none of these limitations is internet related.



You would not agree with that, would you?

**Mr Shetliffe**—I would totally agree with that, actually. That is really the point that I have been making. If Australian retailers sit around, do not take notice of this and do not turn it into an opportunity, it will be all threat and they will fail. That is about their inability to respond and manage their businesses in response to a changing marketplace and changing consumers. To that extent you are right.

My point about the Internet in relation to the tax regime is that, if as a consequence of the way our tax laws are structured we give a competitive advantage to people that are coming in offshore, then that is unfair and unreasonable. That is the proposition. If you put that to one side and put an argument about how retailers or other businesses survive in today's world, it is about those things that you just alluded to, the resourcefulness and manageability of businesses.

We would argue in a competitive marketplace that that is the thing that really matters. But, if you put a government imposed tax regime or regulatory regime—and do not forget all the consumer laws and the Trade Practices Act that apply to retailers in Australia—that cannot be ignored. If by government regulation you are disadvantaging Australian businesses, then that is the issue with which we take exception.

**Senator WATSON**—In relation to the commercial entry threshold of \$1,000 for goods imported by post, the decision taken by Customs as from April next year is to reduce that threshold to \$250.

**Mr Shetliffe**—Do I support that?

**Senator WATSON**—Yes.

**Mr Shetliffe**—Yes, and I believe it should go lower.

**Mr BEDDALL**—The Canadians we are told have \$20. Do you think that is a realistic amount? I know the ideal is zero, but \$20 is what we have been told the Canadians have as their threshold.

**Mr Shetliffe**—Yes. That would be much more acceptable than \$200, which is much more acceptable than \$1,000. There is probably not that many goods that you could justify coming in on a commercial basis that were less than \$20 because the freight charge is likely to have knocked it out of the market anyway. I suspect there is a balance there somewhere that one could establish. If one country can manage with \$20, I cannot see why Australia cannot manage with \$20. The challenge, of course, is to believe that what the paperwork says is in fact in the article.

**Senator WATSON**—Apart from having a level tax playing field, you do not really

come up with any other recommendations. You say there are problems, but there are also opportunities. Do you have any recommendations you would like to put to the committee?

**Mr Shetliffe**—I think that the major recommendation that I would like to put is really in terms of the comment I made about whole of government. This issue cuts across not just retailing but a whole range of the way in which business is transacted.

**Senator GIBSON**—The government set up a national office of information economy under Minister Alston which is meant to coordinate all of those activities.

**Mr Shetliffe**—Yes, and we applaud that as far as it goes. But we really need to make sure that government itself is taking advantage of the technologies in terms of its own agencies and to some extent it is. Certainly Customs are and certainly the tax office is. That makes a big difference to compliance costs for Australian businesses, so we certainly applaud that.

It is important that a whole variety of agencies that one would not normally associate as being involved in electronic commerce get caught into it. I just hope that, if that office has been set up, it does both establish the policy and the funding arrangements, because the funding for support for education programs—and we have been having discussions with DIST on that—still seems to be coming out of DIST. So I am not yet convinced that government has in fact got a coordinated and strategic approach to this.

Coming back to your question, yes, there are a lot of recommendations. Certainly education of businesses is an absolutely critical one, but that is not directly related to tax and those kinds of issues. There are a whole lot of things one might say about the Internet itself. In talking about the tax issues, then the major issue from our perspective is the sales tax, indirect tax issue. I am sure there are a lot of other tax issues and certainly, if you read the Tax Office's paper, there are a lot of other issues that relate to people's personal income tax and all sorts of tax havens and all those kinds of issues, which I have deliberately stayed clear of because they are not really in my area of responsibility.

**CHAIR**—Thank you very much, David. We will, on completion of our inquiry, as always, be delighted to send you a copy of our report, which will make recommendations to government about a whole range of things that we are hearing about over the next few months.

**Mr Shetliffe**—Certainly, if there is any more information you need, do not hesitate to contact us and we will be happy to provide supplementary information on a specific issue if it comes to mind.

**CHAIR**—Thank you very much.

### **Luncheon adjournment**



[1.49 p.m.]

**MULDOON, Mr Kenneth Robert, Secretary, CAPEC Pty Ltd, PO Box 484, Mascot, New South Wales 2020**

**CHAIR**—I now welcome the representative of CAPEC Pty Ltd to today's hearing. We have received your written submission. Would you like to make a brief opening statement to the committee before we start to ask you questions about your submission?

**Mr Muldoon**—Yes, very briefly. I should first of all outline that CAPEC is an industry association that has only been recently re-formed in Australia. It represents the four major express carriers here of DHL, TNT, Federal Express and UPS. It is an industry association but only of the four major carriers. While it has only recently been formed, as its secretary I am hoping that the industry can play a more active role throughout in the industry and in the developments of the import-export trade in Australia. I am hoping that our profile will increase a little over time.

As you say, you have already seen our submission. The main point I would like to raise is that I would like to see the Internet commerce debate be more of a positive debate looking at the opportunities for Australian industry, rather than looking at some perceived obstacles and threats on an import side. I think Australia generally has to be more outward focused and I think the Internet gives us a wonderful opportunity. Certainly the timing is that if we do not get on board now we will be in a continual catch-up mode.

**CHAIR**—Thank you for that. You recommended raising 'screen free' limits. Others who have appeared before this committee have recommended lowering them or eliminating them altogether except in cases of grandmothers and presents. Would you like to talk to that issue? How high and why?

**Mr Muldoon**—The threshold debate has been around for a long time. It is probably currently in a number of arenas—this current one, the review of the Australian Postal Corporation Act, which will probably look at it to some degree, and the previous debate surrounding the change which was eventually deferred until 1 April next year. There have also been a number of reviews within Customs.

One of the key elements there is harmonisation. I suppose one of the major points that we would like to argue is that the thresholds of the post and the other modes should be harmonised. At the moment legislation is there that that will happen on 1 April to bring everyone down to \$250. We believe it would probably be more appropriate and would probably stimulate more trade if that limit were taken up to \$1,000 or beyond. There have been several studies including ones by Customs, on which we can give you the statistics, of how many shipments are coming in under these limits and what the effect of those are on the taxation base. The number is included in the Customs submission and I will provide the figure for you. There is a full KPMG study that was done on potential rises of

the threshold to \$1,500.

To me, one of the critical elements is that a rise of the thresholds, I believe, would allow end consumers to buy goods cheaper. Personally, I believe that there is not a great risk to our industry protection regime—quite the opposite. Most of the commodities you see coming in have no Australian production. It was very interesting this morning talking to the Australian Fishing Tackle Association, and you have had representations from the jewellers' association. Most of them say that there is no Australian industry, so we are talking here about concerns from a service industry that is servicing consumers. I believe that if you look at it from that perspective, all a lower threshold would do is to add costs to consumers for no real benefit to our Australian manufacturing base.

**CHAIR**—Some others argue from the viewpoint of equity—not of decreasing competition by lowering the limit. They argue that, because we have a wholesale sales tax regime in place and because it is set at varying rates and because some of them are very high, by the time you add the little bit of duty—because most things are down to four per cent or five per cent now anyway—to wholesale sales tax, you severely disadvantage Australian players versus companies that market into Australia via the Internet or any other mechanism whatsoever. They are simply shipping into Australia without an Australian base.

**Mr Muldoon**—I think there is a little confusion—and I have not had the opportunity to look at the papers that were presented this morning by the Fishing Tackle Association—because it seemed to contradict to some degree the statement made by Customs in their submission. They say:

It is unlikely that reducing the duty and sales tax free limit will in itself increase the competitiveness of Australian retailers.

They then goes on to say:

. . . even if duty and sales tax were paid it would still be cheaper to import the goods through internet/mail order.

There seems to be a little bit of conflicting evidence on that, or at least claims this morning. It comes down to this hurt. There is a perception that the thresholds are causing hurt to Australian retailers. I would probably like to have a lot more research done on that. If the Customs assertion is accurate, that it would still be cheaper, all we are doing is imposing a cost on our consumers. Even if the duty and sales tax were paid, and if it were still cheaper to buy over the Internet, there would be no benefit to the retailers; they would still lose the sale. The consumer then would have to pay the duty and sales tax. The consumer then would also probably be burdened with Customs cost recovery charges, and there would be no benefit to the Australian manufacturing sector or to any sector in Australia.

**Mr GRIFFIN**—So you are arguing that it is a burden for people to actually have to pay the duty and sales tax they should be paying, in effect?

**Mr Muldoon**—No. The thresholds are there for a reason. Thresholds would essentially be put in place for two reasons: one, industry protection and, two, collection of the revenue by the Australian government. If you say that there is no industry protection role within the thresholds—if that has gone or, in the majority of cases that we are looking at of goods coming in, there is no Australian production base—it becomes a question of loss of revenue. There is the additional angle, I suppose, of retail protection.

**Mr BEDDALL**—That is the very point, though; isn't it? This inquiry is about the dangers of the revenue base of the Internet.

**Mr Muldoon**—Yes.

**Mr BEDDALL**—If we wait and get the empirical evidence that it has caused damage, it may be too late. The example given earlier this morning in evidence was that, of 1,000 shirts or 5,000 shirts coming in being consigned to individual people, all those items of apparel would attract sales tax. If they are sold domestically, they do not attract sales tax because they are imported. That is a substantial amount of revenue foregone by the Commonwealth. Should the government decide to move to a broad based tax, then even more drainage of revenue will happen as Internet shopping increases, because one of the advantages of Internet shopping is that you do not pay those sales taxes on individual items. So Internet shopping gets a comparative advantage in the bases of subsidy by the taxpayer.

**Mr Muldoon**—Certainly, if there is consolidation for commercial distribution, then, yes, that would seem potentially inappropriate and not what the thresholds were for. However, in relation to the threshold that is there for the individual consumer buying a one-off—as I say, with the taxation implications—there has been a plethora of claims about what that level is. I think the Australian Taxation Office in its discussion paper said there should be some benchmarking and some proper research done, and I would very strongly support that. Our industry strongly supports that. If we can assist in any way, we will, for there to be some reasoned debate and gathering of data to say what that true leakage is. In relation to the circumstances that were outlined this morning, including the ones on mis-valuation et cetera, personally I see those distracting from this whole discussion. With any trade that happens, someone can mis-declare what the value of the good is.

**Mr BEDDALL**—They are just fraud. They are not part of this inquiry; they are fraud. The ones where they had \$63 instead of \$650—that is fraud.

**Mr Muldoon**—I think if you look at it and say, 'Well, there is no industry protection role,' then I agree that there needs to be a proper assessment done of what the

revenue leakage is by not collecting this. Secondly, to the converse, if it were collected then what would be the result? Now, if those results are increased prices to consumers for no industry protection level, and that is a political decision that that should happen, then so be it. But the main thing that I would like to see is some of the emotion removed from a lot of the emotive cries—that the thresholds are causing injury to industries here in Australia—and a look at the data and the facts.

**Mr BEDDALL**—But I do not think the tackle people were actually saying that. The jewellers certainly were; the jewellers could not quantify one shop that had closed because of the Internet and their competitive pressures. The tackle people were not saying that. But the real issue here—to come back to the central point—is the tax revenue base.

This is a whole new way to shop. Everyone acknowledges that. This is not electronic mail order, this is an opportunity for people to go and shop offshore, and one of the reasons that it will be attractive to shop offshore is that very high rates of sales tax will not apply. And that is an advantage that I think we should not give to an offshore retailer if we do not give it to an onshore retailer. The converse argument is to abolish sales tax.

**Mr Muldoon**—I would very much like to avoid getting into the debate of the GST and the abolition of sales tax.

**Mr BEDDALL**—I would be doing the same thing, though.

**Mr Muldoon**—I would not like to get into that debate. I believe that there is an opportunity for Australia to look at the Internet and to trade. What has happened is that if you look at a lot of these American based companies, because that is where the Internet has probably developed most and why they have such an interest in it, they have set their sites up. They have invested in their sites and they have invested in the infrastructure that goes with it. They are able to offer economies of scale and they are able to offer product range to consumers, and it is about providing a service to a consumer as a retailer is here in Australia. But they have got those economies of scale because they have worked and said, 'Okay, there is no reason for us to limit our market to the physical boundaries of our country,' even in a retail trade. They have been able to say, 'Our market is the world.' And there is no reason why Australia should not do the same.

**Mr BEDDALL**—No, there is. We have not got the manufacturing bases to supply the goods.

**Mr Muldoon**—There are enough companies here that are starting to do it on the Internet. If you say that we can never achieve those economies of scale because we do not have the domestic base then you are right: we have got some real problems. But there is no reason why Australian manufacturers cannot use the Internet and do exactly the same and say 'Our sales base is now the world,' and achieve those economies of scale.

**Mr BEDDALL**—But surely in the United States that is based on a production base as well as a sales base?

**Mr Muldoon**—It would be both, but Amazon Books is a prime example. It just gathers books from around the world and distributes them to anywhere.

**Mr BEDDALL**—I have heard a lot of arguments about the US free market and its regimes. You can say, for example, that their sales tax on motor vehicles is 2½ per cent, but on a four-wheel drive—what they call a pick-up truck—it is higher than Australia. It is not always a free market like that. And this is a market driven by one country.

**Mr Muldoon**—It is driven by one country at the moment, because most of the commercial sites are on there, and I think that is probably one of the most important things. The Internet will have international sites, and it will develop more and more. My push would be for Australia to be there now as one of the next countries to take it up and for our manufacturing base to use that capability before America, Europe and everyone else floods our market. The Internet commerce will be there; it will not go away, it will only increase. The point for Australia is to be there at the forefront. We cannot be number one, because as you say, the States has done it.

The opportunity, though, is there now for us to take the next step and be ahead of others and gain from that. I believe it is more important for the government to try to help industry and promote industry to take advantage of that opportunity rather than to look at the negative and protectionist environment of stopping goods coming into our country.

**CHAIR**—This morning the customs brokers suggested that rather than either increasing the ‘screen free’ limit or lowering it perhaps a uniform charge at some minimum level should be put on every packet that comes into Australia, and that all processing should be done electronically with some kind of regime to exempt presents from grandma. What do you think of that idea?

**Mr Muldoon**—You raised the issue of the presents from grandma, and I think that is very interesting, because I think we would see a lot of presents from grandma coming in.

**CHAIR**—We already do.

**Mr Muldoon**—If we already do, you start to say, ‘Is it a real problem to our taxation base?’ As I say, the Australian Taxation Office in its discussion paper does not believe that the thresholds are such a concern. On the idea of adding on a cost to every shipment, again, if you do not have a major concern for your taxation base and you do not have a benefit for your Australian industry, you are just creating a processing load and then passing on the cost of a processing load to a consumer for no good reason. Personally, I cannot see why.



In terms of IT processing, certainly. It is one thing about the express carrier business and slightly different from the post, where we do gather all this data, all the information, and under any system that we developed we could probably facilitate. At the moment we gather all that data, all the values and everything, even for goods below the \$250 threshold. If people want to find out what is coming in through our systems, we can gather that data for our commercial systems and we can provide it.

There have been some concerns that data integrity would be lost if the thresholds were raised. We provided a supplementary submission making it quite clear that, if the thresholds were raised, we would continue to work with Customs and ABS to provide that data. But, as I say, a dollar figure could be added on if that was what was decided. Personally, I just do not see what that dollar figure is hoping to achieve. If it is to protect our retail industry associations but it would still be cheaper for the user to buy over the Internet even with that, then I have got some real concerns on what it is trying to achieve.

There is discussion from the retail industry about how this might benefit small scale retail outlets where they could come and suddenly offer a wider range of goods. It was quite rightly asked, if that retailer is not offering a real value added step in the process, why wouldn't the customer just sit at home and order it himself? If we wish to protect a service industry at the cost to the consumer, then that would be a decision that we can make. But, personally, it is not one I would support.

**CHAIR**—Fair enough. I come back again to how you deal with the equity issue, saying to the retailers, 'It is a big, bad competitive world out there. You have got to swim. If the sharks are around, you'd better learn to swim faster if you want to get away from the shark.' That is fair enough. But what about when government itself becomes a shark by imposing impost on a fishing tackle reel if it is sold in Australia? If a retailer or a wholesaler imports 200 of these things and puts them in the shop and sells one to a customer, by the time he takes care of both the duty and the wholesale sales tax it is about 33 per cent of the wholesale value of the product added on to the wholesale price before he starts to add his margin to it. What do you say to him in terms of equity when the Australian government takes that from him and allows the same reel to come in by Australia Post or air freight and go straight to the customer and no tax imposition is put on, therefore encouraging the overseas supplier rather than the Australian supplier? What do you say to him about equity?

**Mr Muldoon**—I would say that the Australian retailer, to me, can still always have a role in retailing in Australia even if there are cost advantages from overseas. But, equally, he would still not gain that sale because someone has set up an international marketing regime that will allow those goods, even if the duty and sales tax are paid, to come into this country and it goes to the end user cheaper. To me, the question is not about whether there is equity there; the question is about the consumer. Do you want to make the consumer pay a higher price?

**Mr BEDDALL**—The argument from the tackle people, or bait and tackle or whatever they were, was that they were cheaper than the international price.

**Mr Muldoon**—That is what I am saying. I have not had the opportunity to look at that evidence and I would just like to balance it and have a look at that versus the claims that were made by Customs that that may not be the case.

**Mr BEDDALL**—Nobody is saying that we should give a price advantage to a domestic retailer in the increasingly globalised market. What we are saying is that, if the domestic retailer is uncompetitive because there is a government impost on his sale that does not apply to the Internet sale, then there is an equity argument in that, if that is the differential.

**CHAIR**—We are asking the question, not saying it.

**Mr BEDDALL**—I will say it. I think it is significant. It is demonstrable in some issues.

**Mr Muldoon**—I think it is significant. It may be demonstrable in some and I think it would be quite the opposite in the others, where there would still be a distinct price advantage to buy it from overseas. I still think it comes back to a retail industry being about servicing a client and about servicing a consumer. If we are talking about our manufacturing base here receiving protection, I believe that we Australians should do everything to promote our manufacturing base and use the Internet to get that manufacturing base looking global and expanding itself.

But if we are talking about areas where there is no Australian manufacturing base and we are talking about protection of the service sector, a service sector that is designed for the consumer, then I suppose I would just like to have some questions about where that is really targeted, particularly if, as the Australian Taxation Office has said, at the moment, within the next couple of years, they do not see a real threat to this trade and the threshold. More, they are looking to see what opportunities there are if Australia grasps this opportunity and starts to export.

**Mr BEDDALL**—We have had that argument from the Flat Earth Society on a whole range of products. We are the most open market in the world and that is fine, but you cannot keep being the most open market in the world.

**Mr Muldoon**—But the point remains that, if we do not have an Australian industry and an Australian manufacturing sector here, then we are just imposing additional costs on consumers.

**Mr BEDDALL**—But isn't it true that the consumer has to also pay for the warranty provision? That is part of the price—all of those things that are built into a retail

price. Someone selling on the Internet, like Amazon.com, is just shipping; they do not have any other obligations that a retailer will have. Those retailers have to build that cost into the price.

**Mr Muldoon**—I agree. And I think that is why Australian retailers will always still have a role. Personally I have used the Internet a great deal but I do not buy anything over the Internet. I like to go in and have a look at something, touch, feel, and when I buy it I want it then to use. So I believe there is always a service that the Australian retailer can provide and therefore it will remain. As for the analogy of a shopping mall being set up and the threat that that has on corner stores, you do not have as many corner stores but you still have corner stores because they provide a service.

With warranty issues, yes, there is some concern. I think it is very important, and it is interesting to see some people now alerting consumers to the problems with buying on the Internet, when you talk about warranties, for example, the Fishing Tackle Association's idea of a reel that is not designed for Australian specifications. Even if there is a price advantage because of the economies of scale of some of these other suppliers, there will always be a role for Australian-based retail. But it is a matter of them realising what their better market is or, alternatively, moving their shop into the shopping mall and getting out there and competing on the international market.

From where I go, a manufacturing base in Australia using Australia as a distribution base is far better, I believe, in the long term than protecting a service sector in Australia. There were discussions this morning about laws being made in Australia. I think that is a trade that we should be concerned about more so than looking at protecting the retail sector. I would prefer to see some efforts going into promoting Australia's production and distribution more than potentially drawing up these barriers. You talked about the concern for goods from grannies coming in. If you take the line that a retailer should not be disadvantaged, why have a gift concession? Why have a duty free concession for goods coming in? This concession does not sit by itself. There is a range of low value, effectively non-commercial or insignificant value concessions that sit there for a reason. I do not think it should be overstated what the implications of that are on our taxation base.

**Mr BEDDALL**—The rationale behind those concessions predates the Internet. The Taxation Office surely cannot deny that. I know it predates the Internet. When I was the Minister for Customs, there was no Internet, and all of those things were based on an acceptance that someone will send a gift and there is a certain level at which the gift should not attract any duty. That was long before this type of commerce became possible. Someone pointed out earlier today that we are not a country that has actually taken to mail order in a big way, so that has not been a real problem for us. Some people do, but not many. All those concessions were based in a different time zone.

**Mr Muldoon**—They were, when there was less international trade, and there is

more international trade now. I do not dispute that. Equally, those concessions that are sitting there are at the moment have been in place since 1985. The true value of a dollar since 1985 has changed dramatically as well. The issue is still there in terms of at what volume these are coming in under these low value concessions relative to the total volume of trade in Australia. I think, yes, they are very important statistics that should be before the committee. I would much prefer to see any decisions on this based on those informed and valid data rather than emotive calls.

**CHAIR**—Those are reasonable questions and I think we ought to think about asking the tax office or ABS about that.

**Mr Muldoon**—You are, of course, getting some statistics through Customs and that survey that is going on at the moment, which is talking about what the revenue leakage is. I am sure this is part of your considerations—the tax and the Internet from the Australian Taxation Office.

**CHAIR**—Absolutely.

**Mr Muldoon**—It is unlikely that in the next one to two years there will be any appreciable impact on revenue collections. This is the Australian Taxation Office's finding in terms of the Internet. As I say, I would just like to see the base of the discussion.

**Mr BEDDALL**—It is a pretty short time span, isn't it, one to two years? It is a very hedged bet.

**Mr Muldoon**—The Australian Taxation Office also suggested that there be some benchmarking exercises and proper monitoring done. When I was drafting the submission for CAPEC, I looked at that and I thought, 'That is a bit hard to argue against.'

**Mr BEDDALL**—Sure. I would not disagree. Maybe one of the options is that, instead of opening up first, we do not open up until we have got the data. In the past what we have tended to do is open the gates, then go and get the data.

**Mr Muldoon**—I think a lot of the data is available, certainly from the air industry, the express carrier industry. The data is there and it is already provided to Customs in air cargo automation form. There might be some question marks about what is coming in through the post. But again, if the post has that threshold now, the decisions can be made on the air express industry on an informed basis now. I would suggest that that should be done.

The other point you talk about is the barriers. If you look at what is happening in the TCF and car industries, the move there, which drew a lot of coverage, was to slow our tariff reductions down; it was not to impose greater tariffs. I have some real concerns on an international level if Australia was to say, 'We are imposing a barrier to trade, we are

increasing a barrier to trade' in the environment, rather than removing a barrier to trade in this world. That is particularly so when that barrier to trade that we are raising I think has some questionable value. The flow-on effects to Australian industry are very questionable and would probably have adverse effects for Australian consumers.

**CHAIR**—By the same token, let us take ABC fishing rod manufacturer, who markets in Australia through a wholesaler, who distributes to a range of retailers. That is one stream for the manufacturer of a rod. That manufacturer also takes orders on the Internet direct from customers in Australia. You have got two competition chains. One of them is reasonably expensive for him, in that he markets at a price but then the wholesaler wants their chop and the retailer wants their chop and probably the shipping costs are less because you consolidate.

On the other route, what he manages to do is to totally bypass the tax system. Forget about the revenue loss implication. It is just that he has one competition chain that has government imposed in the middle of it with charges, for whatever reason. Then he has another distribution chain where there are no charges. That is like giving Australian companies the opportunity of establishing their head office in Sydney but banking in the Bahamas or the Cayman Islands versus banking down in George Street. Is that fair?

**Mr Muldoon**—The Internet commerce is certainly going to provide a few headaches for the banking industry, I am sure.

**CHAIR**—It provides a lot of challenges and a lot of opportunities.

**Mr Muldoon**—I can see what you are saying. If someone does something on a wholly commercial basis, they have these imposts put upon them, and if something is done for an individual consumer that is removed. I think that was the whole intent when these thresholds came in and it links in with many of the other thresholds and, again, I say they are duty free. You then start to ask the same question: 'Why can someone bring in something just because they have been travelling overseas?'

You start to question a lot of these things that are going to individual consumer purchases as opposed to large scale commercial activity. I would say, yes, historically there has been a recognition internationally that there is a difference. These thresholds are not only here in Australia; they are everywhere else. As Customs said, ours are relatively low.

**CHAIR**—Our tariffs?

**Mr Muldoon**—Our thresholds. Look at the US threshold: \$US1,200.

**CHAIR**—But the Canadian one is \$20.

**Mr Muldoon**—The Canadian is an interesting one. The Canadian one is a lot more than just the \$20.

**CHAIR**—It is \$20 tax.

**Mr Muldoon**—Yes. It is a whole regime that goes around the Canadian system. It is not just that you still have a customs force and you have a Canadian threshold. In Canada there is a totally different system where the carriers now collect that duty on behalf of the government and remit it at the end of each month. They are given the role of collecting and assessing the amount of duty.

If we were to introduce a system here that had that lower level, the consumer would not only have to pay the duty and sales tax but he would also then have to pay a customs cost recovery charge. What you are getting into there is that it becomes a question as to the validity of Australia's customs cost recovery charge. It was said before about levying on every entry. Here in Australia, for anything that is above the screen free threshold, there is a charge for that Customs process.

It is the same, whether it is an individual consumer, if you buy the goods, or if it is one of the large chemical companies bringing in \$1 million worth. You start to question equity there and the value of those goods. Should you introduce a scale system? I think you mentioned one of those. I think you start to get into a lot of technicalities, and it might be good to come in totally fresh and say, 'Yes, we could develop a whole new system which has certain equities.'

The thresholds have been there for a while, and I believe internationally they are there and it is recognised. As I say, I would have great difficulty and concern if Australia was to start to impose tariff barriers again. That is the way the international community would look at it.

**Senator WATSON**—How do you view the one consignment with, say, 100 invoices for under \$45?

**Mr Muldoon**—I would have a concern with the concept that was put forward today of someone consolidating and moving them through. Certainly that is not so much what our business is about. We sell our business on the fact that someone orders it—if you were looking at Internet—and it is with them within a couple of days. I think even the Australian Retail Association said that that is not where that consolidation can happen. That is only for goods which are not time critical.

**Senator WATSON**—I am not criticising your practices but that is happening. Should we stamp that out?

**Mr Muldoon**—If we were to say that that has dramatic implications for our

taxation base and has implications for our retail industry or our manufacturing base in Australia, then I certainly think we should look at it. But I think we should look to see what those implications are and not just stamp it out without making an informed decision.

**Senator WATSON**—Is it a widespread practice?

**Mr Muldoon**—Again, I say certainly not in the area where I work.

**Senator WATSON**—No, not in your area, but are you aware that it is widespread amongst your associates?

**Mr Muldoon**—No, I do not believe you would see most of it being widespread. I think there has been a lot of emotive debate and a lot of claims that are not quite right. We do a lot of trade through Amazon Books. People are saying, ‘No-one would order through Amazon and use our industry.’ They do, because they want it quickly. That, to me, is not so much about Internet commerce. The Internet is only offering these facilities. I could not comment too much on the freight consolidation aspect. Maybe the freight forwarders and Customs are better placed to tell you whether that is happening. If a system was introduced to remove that, it would be more up to Customs to police it, and it becomes more of a policing issue outside the realms of what Internet commerce is about.

**Mr BEDDALL**—With Amazon Books, some books are not time critical and others are; otherwise it is not an Internet sale. Or maybe it is an availability thing.

**Mr Muldoon**—As was pointed out, Amazon was not there. It was developed around this. They are a company that can now offer a vast range of books and offer them at a cheap price because of the economies of scale that they are working under.

**Mr BEDDALL**—The Parliamentary Library gave evidence very early and told us that it is never a cost benefit for them to airfreight. If they want a book—they do order on the Internet—they probably use Amazon in terms of a book they could wait six to eight weeks for because it comes by sea mail and therefore it is cost-effective. But if you need the book, then you order it through another freight forwarder.

**Mr Muldoon**—There is a price premium for using our service. Equally, if you want the book—I am not a purchaser. If I buy something, I want it in front of me now. If I buy it through Amazon Books, I will probably try and get it here as quickly as possible. The alternative is to go down to the shops. I think it is very much an unknown about how much is impulse buying and being there in front of the product. That is why I welcome the idea of benchmarking exercises and monitoring it. The only thing I would push is that the benchmarking exercise should be done with a harmonised threshold of \$1,000 and not \$250.

**Senator WATSON**—I presume you have seen the report from the Taxation Office on the Internet. Have you got any comments on that?

**Mr Muldoon**—I like the report that came out of the Department of Foreign Affairs and Trade on the new Silk Road. I found it heartening to see the government and its agencies looking to do exactly what I am trying to do and say, ‘Stop looking at the Internet as a threat and look at it as an opportunity,’ and start to say, ‘We shouldn’t build barriers around Australia. We should look at how we can develop our export trade for the good of our economy and should see the Internet as an ideal opportunity to do that.’

**Senator GIBSON**—Another opportunity is to change our tax system and move to a broad based indirect tax. Sorry I was not here earlier on. If we do change to a broad based indirect system and your firm is going to get mixed up in this, do you have any comment about the practicalities of that?

**Mr Muldoon**—If there was a broad based tax system and it said that on any consumer goods over a certain threshold there would be a tax levied, it would become a question of administration, as Customs have said. You have talked throughout your hearings about the actual administration if the thresholds were removed. Most of the goods that are coming in under the thresholds are coming in through either our industry—and not necessarily just our four but the broader air courier industry—or through parcels post. I think it would come to a point where we would be potentially given that task. If there is a broad based tax system, I think our industry would happily work with the authorities in looking at a feasible way of gathering that money and how that could work. If it was to be imposed on imports, I can see some commonsense in one of the easiest ways, which is through our industry gathering it, and the Canadian example looks at that. But, if it is broad based, I still think there is still room for thresholds.

**Senator GIBSON**—Sure. Most of the rest of the world runs a VAT or a GST or a retail sales tax. The threshold question which you were talking about before has obviously been addressed elsewhere, and so our current threshold fits in with other countries’ perception.

**Mr Muldoon**—As you say, the UK has a threshold, the US has a threshold and there have been thresholds throughout the world. The OECD, looking at parcels delivery, talks about thresholds, and in fact I only chased up the OECD paper after it was raised by I think it was the ACCC before you. Again, it looks very closely at the Canadian system, but it recognises that these thresholds have been used throughout the world.

**Mr BEDDALL**—Except, Brian, the home of the Internet does not have a value added tax—the United States of America.

**Mr Muldoon**—But it is interesting. The Internet is there, and the US—



**Senator GIBSON**—The US has retail sales tax, though.

**Mr Muldoon**—Only in some states.

**Senator GIBSON**—Well, most states.

**Mr Muldoon**—The US, as I think you commented, is obviously expounding the virtues of the Internet as most of the benefit is there. But the benefits are there because what they have done is set up the shopping mall, and people now go to it. It is up to Australia to get their shops in that shopping mall. To try and ignore the fact that the shopping mall is there and keep trying to run your corner store does not hold a lot of—

**Mr BEDDALL**—We had the classic example this morning where someone was trying to set it up but then there were territorial fights over who owns the ground the mall is going to be built on. That is the classic Australian reaction.

**Mr Muldoon**—It is very understandable within the retail industry if an association started to try and show favourites. But it should be up to industry. You look at a case study in that Foreign Affairs and Trade book, Mick's Whips, it is just wonderful. A two-man operation, and suddenly—

**Mr BEDDALL**—It is not going to compete with Amazon.com, is it?

**Mr Muldoon**—No, but it is a wonderful example where a two-man operation can go international, and the Internet provides that opportunity. You talk about getting economies of scale and the laws that were talked about. As I say, I would much prefer to see Australia developing and promoting that export activity than protecting a service industry—and we are a service industry, and it will happen.

**Mr BEDDALL**—But that is not unusual for Australian companies. If you go back to the McKinsey report *Born Global*, there are a whole series of Australian businesses that were born as international businesses. They are not retail, and that is the difference. Retail has not been an international trading goods sector until now.

Have you got any indications of what the impact will be on the Japanese? The most protected retail sector in the world is the Japanese.

**Mr Muldoon**—No, I don't. I could not comment. Maybe DFAT would be a better one to look for.

**Mr BEDDALL**—The unemployment benefit is called employment in Daimaru store.

**Mr Muldoon**—As I say, I cannot really comment, but personally I believe

Australia has a wonderful opportunity to set itself up not just as a regional headquarters but also a manufacturing base and a distribution base for Asia and even beyond Asia the world, the same as the Americans have done. If we were the second major country to embrace the Internet trade, better for us, because every time another country embraces it before we do it is a market that we have lost, or a potential marketing opportunity that we have lost.

**Mr BEDDALL**—We do have one advantage: we have got the best postal system, haven't we, internationally?

**Mr Muldoon**—Yes. I think there is more positive to be gained out of this and, as I say, I strongly believe that the benefits are there for the consumer for a raise in the threshold without adverse implications to our industry assistance or to our taxation.

**CHAIR**—Very good. Anybody got anything else? Thank you very much, Ken. We will take a brief break.

[2.48 p.m.]

**PATTINSON, Mr Hugh Matthew, School of Marketing, Faculty of Business, University of Technology, PO Box 123, Broadway, New South Wales 2007**

**CHAIR**—Welcome. In what capacity are you appearing before the committee?

**Mr Pattinson**—As a private citizen.

**CHAIR**—We have received your submission. Would you like to make a brief opening statement to the committee before we start asking questions?

**Mr Pattinson**—Yes, thank you. The main focus of the submission that I put forward, as I indicated in a note to Stephen when I put the submission in, was that I was looking more from a strategic perspective. I know that the actual inquiry is focusing a lot more on taxation and copyright, but I was trying to emphasise the need to make sure that we invest properly in our infrastructure to be able to provide state-of-the-art, leading edge, Internet based products and services, and to build the leadership position in a number of new industries that may come out of this area. So the focus of this particular submission is: what are the building blocks that we need to put into place over the next 10 or so years in terms of building an effective infrastructure?

**CHAIR**—Thank you for that, Hugh, but I do not think it is fair to say that the committee is focusing on tax or on security. I think the committee has an open mind and is willing to look across all the broad issues involved. Although we are an accounting body by name, we are even prepared to look at technology in this instance. It is just that certain hearings wind up with certain groups of witnesses. We started off this morning with the Australian Fishing Tackle Association who were concerned about tax.

Tell us about Internet2. Why is it important? How far away is it? What can a committee like ours do to help hasten it on, if that is of any potential benefit to Australia?

**Mr Pattinson**—As I understand it, Internet2 is a tag given to something currently being researched which will be the next generation of what we know today as the Internet. A couple of months back President Clinton supplied around \$US150 million to the scientific foundation over there, with the aim of assisting various companies and researchers to develop the next generation of the Internet.

The claim at this stage is that it will give between 100 and 1,000 times the current performance of the Internet. It is expected that a version of that will be up and running within five years. What I am really trying to say is that, once an environment like that comes into being, with that extra performance, capability and functionality, policy makers and companies looking at developing information based products and services need to really lift their horizon in terms of the potential products and services they should be

looking at developing.

But I reckon we should go further than that by actually becoming a part of the teams, organisations or groups that are developing aspects of that new environment. By developing technologies associated with that environment, we would have a chance to have a leadership role as this new environment rolled out and developed. We then get first access to that faster environment, to that environment that has a lot more multimedia capability than the one we have today.

**CHAIR**—Have you, through your work at the university, any idea of what the take-up rate by individuals and/or companies in Australia is—those now actively using the Internet—and do you have any idea about where we are likely to go?

**Mr Pattinson**—I have written a few papers in this area, although they have a more international perspective. Just by way of introduction, I am a lecturer in the School of Marketing at the University of Technology here in Sydney. I have been looking at this area for about three years. Before that I was in the computer industry as a marketer. I lecture in the area of international marketing. I also coordinate a postgraduate subject which is essentially all about marketing on the Internet.

My understanding of the worldwide Internet take-up rate is that about this time last year around 50 to 70 million people were using Web browsers to get into the World Wide Web. If you look at the Internet from a categorisation point of view, the Internet, as you have probably already been told, is a set of interconnected networks. Networks can go right down to one computer—a person with one computer—to a server that deals with hundreds of people. So the indicator we tend to use is the number of people who have downloaded or bought Web browsers such as Netscape Navigator or Internet Explorer—whatever version. We try to count them.

I attended a session a couple of nights ago where it was suggested that more than 1½ million people in Australia are using the World Wide Web today. If you look at the figures looking out for the next few years—out to the year 2000, say—we have put in writing that we expect the figure of people using the World Wide Web or a successor of it to be between 100 and 500 million people by the year 2000. The figures are very wide. That is worldwide. International Data Corporation, which is one of the main research companies in this area, believes that a minimum of 170 million people will be using the World Wide Web by the year 2000, using current browser technology. I am not quite sure how that would translate down to Australia, but I think we would be looking in the vicinity of four or five million users by the year 2000.

**CHAIR**—Is our business taking it up though?

**Mr Pattinson**—In terms of business, the worldwide figure we have seen in that area shows that there were around 50,000 companies with home pages in early 1996.

There is talk of that being around 75,000, but I cannot sustain that. I have not got a documented position on that. I am not exactly sure what the figure here in Australia is at the moment. It would be probably around 5,000, but I cannot document that exact figure for business use. What I do believe though is that within five years—and certainly between five and 10 years from now—most if not all businesses in Australia will have a home page of some sort on the World Wide Web. I am not saying anything about how they will use it, I am saying they will have some sort of presence in that environment.

**Mr ANTHONY**—You mentioned before that you are counting the number of consumers buying the software for Internet—

**Mr Pattinson**—I actually said, ‘the people who are downloading or buying the software,’ because the bulk of—

**Mr ANTHONY**—So that figure of 1 to 1.5 is people who have bought it or downloaded it.

**Mr Pattinson**—That is correct.

**Mr ANTHONY**—How do you monitor downloading of it?

**Mr Pattinson**—That is a difficult problem. We really have to rely on the vendors’ claims. As I said earlier on, the figures are very rubbery in this area, because people may download it but not use it.

**Mr ANTHONY**—Can you copy it easily?

**Mr Pattinson**—I do not know of anyone who has copied it but, yes, if you downloaded it to a set of diskettes, you could take it to another machine and copy it. If you want further support of a browser, though, you have generally got to go back and register with the company.

Certain groups in society can get it for nothing for longer term, such as academics and various other groups. A lot of people will download it on a 90-day trial, look at it and then upgrade to the next one. But a lot of businesses need more support. Also, they are putting in what we call Intranets—you have probably heard people mention those—and they need to have much more rigorous licensing processes for that.

**Mr ANTHONY**—Of the 1 to 1.5 Australians who have access to Internet regularly, can you surmise how many would actually have made a purchase?

**Mr Pattinson**—Very few.

**Mr ANTHONY**—Because that is where this inquiry is coming down to.

**Mr Pattinson**—I do not have any exact figures. For instance, I have not looked at www.consult and those groups that look at that area, but my estimate would be well under 10 per cent of that group—very low. There are still some significant issues worldwide. As you are probably already aware, there is also a problem in Australia of issues in terms of doing transactions over that environment—providing credit card information, in other words. A lot of people are still looking at the area. They go in and get information on a product or a service but use another means to purchase the product. At this stage I would still say that the actual purchasing activity, relatively speaking, is quite low in that group.

**Senator WATSON**—Would the majority be students using it for educational type purposes or—

**Mr Pattinson**—A mixture. There are students and research groups. It does have a heritage in that area. However, a lot of software distribution is done that way. A lot of people in the computer industry or people who require software for certain types of activity would be downloading it through the Web.

**Mr GRIFFIN**—Do you think the incidence of people using the Internet to engage in commerce is likely to increase dramatically or—

**Mr Pattinson**—I believe it will increase exponentially, because I think that information based products and services are where a lot of wealth creation is going on. In one of the lectures we present, we say that if you can digitise something—if you can convert something into a piece of information that can be stored and then sent around the world through a network—you have a product in that area that you can use as a basis for running a commercial business out of.

So I would say that a lot of products and services will come into that category. They will increase. Most of the information we have got can be converted into software. You have probably been hearing submissions about digital radio and digital television. All sorts of things around us are going to be put into this environment and they will be able to be traded. That will be a commercial environment. So, yes, I cannot say how much, but I would say it would be an exponential growth.

**Mr GRIFFIN**—What about the average punter though, the person who has actually got the Internet on at home for an educational purpose or for another purpose and is becoming more and more familiar with it: do you think there is likely to be a massive increase in their usage of the system with respect to purchasing?

**Mr Pattinson**—I do, once the perception of insecurity in transactions is overcome. That still remains one of the greatest inhibitors to commerce taking off in this area.

**Mr GRIFFIN**—Do you think that can be overcome though?

**Mr Pattinson**—I believe so. One of the lecturers who works for me in international marketing runs a business through the web. That would be a classic Internet start up. He does that in association with another large company, and he is doing very well through that.

In terms of transactions and conducting business, I would see it being an area where small to medium enterprise organisations will take hold of it. They will be able to grow fairly rapidly if they have the right products and services and also provide the right sort of what I call added value—not supplying just information but also consulting, advice or some sort of additional service on top.

**Mr GRIFFIN**—Do you think that security issue with transactions—handing over credit card numbers and suddenly finding out you have been stung for thousands—is capable of being addressed?

**Mr Pattinson**—It depends on who you speak to. I believe that the secure electronic transaction standard that Visa, American Express, Mastercard and others have put forward is probably sufficient for this environment, but I am not in a world that says that will not happen. Some people say it is adequate, some do not. I think for a lot of people that will be sufficient.

**Mr BEDDALL**—Do you use your credit card on the Internet?

**Mr Pattinson**—I do not, no. There you are, there is a good admission. Actually, that is not quite true. I have, but I did not complete the transaction. But that was not because of the security. It was because I went into Amazon.com, the electronic book store. I went through the catalogues, had a look at all the material and looked at some of the book reviews. The thing that put me off was that it was going to take me 10 days to get the book and it was going to cost me a DHL fee. I just wandered around to the Australian Institute of Management in North Sydney and got the book on the spot. So it was not so much security that was the issue there; it was more convenience. But that is not always going to be the case, especially when we get to the situation where some of those books can be downloaded electronically, as against having the physical thing.

On that point, I think one of the biggest challenges for a lot of smaller companies in this area is that, if they are providing information on the web about a service that is a physical service—for instance, you have probably heard about the services where people are selling chillies, sauces, food and that sort of thing—one of the biggest challenges for small to medium enterprise companies, apart from security, is having the logistics in place to be able to physically distribute a product around the world in a profitable manner. A lot of companies are having a great deal of difficulty with that aspect. It is all right if you have a product that is in the environment—that is completely information based. Once it becomes physical, it can be quite expensive to ship successfully.

**Senator GIBSON**—I would like to ask about education and the supply of expertise on the whole IT arena. In recent times, there have been various people saying that there is a worldwide shortage of expertise. Do you agree with that, and do you perceive that it is so here in Australia?

**Mr Pattinson**—I would agree with that, although, like all IT areas, there are shortages in some areas and not in others. I think in terms of—

**Senator GIBSON**—Looking ahead, where are the shortages in Australia over the next five years?

**Mr Pattinson**—I guess I am looking more at the business perception side. In terms of straight IT professionals, there is still room for development. There is still room for people to be able to design multimedia web sites effectively and creatively, and also the software support that goes with that, such as Java programming and other types of links, and bringing in traditional information technology architectures, so that they are able to operate in this sort of environment. There has been a lot of work on that in the last couple of years, and I think there is still a shortage of skills in that area.

My main interest in this is actually business people becoming much more aware of this technology and how they look at that technology in terms of developing business strategies. Is it the case that they now have to almost look at this technology evolving and their business strategies together to come up with new products, or does one drive the other? That is my focus. Right at this moment I would have to say in the area that I come from, particularly in marketing, we are desperately short of people with that sort of knowledge.

**Senator GIBSON**—What should government be doing about this?

**Mr Pattinson**—As I pointed out in this paper, I think that we have to look at the idea of coming up with some sort of standard in terms of what I would call some infrastructure literacy. As I pointed out in the submission there, Morgan and Banks last year did a survey where they claimed that in certain different levels of executives and business there was a very low PC capability. From what I could work out from the surveys they did, you are talking about people perhaps knowing about how to use a word processor, which we all know about, and probably using a spreadsheet. But how many people actually understand this sort of new environment and not only understand what it is but understand how to develop strategies? How do people, consumers or potential business people, go through this sort of environment, the world wide web? How do consumers go through it? How do you get them interested in your products and services and move that then to closing a business transaction?

It has improved a lot. I have been working in this area, as I said, for three years. At the start of that particular time, 80 per cent of the people in a classroom would not



know a thing about the Internet. They said, 'Oh, yes. That's something from university,' or 'It's something in Defence.' Six months later, probably about a quarter of the people had heard of it but did not really know what it meant. About the start of last year about half of the people knew about it. We get to late last year and we are starting to see most people not only knowing about it but, at least in our area, using it for research, using it do all their assignments. We are now, this year, getting a lot of business people in the courses, particularly in the postgraduate courses, saying, 'Well, look. It's now become a marketing problem.' We are getting questions at work about this new area. They want to know what they need to understand about this new marketing or business tool and how they can actually work it in with their strategies and operations. So I would say that particularly from the start of 1997 the awareness has been really strong. It has become stronger.

**Senator GIBSON**—In recent times there have been certain leaders in the area basically saying we could double the output of our tertiary education institutions in the wide area of IT in general and still not have an oversupply. Does that make sense to you?

**Mr Pattinson**—I would not necessarily say it is a numbers thing in terms of just doubling the output—

**Senator GIBSON**—No.

**Mr Pattinson**—I am not so much in agreement necessarily in terms of saying that there should be a straight doubling of the number of people getting degrees. It is also probably a case of incorporating this sort of material or these sorts of ideas within a lot of existing courses. For instance, where somebody does an MBA, a masters course or even an undergraduate course or one through TAFE or wherever we start bringing in a lot of these ideas where they are relevant to people's particular courses.

Sometimes, though, when a new area comes in like this you need to develop new subjects or new courses or new specialities in it to get the focus on it. Certainly we are in the position where we think we need to do that, but it may be within, say, three or four years from now it will be permeated throughout the business area. It may not necessarily be a straight area of speciality. It will be that you do a standard marketing strategy or a business strategy course or a finance course. It may well be part of it anyway. I guess it is a question of how you defuse this information into the structures that we have.

**Senator GIBSON**—Should governments be considering such things as offering extra scholarships for people to head in this direction?

**Mr Pattinson**—I think so—although, from my perspective, the government side should make sure that the funding occurs and that we have the bandwidth, the infrastructure and some materials in place to get people to a basic level of capability in this area, rather than just pure scholarships. So I would rather see it at the structural side

rather than necessarily at the scholarship side.

**Mr BEDDALL**—Do you think that Internet2 will be interchangeable with Microsoft of the year 2003? The question is: is it going to be Windows 2003 and Internet2, and will one key player like Microsoft dominate it?

**Mr Pattinson**—That is a very good question. On one side you have the current Internet community preferring diversity—actually not preferring anyone to control the environment. On the other side you have the bigger players who really would like to dominate. We have already seen Microsoft with their early attempts. With Microsoft Network their aim was to actually try to control this environment. They failed. They now have changed their company structure so that the products they are delivering are Internet ready, or have Internet links. Also, now you can download Internet Explorer 4.

If you asked me who is going to win in terms of Netscape or Microsoft in the browser area, I guess if I were going to put a bet on it—and it may be a better bet than the Melbourne Cup—I would tend to say that I think Microsoft's history suggests that they will take a much stronger role than they have now. Typically their first few versions of products in the past, such as Excel and Word, have been fairly weak. But on about their third or fourth version they tend to get very strong and then with their connections with all the operating systems and other products they do become dominant. So I would see them as being still a very significant player.

The question also is their relationship with Intel and some of the other hardware suppliers. History would suggest that, on the one hand, Microsoft is likely to strengthen its position significantly. I think we are almost up to about 25 per cent of browsers out there being Internet Explorer now. It was about only five or 10 per cent a year ago. So it would not be unreasonable to say that within a couple of years that figure will be getting up towards the 50 per cent mark. Who looks after the area is an issue from a government point of view.

**Mr BEDDALL**—In relation to the commercialisation of the Internet, once you get someone overly dominant, then it is who makes all the money, and there are the costs and fees that go with that. Microsoft has shown that it is capable of making large amounts of money.

**Mr Pattinson**—It is. But another side to that is that when we started looking at this area in 1994 we thought that the Internet was not going to be the avenue for electronic commerce. We actually thought at the time that CommerceNet, which was being developed at the time of which IBM was one of the main players, was going to be the environment that electronic commerce was going to occur in. That has not happened. Instead, we have companies getting together developing their own rigorous intranets, then connecting that into the Internet and using that as a transfer between other companies. But there are also companies that are now growing out of their intranets and bringing in other

companies in alliances to build bigger intranets or extranets—literally building other networks. But they are still interfacing through the Internet. So it is not a guarantee that Microsoft will do it, but it is a reasonable bet. Certainly in the immediate interface they will grow a lot stronger than they are now.

**Mr ANTHONY**—In your paper, which is quite different from the submissions that we have had but very interesting, you talk about—following on from Mr Beddall—the high speed broadband roll-out. There has been a big debate about cable and the huge amount of allocation of resources in that area which have been less than efficient. Of course, the issue of satellites is coming into it now. Where do you see the future of the next century? Are most people on the Internet going to be connected through satellites?

**Mr Pattinson**—People outside the cities in the country areas will either be connected through a broadband connection or satellite. I come from the bush myself and I think that there are some great opportunities for farmers in rural communities to do a lot of communication through this area. I would see a lot of them being connected through satellites.

Although, with deregulation at the moment, we are seeing some telco companies supplying cable services to some of the bigger regional centres. For instance, Ballarat and some other places like that are getting some cable vendors in there to put down a network for them. What I am really saying is that by the year 2000 or thereabouts we need to have everybody connected up with that sort of bandwidth so that they can use all the multimedia capability in the area.

You basically need a cable to start with. If you are up in Murwillumbah or somewhere around there and I want to communicate with you, I would want to have my laptop here, perhaps with a camera and a microphone and then I communicate with you with the same technology. That is one TV channel on a cable network. When you start looking at a suburb or an area, 500 channels is really nothing in terms of data service.

**Mr ANTHONY**—From a shopping point of view, I could be talking to someone over the screen and they could be literally showing me some products and asking, 'Is this the part you are after?'

**Mr Pattinson**—That is right. Yes. On the same channel you would use video conferencing and, apart from shopping, you would use that channel for other business activities as well. I think that is really the major area of cable. We all talk about pay TV and we have seen the money that has been lost there, but to me that is where the real game is.

**Mr BEDDALL**—Just to pick up on that point, a lot of the Optus stuff is actually a coax/fibre hybrid.

**Mr Pattinson**—That is right.

**Mr BEDDALL**—And it can only carry a bit of telephony and the pay.

**Mr Pattinson**—That is correct, which is why really within a very short time, if we are going to follow a broadband strategy, we are actually going to have to upgrade even the cable that we have.

**Mr BEDDALL**—Most of Telstra is fibre.

**Mr Pattinson**—Telstra is, but you are right about Optus. We are going to have another issue there with deregulation, too. A lot of people will build multiples of different types of infrastructure at the moment to try to avoid connection costs into Telstra's system. So we have got a couple of wires up there, but we are going to see a plethora of different technologies.

The point is that we have to have a broadband system that can at least give us that channel sort of capability and as we go along give us a faster version of that. So we probably have to go through a couple of iterations of that before we get reasonable communication.

**Mr BEDDALL**—If you were giving the government advice about what sort of bandwidth you need to go in, the best way to deliver that would be something like a cable transmission authority, rather than everyone else running around, laying fibre and then selling access to that like the electricity grids.

**Mr Pattinson**—It is a hard question. You asked there about whether we are looking at a deregulated, highly competitive environment or whether we are actually looking at a much more regulated, perhaps even almost like a monopoly or duopoly situation only for the cable.

**Mr BEDDALL**—That is what is happening with power transmission, basically.

**Mr Pattinson**—And also in Britain with British Rail and all that. They have rail track. So what we say is that we have an infrastructure management group and then everybody buys capacity from that. Yes, that is not an unreasonable idea.

**Mr BEDDALL**—I tried to tell Telstra lots of things and one was not to spend \$4 billion on a roll-out.

**Mr Pattinson**—But there are some real challenges if you look at the British experience. You have to make sure that that group is not just making excess profits for its shareholders. It is actually genuinely investing, not only in infrastructure for the present but in infrastructure for the right level of horizon for the future.

**Mr BEDDALL**—We have got a satellite up there that does not work, but if they ever get the satellite up, the digital technology from satellite gives you enough capacity. What about the old historic time delay mechanisms that always come from satellites even with telephony? How does that affect digital?

**Mr Pattinson**—I am not actually so familiar with the satellite technology from that point of view in terms of time delays. I guess the only real comment I can make on satellites, from my point of view, is that people like Motorola, who are putting up their low earth systems, and others are hoping now that they will make money out of being able to supply these services through there. Because of deregulation on the ground, they are not going to make much money out of local phone calls.

Yes, it is true that there is still development in switching and also in bandwidths, too. I know with cable at the moment that you can download with 10 megabits and you will be able to go up to 45 megabits a second, but you can only backload at around 56 or perhaps 128K in future. I think satellites have the same problem with backloading.

There is still some development to go in that area. From our experience, a 10 megabit per second download is pretty adequate for most businesses. You just have to be able to get the images down. You have to have a system with probably around 64 to about 96 megs of memory so you can bring down the image quickly. And it depends on how much back communication you need.

**Mr BEDDALL**—But 10 megabits gives you that video conferencing which is a little bit like the Keystone Cops. That sort of technology does not give you a clear image. You do not get television quality image, do you?

**Mr Pattinson**—Ten megabits? No, you would need to go up a bit higher than that, yes, but that would be sufficient for a lot of the activity we would do. Although for true video conferencing, yes, we would have to go up higher than that. Then that does imply at least another iteration higher than the technology that we have got at the moment.

**Mr BEDDALL**—Mr Anthony was talking about this and I think it is probably the next stage in Internet shopping. I ring Joe Bloggs' shirt manufacturing, he holds it up and says, 'Is this the one you want?' But you need a much better clarity of picture and a better capacity to be able to do that than is currently available on the Internet?

**Mr Pattinson**—Yes, although 10 would be sufficient for that.

**Mr ANTHONY**—Australians have a propensity to get new gadgets. We have all got mobile phones now. In your studies, how much of the Internet connection, if any, is going through a mobile phone?

**Mr Pattinson**—We have only just got mobile phones out with Internet connection

in the last six months. So it is very low at this stage.

**CHAIR**—It is very slow, is it?

**Mr Pattinson**—Yes, it is.

**Mr ANTHONY**—But as we move more towards that, people will perhaps have a main line or if you are out in the middle of nowhere, the bush or wherever, it all comes down to the next phase which is the reliability of digital. It is not reliable to date.

**Mr Pattinson**—Yes, there are certain parts in this town where you drive and you cannot get access.

**Mr ANTHONY**—Yes. It is getting worse. The more users that are coming on, the more it is jammed and the more it drops out. Are we going to see that Internet usage will predominantly have to be through cable? If you are going to go on satellite, you will drop out, won't you?

**Mr Pattinson**—I would think from a broadband perspective, yes, but once Motorola puts Iridium in place and some of those systems—

**Mr ANTHONY**—This is the low orbiting satellite, is it?

**Mr Pattinson**—Yes, the low orbiting satellite. They have about 64 satellites they are putting up. There are a number of other companies doing the same thing.

**Mr ANTHONY**—That is the same as Vodafone, because they are doing the same thing, are they not?

**Mr Pattinson**—I don't think they are using Motorola; they are using a different one. There are going to be a whole lot of other devices apart from mobile phones that will be used specifically in that area. We have got the mobile phone that can go on very slowly at the moment, but we will see generations of hand-held devices. You will have your GPS system on your tractor as well on the farm and as a salesperson you will have other sorts of things in your car. There are going to be a lot of devices there. I am not sure what percentage they will actually constitute of the total usage of the Internet. I cannot comment on that. It will be significant, but I cannot put a number on it.

**Mr BEDDALL**—With Iridium, is it the wrong impression that they are orbiting satellites? They are actually stationary, are they not?

**Mr Pattinson**—Yes, GO stationary.

**Mr BEDDALL**—GO stationary.

**Mr Pattinson**—Low orbiting is to do with their altitude, rather than the earth.

**Mr BEDDALL**—They spin where they are, rather than spin around the earth.

**Mr Pattinson**—Yes.

**CHAIR**—We are talking to Telstra tomorrow morning. If you had the opportunity to sit on this side of the table, what questions would you ask them?

**Mr Pattinson**—I would ask them about their strategy for data services. Frank Blount used to talk about that a couple of years back. I think his original strategy in working with Foxtel was to look at the cable area for data services. I would ask him for an update in that area to see whether he sees that as still being a central part of their strategy—data services for businesses and for individuals as well.

**CHAIR**—Are you talking about internally within Australia?

**Mr Pattinson**—In Australia. I think it would be in Australia as far as Telstra is concerned at this stage.

**CHAIR**—How about bandwidth between here and the States and here and South-East Asia?

**Mr Pattinson**—I mean that we have the broadband network, satellite network for Australia. The question of having high speed access to the US, to Europe—which I find fairly weak at the moment—and to Asia has to be asked as well. In future, that is going to be a significant part of our capability to be able to trade in information based products and services, to be able to have a pipeline big enough to be able to go into Singapore and provide all these channels and multimedia services. So, yes, you would have to ask them what their strategy was in that area.

**CHAIR**—In evidence last week the Australian Society of Science and Technology said that there is likely to be a shortfall which will start to show up within about six months, that it will peak and then come back.

**Mr Pattinson**—Yes, I read that and I think that is right. We need to get on to Telstra and Optus and the other guys to find out how they are going to fix that. I have not seen their plans in that area, so I think they need to be probed on that.

**Mr BEDDALL**—How does the Internet community view timed calls on the Internet?

**Mr Pattinson**—With great disdain. I would like to make one comment on that which I think is pertinent, and that is the way that Telstra has been handling the roll-out

of cable modems. The whole situation of charging in that area is actually very discouraging of people taking up the environment that we are talking about—using the cable environment for Internet access. Of course, you pay extra for the modem, but they are charging you for the amount of material you take down, not just by the hour or whatever, and at this stage that turns out to be very expensive.

**Mr BEDDALL**—What about Telstra's claim—and I think there is some legitimacy in the claim—that some people log on and just do not log off?

**Mr Pattinson**—I have never done that but, yes, there would be people who would do that.

**Mr BEDDALL**—They are just basically lazy.

**Mr Pattinson**—Yes.

**Mr BEDDALL**—Are you aware of a mechanism in technology that would drop it out after a while if it has not utilised? You really need to disconnect it.

**Mr Pattinson**—The provider that I use does that. You have to log in every 10 minutes or you will be disconnected. I use OzeMail—you probably know of them—and they have a system where you have to press something to stay logged on, or at least that is what you think is happening. My bill suggests that is what happening.

**Mr ANTHONY**—Is it a screen saver system?

**Mr Pattinson**—Yes.

**Mr ANTHONY**—Do they time the Internet in other countries?

**Mr Pattinson**—I do not know about that.

**Mr ANTHONY**—Is it not inevitable—I have to choose these words carefully—that it will be timed, because everyone is going to go to that form of communication?

**Mr Pattinson**—It will be. There is another issue in there as to where telecommunications companies are going to make their money. Some analysts out there believe that within about five years a lot of telecommunications companies will not be profitable because a lot of the telecommunications traffic will go into this environment. If they do not get control of a part of this environment, they will lose profitability. Their answer to that would be to charge for local calls or to charge for access into this area.

**Mr ANTHONY**—Or they go into retailing or something like that.



**Mr Pattinson**—Exactly. Undoubtedly, there will be a lot of pressure for them to do that. There are charged local calls in the United States, but that seems to be offset by lower access rates by the actual providers themselves.

**Mr ANTHONY**—Because of greater competition?

**Mr Pattinson**—Yes, because of greater competition, but also because people are now doing more of their telephony and their communication in that area anyway.

**Mr BEDDALL**—Other networks are not being utilised, for example—I am sure it is the same in New South Wales—Queensland Rail, the Queensland Electricity Commission and the defence forces. These are all parallel telecommunications networks that are not being utilised. Do you envisage that some of those could be used for broadband capacity, say, at places like Lismore?

**Mr Pattinson**—Such as using the microwave networks or the power lines?

**Mr BEDDALL**—Yes.

**Mr Pattinson**—It could be done. Although it was talked about a lot, particularly in the UK earlier in the 1990s when they were deregulating—you heard about all the utilities and British Rail doing it—from what I can see so far it has not evolved that way. You would need to have people within those groups, utilities or companies putting some strategic effort or focus into it, and then they would have to work out how they would make money from it.

Probably nearly 12 months ago, I had discussions with NBN, the Channel 9 supplier for the northern region of New South Wales. They were talking about the idea of using their repeaters and their systems to provide data services. They were keen on it, but the difficulty was that they were trying to work out what business they were really in and how they were going to make money out of doing it. What sort of access charge would you provide for that?

**Mr BEDDALL**—If I am a new telco, just started up in Australia, and being screwed to death by the current carrier and I come to you as a person who has got a capacity, all of a sudden there is a different proposition because all you are doing is selling on-line time.

**Mr Pattinson**—You have got excess capacity and you just sell them the capacity.

**Mr BEDDALL**—You sell them on-line time?

**Mr Pattinson**- Yes. Even then, even with a company such as NBN or one of the electricity supply companies, they have still got to think about that in terms of their

strategic plans. A lot of that, I think, goes down to whether they have really thought about it as an option as well.

**Mr BEDDALL**—One telco I know a bit about is actually looking at using that capacity to establish call centres in country towns—creating jobs in areas where you would not normally have it—and they are looking at using capacity like power generators or whatever.

**Mr Pattinson**—Power generators or the microwave or, in some cases, there are other optical fibre networks already out there.

**CHAIR**—Thank you very much, it has been most informative. People had lots of questions for you. As I said in the beginning, this inquiry is about a lot more than tax.

**Mr Pattinson**—Yes, I can see that, which is good to hear. I hope it goes well and that you come up with some very interesting and innovative ideas for the government.

**CHAIR**—We hope so, undoubtedly. Thank you very much for your input and for sharing your thoughts with us today.

[3.34 p.m.]

**BOULOUGOURIS, Mr Con, Solicitor, Phillips Fox, 255 Elizabeth St, Sydney, New South Wales, 2000**

**COUSINS, Mr Richard, Chairman, Internet Industry Association, PO Box 826, Epping, New South Wales, 2121**

**FAIR, Mr Patrick, Deputy Chairman, Internet Industry Association, PO Box 826, Epping, New South Wales, 2121**

**WARD, Mr Michael, Alternate Director, Internet Industry Association, PO Box 826, Epping, New South Wales, 2121**

**CHAIR**—I welcome representatives of the Internet Industry Association to today's hearing. In what capacity do you appear before the committee today?

**Mr Ward**—I am the corporate relations Vice-President of OzeMail and I appear in the capacity as Alternate Director on the Internet Industry Association board.

**Mr Fair**—I am a partner at the law firm Phillips Fox and I am the Deputy Chairman of the Internet Industry Association.

**CHAIR**—We have received your brief submission. Would one or more of you like to make a brief opening statement before we commence asking questions about what you have told us and about other things we have already learned in the course of the inquiry?

**Mr Cousins**—There are three points we would like to make. Firstly, Australia has been very slow in embracing electronic commerce and many people have looked at why. We have some views on that. I think that is for two major reasons. The first is the widely held perception in Australian business circles that the Internet is unsafe—we think it is far more a perception than a reality. The second is that the major banks have been quite slow in embracing the financial facilities for electronic commerce, and that has been an impediment. On quite a number of indicators we see the market taking up very rapidly. One measure that we use is the number of Australian domain names in the commercial sector. There were 10,000 of those at the end of last year, there are now 32,000. We see the move accelerating quite rapidly.

Secondly, we would like to comment on the whole regulatory framework. There is far too much regulatory emphasis on the Internet, much of it with local views of issues rather than the global view that we must take. The Internet transcends any state and even any national boundaries. While we have got to look at it from an Australian perspective, we must also do so from a global perspective.

As you may have seen from the thrust of our submission, an area of particular concern to us is the Australian Taxation Office's approach. It is one of many departments where we have felt differing views, but the specific views in the Taxation Office that concern us are in their report. Some we agree with. We certainly agree with such things as the Taxation Office becoming a Net citizen and the idea of ACN numbers on appropriate pages on Web sites. They are positive things. Our concerns are at some of the recommendation where we feel that the advice that may have been given certainly does not reflect the way we see the industry. We also see a basic misunderstanding of how the industry will evolve over the next year or two.

Let me give you three indications of that. One is that on behalf of the association I participated in a couple of the Taxation Office meetings. In one meeting in particular the whole thinking was what was of concern, not what was said. The thinking was that we should limit electronic transactions to \$100 because that is the largest banknote we have, or \$500 because that is what you can get out of an ATM. If we start limiting things we are going to have more problems.

The second is the view that the industry will come down to seven major ISPs and, therefore, you can regulate it. We think that is wrong. There will be seven large ISPs, but we believe the industry is going to shape up much more differently than that.

The third is the suggestion by the ATO that it costs about half a million dollars to put an electronic commerce site together and therefore that it will, again, be easy to police. That is just dead wrong. There are some people paying that sort of money, but they should not be paying that sort of money. It can be done much cheaper. In terms of the regulatory environment we would say two things: it must be a free trade zone, while we protect our nation's ability to raise revenues; and there must not be any new taxes on the Net in order to make us competitive internationally.

Thirdly, we feel that we have got to look at the opportunity. We believe that, as a nation, we must move to being a Net exporter of electronic commerce. We should not be looking at what we need to stop things happening. We have got to look at what we can do to make more happen for Australia. We have the ingredients to do that. Many of them are not working yet in terms of a harmonious environment. What we feel we need there is a very light regulatory hand. We do need regulation, we do need to stop things getting out of hand, but we do not need the heavy-handedness that we are seeing from some quarters.

We support the idea of industry incentives for the development of the electronic commerce industry. We are not talking about the Internet industry, per se, but we are talking about the overall industry environment. In summary, we feel we need a sound, uniform national policy. One of our concerns is the state orientation of a lot of thinking, say in the area of content, which we think is not only impractical but is just going to slow things down.

To us, we need a positive rather than a preventative approach to all that we are doing. If I could just put in some figures. The AIIA, which we work closely with and support, provided some 1995 export figures where the wheat exports were \$2 billion, the wool was \$3.4 billion and the information technology industry was \$3.6 billion. It is a major area.

I put it to you that the information technology industry is going to merge into the Internet industry. That is why Microsoft is fighting for control of the Net browser market and that whole arena. As a country, we must recognise that the Internet and the issues related to that are going to be a major economic and significant factor for us. Therefore, the opportunity to ride the Net wave must be taken up because we cannot keep riding on the sheep's back.

**CHAIR**—Thank you very much. You mentioned the banks and how slow they have been. Are you aware of the fact that the NAB intends to go with on-line banking next month?

**Mr Cousins**—Yes, we are aware of some of that. I think the real issue is that we still feel they need encouragement—or a kick in the tail is the polite way to put it. It has been a factor that has held back electronic commerce. There is a lack of confidence because, if you want to do on-line transaction banking at this stage, you cannot do it with a major recognised brand name. You can technically do it, and that has been possible for quite some time. We see that a lot of this is a confidence issue and we see a need for that to be accelerated and accentuated and not just made technically available.

**Senator WATSON**—How do you do that? Encrypting is one way to make it safer. The banks are going to lose a lot of money if it goes wrong.

**Mr Cousins**—I would suggest that the banks have been ultraconservative in this when they could have taken a leading role—we are not trying to sit here and bank bash. My personal comment on that when people ask—and I do get asked this a lot—is that I would much rather use my credit card over the Net than I would give it to a waiter in a restaurant where he takes it out the back and I do not know how many copies makes.

Michael made the point this morning that when there was water trouble in Sydney and the quality of water was an issue, we saw politicians drinking a glass of purified water. I am not suggesting we go that far but perhaps we need to see public figures using the Net for transactions. We need to see some examples encouraging business to use it. The encryption facilities are there and the tools are there to do it. There is a lagging perception that it is unsafe.

**Mr Ward**—I think the Internet industry is a young industry and most of the organisations involved in the provision of Internet services are small start-up companies. Three years ago our business comprised seven people in a small room in St Leonards and

it is now over 300 people with offices in Sydney, Melbourne, Brisbane and Perth. What we are looking at, I suppose, is trying to integrate our service offering into the normal financial system.

If someone tries to join OzeMail on-line and put their credit card details on-line, we have had tremendous difficulty getting the banks to agree that they will manage that transaction on-line so that, in the same way you might use it at a shop or in the same way as you would use it over a telephone service, the liability for that transaction is not worn by the bank. They claim to authorise the card but, in fact, it is not a real authorisation, so we are wearing several hundred thousand dollars worth of bad debt.

If I am the merchant and, instead of having a shopfront I have an Internet shopfront, I need to have some level of confidence that when someone puts a credit card through my system and it goes to the bank and the bank says, 'Yes, you can accept that transaction' that that is a genuine acceptance of the transaction and that the liability is worn by the provider of the card and not by the merchant. To date, that has not been the case.

It has meant that, for example, if we look at overseas businesses where Australians are shopping overseas, they are shopping overseas with confidence because of the organisations they are shopping with, but here you cannot get that real time banking cover for that transaction, so the merchant has to wear the liability. That is a significant disincentive for merchants.

**Mr BEDDALL**—Is that the same for Visa and Mastercard?

**Mr Ward**—Yes.

**Mr BEDDALL**—But you are using, say, Citibank Mastercard—

**Mr Ward**—Yes.

**Mr BEDDALL**—That is a full transaction.

**Mr Ward**—Approved at the point of the transaction. If we are going to Amazon Books and buying books on-line, a credit card is approved at that point, Amazon Books has confidence that that is a real credit card and a real transaction and they can put the books in the post and send them to you. In Australia you cannot have that confidence.

**Mr BEDDALL**—Even, say, National Mastercard or Commonwealth Bank Mastercard?

**Mr Ward**—No.

**Mr BEDDALL**—Have you approached Mastercard and Visa rather than the banks?

**Mr Ward**—I cannot tell you how much detail we have gone into in this exercise. We have in fact got to the point where we have been exchanging faxes with some of the credit card managers—Amex, for example—in trying to have an authentication process which is a genuine one, because what we are trying to create here is an instantaneous experience. A person comes on-line, they put their details in, they then use the Internet. We have been wearing that liability; our merchants have to wear that liability. We would prefer it if it were a real life credit approval and that liability was borne by the banking institutions or the card providers.

**Mr BEDDALL**—Amex and Diners are not Australian banks.

**Mr Ward**—No, they are not Australian banks; but the financial institutions through which they transact those approvals are banks. All of ours, for example, go through the Commonwealth. They will approve a credit card transaction with an Amex card and we will find out 10 days later that the Amex card is invalid. We even wear the cost of putting the transaction through, let alone the cost of the service that we have provided in that period.

**Mr ANTHONY**—Can I just move back one step. If I order a good through the Internet, I give them my Amex card—

**Mr BEDDALL**—Whip around and tell them it is stolen.

**Mr ANTHONY**—Yes, I have stolen it. What happens then? Do the goods come to me?

**Mr Ward**—What you will find in many cases is that the merchant at the other end is taking that card number manually and ringing up to check that that is a valid card before they ship the goods. So the whole point of electronic commerce is lost in this equation.

**Mr ANTHONY**—But they must do that anyway. They are fools if they do not.

**Mr Ward**—But they do not need to. We could all validate these processes instantly if the financial sector was prepared to support the medium in the same way—

**Mr ANTHONY**—They are not at the moment; that is your argument.

**Mr Ward**—We have been going through this process intensely for some 12 months trying to get to the point where the financial sector was prepared to cover these types of services to encourage people to come on-line. We have got machines waiting to

hold shops on-line and we have got people waiting to put them in there; but they need this cover, because otherwise they are carrying the liability. That has been a major problem.

**Senator GIBSON**—Why won't one of the smaller banks break and start that service?

**Mr Ward**—That is a very good question.

**CHAIR**—What is the real difference between the environment here and that in the states? An Amex card is an Amex card, Visa is Visa and Mastercard is Mastercard.

**Mr Ward**—That is right; but it is the bank through which you pass the transaction that is the point at which the authorisation occurs, or they forward it to the originating bank or card provider for authentication. That has not been happening today.

**Mr BEDDALL**—Often authentication is not even done in Australia, though.

**Mr Ward**—Often it is not; that is right. It is done internationally.

**CHAIR**—But you are saying to me that the Yanks do it.

**Mr Ward**—Of course.

**Mr Cousins**—We are using this is an illustration—

**Mr Ward**—That we are at least a year or two behind.

**CHAIR**—And they have multiple banks. There are banks everywhere.

**Mr Ward**—Absolutely. It is not a complex task. They have been unwilling to provide this level of service to the Internet.

**Senator GIBSON**—Which suggests that there is really an opportunity for an Aussie Home Loans type to break the system.

**Mr Ward**—A massive opportunity. When I spoke to the retail banking conference a few weeks ago, I suggested that we would be very happy if Telstra became a financial institution. Telstra can not only validate the card but also validate the details of the person and the fact that a person lives there, has a phone, has a phone number and are a real entity.

**CHAIR**—You do not mind if we ask Telstra that tomorrow, do you!

**Mr Ward**—I think that has undermined confidence in the use of vehicles like



credit cards on the Internet. With the Wallis inquiry opening up the options for a number of players, such as Telstra, to become financial institutions, we believe that we will see a great proliferation of that, and that we will see electronic commerce seriously take off in the new year.

**Mr BEDDALL**—I want to come to the issue of electronic commerce, because one of the things that we have had a bit of discussion about from witnesses today—and trying to get away from the people who are scared of the Internet and they are going to close their business because they cannot compete—is the problem for people who can compete pricewise. On a domestic level, they have to charge wholesale sales tax and pass that on to government, whereas if they buy the same product internationally, it is only uncompetitive because there is no wholesale sales tax charged at the point of sale. How do you give that transaction equity with the one on the domestic level? How do you stop the tax base bleeding? To take that a little bit further, if we do go to a broad based consumption tax, there becomes an incentive to buy through the Net to avoid the tax rather than for any other reason to use the Net.

**Mr Cousins**—I think one of the issues is that we have to look at rethinking the way we do business. If you take some of the great success stories on the Net such as Amazon.com, it is because it is a virtual bookshop and the whole process. There are several others like Dell that have been looked at. But I think many of our businesses need to rethink their model and look at being competitive. The book companies here are losing book sales. The figure of 19 per cent of academic books coming in via the Net has been put up. I have not seen it substantiated, but it has been claimed. The real answer is that, long term, Australian companies should be looking at changing their business practices not just from a tax point of view but to provide that more economical and more effective delivery of products to the consumer and the business.

Our view is that not only should we be looking at that to stop the replacement of books coming in externally, but why can't we also be having the company that sells the books to the rest of the world, or certainly to Asia? If you come back to confidence being a large part of it, Australia has a high respect in South-East Asia. Our currency normally is a lot stronger than some of those other ones. Again, we have got that whole chain. So I think, in the longer term, we have got the wrong view of it if we are looking at it just from the tax evasion or sales tax evasion point of view. There certainly is a leakage issue, but it is not the be-all and end-all of the equation.

**Mr Ward**—There are two points that I would like to make. Firstly, the export opportunity that exists is far greater than the import that is occurring, which might be below the tax system at the moment—the import of small numbers of goods by individual buyers. The export opportunity for Australia, both in terms of its intellectual property and its goods and services, like education, health, and all those kinds of things which we currently sell physically or in terms of people travelling, we can sell through the Net. That is a vast opportunity for this country. Small businesses will become global businesses. A

company like GMH which sources from 1,000 suppliers all over the world can source from 10,000 suppliers all over the world with pretty much the same technology they currently use. It is, in a sense, an opportunity for us to create an export market.

In terms of a diminishing domestic tax base, because people are going to buy goods in tax havens or areas where the tax is cheaper, I would not have thought the tax differential was going to be the most significant aspect of that. I would have thought the size of the market and the size of the operation was going to be a greater differential in terms of pricing. So we will still buy shoes from Asia, and we will buy them over the Internet, and we will have our size measured, and we will give them our footprint, and they will make shoes for us, and it will still be cheaper than it is here, simply because of the volume of shoes they are making. I do not think the tax is going to have nearly the significant impact that a number of commentators have said it will.

If we want to be specific, if you were looking at, for example, CDs being imported here before the decision about parallel imports, even if I as a domestic user were importing, say, 10 CDs a day, which could get me in under the threshold of Customs, I would still only be importing something like 3½ thousand CDs a year. It is a very small number of CDs compared with the entire CD market of tens of millions sold every year and the tax associated with that is also quite small. I think the ATO has, in a sense, got the little end of the stick at the moment.

What we are planning for in our industry is a massive growth of businesses doing what they currently do but doing it through the vastly more efficient mechanism of the Internet—exchanging goods, suppliers talking to wholesalers and distributors and, through electronic commerce, becoming far more global in who we supply to and what we supply. In many ways, our domestic tax base is going to be boosted significantly by our ability to sell out of Australia rather than importing into Australia. I do not think we will see huge numbers of consumer goods slipping in under the tax net anything like what the ATO seems to be envisaging in their report.

**Mr ANTHONY**—From evidence in other committees, somewhere between 10 and 14 per cent of CDs are coming through the Internet. That is a pretty substantial number from a tax revenue angle.

**Mr Ward**—Yes, but we need to differentiate which CDs are currently available in the market in Australia. Much of the argument about parallel imports was about the importation of CDs which were not currently licensed for manufacture here. That has always been the case for CD imports, and there have been import shops for a long time. I draw that differential quite considerably.

The second thing is that we are in a competitive international market. This technology is allowing that market to extend well beyond national boundaries and we are going to have to recognise the fact that, if we are not price competitive in an international

market, then we need to be looking at our cost structure here and maintaining our competitiveness internationally.

I do not think our tax base is ever going to significantly change if we continue to look for the kinds of principles that the ATO looks for in terms of physical establishment, the principle of residence, source principle and stuff like that. That, in a sense, is the old world. It is like trying to tax horses. There is just no money in that any more, because there are not a lot of horses going around. CDs are not going to be imported because we are not going to have the physical good to import. You are going to download it electronically and the person at the other end is going to be managing a transaction in their territory. So the challenge for us is to make sure it is our territory that is managing the transaction

**Mr BEDDALL**—Tax the plastics.

**Mr Ward**—That is right. We tax the physical good. The physical good is—

**Mr BEDDALL**—You are still going to need a physical good, aren't you? You will download onto the CD?

**Mr Ward**—Yes, you will download onto a writeable CD, or into your system which will automatically store the data and will allow you to replay it at any time.

**Mr BEDDALL**—Books are an interesting issue. I assume they do not attract import duty, and they do not attract sales tax either, do they?

**Mr Ward**—Neither does software, for example.

**Mr BEDDALL**—But there is 19 per cent import and there are issues of access because the publishing cartels have the world carved up into two different areas. We happen to be in the British one rather than the American. So a lot of those books, I am assuming, are books you cannot get. I am child of the 1960s and I cannot get *Woodstock*, for example, on CD in Australia. I am about to see if I can get it on the Internet. I am sure I can.

**Mr Ward**—I am sure you can too.

**Mr BEDDALL**—And, again, that is the availability of—

**Mr Cousins**—The model we need to look at in that environment is that, if there is a product that is being brought in—let's say it is bibles just to pick something that is separate—rather than each one of us bringing in five bibles per year, it has to be far more economic for someone to say, 'I'm going to bring them in in a container load and sell them to you. But the means by which I am going to distribute them to you is over the

Net.' You use the same model for ordering, but you physically move the goods in a far more efficient way. That is the mentality that we have got to get to rather than saying, 'Let's stop people buying bibles over the Net because they're bringing them in under the threshold.' That is the change of paradigm thinking we have got to get in so many of our businesses—from books to CDs, to bibles.

**CHAIR**—Isn't Woolies opening up regular weekly supermarket shopping through the Net now?

**Mr Ward**—Yes, they have been trialling it in Auckland and it has been very successful.

**CHAIR**—I thought I read last week that they are doing it in Queensland.

**Mr Ward**—Yes, they are setting up a trial there.

**CHAIR**—You give them a regular shopping list and, automatically, you get one loaf of bread and two litres of milk every week, but you do not get paprika except when you order it.

**Mr Ward**—That is right.

**Senator GIBSON**—President Clinton's statement of July basically set out a minimalist regulation for the US. I assume your association basically goes along with that?

**Mr Cousins**—Absolutely. The idea of a 'bit' tax as the Europeans are pushing, first of all, has a lot of downside to it, even if everybody was adopting it. But the US controls the Internet electronic commerce future, at least in the foreseeable decade. Without their support, if we try to go any other way we are crazy and I think the Europeans will probably isolate themselves to a very large degree if they go that path. The Canadians have brought in some regulatory controls and there is a mass movement of Internet service providers out of Canada, across the border and operating from there.

**Senator GIBSON**—Can you give us evidence of that?

**Mr Cousins**—Yes, one of us has got the details on that.

**CHAIR**—Could we have that, please?

**Mr Ward**—Yes, I will get someone to send me some written documentation on it.

**Mr Fair**—I think that is a good illustration of bringing together the answer we gave to the question asked before about eroding the revenue base. The answer is that the Internet brings the revenue base into play as a competitive factor for Australian industry,

and there is no escaping it. It is not for the government to try to maintain the existing sales tax revenue base on Australian products and to render them uncompetitive in the international market.

The government has to change its methodology and realise that those taxes are now in play as a cost in competition with international products. We have to adjust the revenue base creatively to try to make sure the products and services that Australia has a competitive advantage in relation to are not rendered uneconomic by the way we render our taxes, rather than taking the approach which some have suggested of attempting to play around with the way the net is regulated or the way people can transact on the net to create artificial barriers to defend an old paradigm. If you do that, you just get migration out of the country.

**Mr BEDDALL**—This is not good news for the PAYE taxpayer, because the only methodology which can be used to increase the tax base is to tax the person rather than the goods.

**Mr Ward**—That assumes, though, that we simply reduce the number of goods we sell that are Australian made and Australian manufactured. Let us forget the Internet exists. People have been buying things from mail order catalogues overseas for many years.

**Mr BEDDALL**—Not in large numbers—not Australians.

**Mr Ward**—But they have, and so the same question applies: how do you deal with that as a potential income stream to the government? The way we have dealt with that is by reducing the amount of stuff anyone can import to a dollar amount not exceeding, I think, \$50. You need to ask yourself whether we should be spending a very large amount of time trying to manage the below \$50 imports that individuals are making as a significant leakage of our tax base or whether in fact we should be looking at the larger end of town.

The consumer driven electronic commerce is not going to be the most significant factor in this equation. Our projections are that, in the next two to three years, up to 80 per cent of electronic commerce will simply be business to business commerce. It will be the transactions of business between suppliers, retailers, wholesalers and distributors in exactly the same kind of format they are using now, but with a global market. They can transact it much more simply and straightforwardly over the Internet, whether it is a private Internet or whether it is a public Internet.

**Senator WATSON**—But, using this new power, how are you going to ensure you do not erode your tax base without, at the same time, driving this industry offshore? That is the big question you have got to ask yourself. How do you do it?

**Mr Ward**—I think that is the same question we have to ask when we are looking at the general arrangements of the World Trade Organisation or within GATT. We are talking about a global free trade zone here: we are not talking about a European free trade zone, an Asian free trade zone and a North American free trade zone; we are talking about a global free trade zone.

**Senator GIBSON**—That is right.

**Mr Ward**—The Internet makes that possible technically. What we have to work out is how best to manage our domestic needs in terms of our tax to ensure we are part of that global trade zone but that we do not undermine our quality of life.

**Senator WATSON**—That is the question I am asking: how do we do it? Internationally, there is a lot of breakdown in that because you cannot get agreement.

**Mr Ward**—Yes, I think that is very true.

**Senator WATSON**—So how do we manage it?

**Mr Cousins**—We are not suggesting it is going to be easy. I do not think anybody suggests it is going to be easy.

**Senator COONAN**—I think we are all interested in what the light regulatory hand is going to do.

**Mr Cousins**—I suppose we are turning it around in saying we have got to take advantage of the opportunities, not try to protect unprotectable approaches. I think that is the challenge internationally.

**Senator WATSON**—But, if we accept that philosophy, we have got to be careful that we maintain some sort of tax base.

**Mr Cousins**—Absolutely.

**Senator WATSON**—We cannot just wipe it off.

**Mr BEDDALL**—You are running into reform fatigue.

**Mr Ward**—Yes, globally we are running into it.

**Mr BEDDALL**—Yes, that is right. Australians have been at the forefront of breaking down barriers. You have seen in two recent decisions by the government that it does not want to do that any more—cars and TCF. It does not want to be at the forefront—maybe for all the right reasons—but it has gone backwards in the march to this

wonderful world that you say Internet brings us. What makes you think that all of a sudden there is going to be a quantum leap in information technology?

**Mr Fair**—Isn't the answer to that question that it is being put as if the alternatives are that in a free market there is no tax revenue and in a market with frictions and barriers there is some tax revenue. That is not right. All our competitors have to raise taxes and have different competitive disadvantages.

To take the CD example, although it is possible to buy CDs on the web for \$12 and \$20, if you want to buy one that is current, you have to buy four or five for it to be a good deal, because of the courier cost of getting it to you. The courier cost is consolidated, and it is the package which starts to approach a collectable duty package which is an economic purchase.

Customers do not usually want to buy four or five CDs at once. Overseas suppliers have a competitive disadvantage selling into the Australian market compared to local shops. Even in cyberspace there are plenty of factors in play which give the government scope to impose some revenue generation—hopefully on higher volumes sold to a larger market.

**Mr BEDDALL**—Today it has been strongly put to this committee that, by reducing the amounts down to, say, \$20 or zero and by clearly defining what you tax, you stop your revenue base from deteriorating but you do not stop the trade factor. What happens is the Internet competes on the same basis as the domestic supplier. Do you see that as a false argument?

**Mr Ward**—No. I do not see it as a false argument, but it is dealing with the small, somewhat trivial end of the business. Patrick is right. The only way to get a financial advantage out of buying CDs in the US is to buy in bulk and have them packaged in bulk. That tends to attract the attention of Customs, so people tend not to do that. They tend to buy things they cannot buy here easily.

**Mr ANTHONY**—One of the examples we had today was 5,000 shirts which were brought in. They were all indemnified to individuals. It took Customs 32 hours to clear them all, and they were all under the threshold.

**Mr Ward**—But that is 5,000 shirts, not 500,000 shirts.

**Mr BEDDALL**—That is one shipment.

**Mr Ward**—We all know that a lot of black market trade goes on in Australia. More tends to be in services than goods.

**Mr ANTHONY**—This was legal. It was all above board.

**Mr Ward**—My concern is that we are over-emphasising what is going to be a relatively small number of goods. Once you have a CD shop in Australia which is on-line and has the same stock levels as one in the US, the price differential will disappear. You will be able to get the goods much more quickly and cheaply by buying them through the CD shop in Australia. Whether you buy them on the Internet or front up to the shop is a completely separate issue.

**Senator GIBSON**—If we change the tax system to a broad based indirect tax, taking up Patrick's point earlier on, will we not be advantaging Australian manufacturers or suppliers and helping their exports?

**Mr Fair**—If we spread the thing more widely, we should then have a fairer market for them to compete internationally.

**Senator GIBSON**—Does your association as a group have any views about the introduction of such a broad based indirect tax?

**Mr Ward**—No. That would be a good discussion.

**CHAIR**—I had not thought about this until just now. If you zero rate exports, what on the Internet is an export?

**Mr Ward**—Any intellectual property that is available to be bought from anyone who supplies that.

**CHAIR**—But how do we define 'export' on the Internet?

**Mr Ward**—The way we would define it—

**CHAIR**—Can we call a ticket on JAL from Tokyo to Melbourne an export?

**Mr Ward**—Is it purchased from Australia?

**CHAIR**—Regardless of where it is purchased from, we can say that we will zero rate that ticket because we want export income, and that is income.

**Senator COONAN**—We are still coming back to source, and that is a real problem.

**Mr Ward**—Why is it a problem?

**Senator COONAN**—Who sources it?

**CHAIR**—But how do you zero rate a service on the Internet? Remember, you say



it is a broad based goods and services tax, so, for the first time, we are going to tax services, whether it be hairdressing, accounting, or computer programs, everything is taxable—at a lower rate, but they are all taxable. Once you get it up on the Internet, how do you know where the hell it has gone?

**Mr Ward**—A transaction occurs; money changes hands. That is the point at which the tax is applied. If that transaction occurs in Japan rather than here, then it is the Japanese end where the tax would be applied, not here. If we do not have an agreement with Japan about a settlement for that process, then the tax goes to the Japanese government and not to the Australian government. Our argument is that we need to make sure we become a transaction hub. We need to make sure that in this region, in particular, where we have established financial institutions, a stable form of government, we make ourselves competitively advantageous by becoming a transaction hub, by becoming a place where those Internet transactions occur.

**Senator GIBSON**—What do we need to do to achieve that? What is missing now?

**Mr Cousins**—That goes back to the whole issue of encouraging the roll-out and encouraging electronic commerce rather than putting any more barriers in place.

**Mr Ward**—I think one of the defining questions in the ATO report and in Internet commerce generally is identity—being able to determine the identity of the business or the person conducting the transaction. We have at the moment a situation where we have no formal process for determining the identity of a person transacting over the Internet in this country, but we are in discussions about setting up certification authorities to give people Internet passports, digital signatures. It seems to me—

**Senator GIBSON**—Does this happen in the States, for instance?

**Mr Ward**—Of course. You can buy a digital signature for \$5 on the Internet from various sites, but it is only worth \$5. You cannot buy a passport from the US government for \$5, but if the Australian government—and this is a point I made to Senator Alston a few weeks ago when we were in Canberra—and our institutions—be they the banks, Australia Post, or whatever—put their standing behind a certification system which recognises digital signatures and gave them value, the same value in fact that we give our passports with the whole 100 point check, photo ID, and the whole thing, then instantly we would be at a competitive advantage. When someone came to an Australian site they would know that they were conducting business with a genuine, certified authority which the Australian government had backed.

**Senator GIBSON**—It is a good idea.

**Senator COONAN**—That is where the transaction would take place, is it—at the transaction hub?

**Mr Ward**—That is where the ATO would be able to identify the transaction because they would be able to identify the point. If it was not transacted with an Australian bank, then it would not be transacted here. But it seems to me that that is a critical step in this process where we can steal a march on them.

**Senator GIBSON**—That is what we need to do, actually.

**Mr Ward**—Because if it is not us, it will be KPMG, Price Waterhouse or Arthur Anderson. They are trying to set themselves up as multinational certification authorities and then national governments will really be customers.

**Mr Fair**—As an organisation, we have made a submission to the minister for communications supporting the step that has been taken by the government of encouraging the public key authentication framework and being a bit prepared to indicate its approval to the development of an authority doing that. But there is a lot more that could be done and it could be done a bit more aggressively to—

**Senator GIBSON**—Could you let us know what you believe the government could do to help Australian development of electronic commerce?

**Mr Fair**—There is discussion about legislation to recognise digital signatures and the legal effect of digital signatures. There is tension between the international models in terms of how they have or have not been successful. But we have not seen a discussion paper on that or much policy development focusing specifically on what Australian legislation might do and how it might work.

**Mr Ward**—The Victorian government currently has draft legislation it is considering in this area.

**Senator GIBSON**—Do we need legislation to take this step?

**Mr Ward**—I think it would lead the way for the Australian government into this process. You can buy a digital signature for \$5, but that is all it is worth. There is no support for that.

**Senator GIBSON**—Sure.

**Mr Ward**—If the form of identification on the Internet is going to be a critical thing—and I think from the tax office's point of view, particularly when companies are conducting a business, it is a critical aspect where you can identify this company has made this transaction and it has gone to book here and it should be part of their taxable income—then that is going to really allow us to take a step forward. So I am happy to undertake to get some documentation to the committee on that.

**Senator GIBSON**—This week's *Economist*, in an editorial on the perils of electronic shopping, makes the point that 'some future analysts point to the need for fewer consumer protection laws, not more', and is really pushing the point that reputation will depend on brands and self-regulation within sectors of the industry. Do you agree with that sort of general thrust?

**Mr Ward**—I think it is one thing to go to a supermarket and be able to identify brands. It is very different when the supermarket is 54 million Web sites. Brand recognition is going to be increasingly difficult.

**Senator GIBSON**—But if those Web sites were aggregated into a mall that had a brand that stipulated—

**Mr Ward**—That had a brand and authentication stamp on it and said, 'This is a trusted site on the Internet and your credit card will be kept private or your bank's details will be private,' then yes, that will make an enormous difference.

**Senator GIBSON**—The suggestion is that, with signatures, the Australian government should stand behind and establish a brand for credibility.

**Mr Cousins**—That gives us a regional advantage—perhaps even an international advantage—but I think the whole thing comes back to credibility. The reason people are happy to buy books from Amazon.com, which no-one had heard of two years ago, is that it has got that reputation. You can set up the same operation as Fred Bloggs Books and probably get nowhere, and therefore in a lot of sectors it is a confidence issue. As you were talking, I was thinking of domain names. We solved the domain name problem in the last year by giving it some credibility and taking it off the front pages as being run by an academic.

I think what we have got is a lot of little instances like that, all of which need to be looked at. Digital signatures is one. There are a number of areas where either the industry can sort them out or private enterprise will. Some need government kicking or prodding or standing behind. But what we need is a proactive environment that solves all these little problems. The last thing we need is 'Oh, there is a problem there, we will put some new regulation in place.'

**Mr Ward**—Or 'We will stop that trade because we do not know how to tax it.' The form of identification that we currently use in Australia for Australian businesses—registered business names or Australian company names—seems to me a perfectly valid tool that you would use on the Internet; and the ATO has picked up on that. The next step then is that we just need to authenticate people who are not businesses, and digital signature technology is currently available and is a process which is not too difficult for most Internet users to come to terms with. It seems to me a perfect way of doing that.

**Senator GIBSON**—You said there were several of these, if you like, relatively small things that can be pursued. Can you advise us later about that?

**Mr Cousins**—Yes. What we would like to do is come back with a written and perhaps more detailed submission in some of these areas following today's presentation.

**Mr Fair**—Can I just bring those comments we were making back to the ATO report, that is, the recommendation that there be a licensing of Internet access providers and a maintenance of IP addressing as a sort of complete list for authentication. We oppose that on the basis that it is a new level of identification where the medium does not require that. The use of ACN numbers, registered business names and a free market use of a certification system with authority behind it will make people as identifiable over the Internet as they are in ordinary commerce.

What I regularly find interesting in government reports discussing particularly Internet content, and the policing role that government needs to have to deal with some aspects of the content on the Net, is that it is a communication medium and you can get around it very quickly. You can see what is going on by surfing it—in fact a lot more easily than you can by knocking on people's doors and visiting their premises and doing physical things. In that way it should not be necessary to have new forms of registration and licensing and new systems to verify who is there—provided existing laws about putting your ACN number on business documents and having your business name registered are applied on the Internet as they are in ordinary documents.

We have a second draft code of conduct which is getting a little dated now and which deals with issues that, since its publication, have been allocated severally to the ACCC, the ACA, and the ABA. In the next draft, we will try and deal with that and split up the issues. But the part that the ACCC will be dealing with says that people who comply with our draft code would identify the entity that the customer is dealing with and the legal persona behind the commerce side. It is a code like that, the use of ordinary tools, which is a better solution, we would say, than the proposal that the tax office is making.

**Mr Cousins**—Certainly, the proposal that has been made that IP addresses be tracked down involves horrendous cost and can be easily circumvented.

**CHAIR**—We are going to have to go, but could I ask you one last question. Back again on the NAB: is the fact that they are this month going on-line with electronic banking going to help this issue of credibility in the Australian marketplace?

**Mr Ward**—Unquestionably.

**CHAIR**—And will it also help solve part of your problem with credit cards?

**Mr Ward**—We think we are halfway there with solving the credit card problem with at least the four major banks.

**CHAIR**—Because we are almost there with Mondex.

**Mr Cousins**—Mondex has been delayed far longer than it should have, because the licence for Mondex happens to be owned by the four major banks in this country. That issue is about to be solved. I suppose the point is that it is running at least a year late. It should have been solved a year ago. Where we are now with the NAB coming out—it should have been the ANZ and Westpac and the NAB and the Commonwealth Bank doing that 12 to 14 months ago, not one of them waiting for which one is going to break ranks and move from the very nice conservative environment. I think that is the underlying problem that we do not want to see perpetuated in all these future aspects.

**CHAIR**—When do you think the other three are likely to go on-line with Internet banking?

**Mr Ward**—Within months.

**CHAIR**—They are close enough technologically.

**Mr Ward**—They all know where each other is.

**CHAIR**—I did not think to ask the NAB that.

**Mr BEDDALL**—My question is to turn the tax issue another way. Sometimes when you are doing an inquiry like this you get skewed by the number of witnesses you get. To date we have been overrun by people who sell physical goods. So that becomes something that you are very conscious of. My overall view is that it would be a much smaller proportion traded on the Net of physical goods as compared to intellectual property. Have you got any skew about what the make-up would be—70:30, 80:20?

**Mr Ward**—I do not think at this point in time we would be able to estimate that confidently. We have been dealing with some of the copyright collection societies who look after intellectual property for artists, literary works and music. Again, they are struggling to try and make decent estimates of that. I think what we would like to see put in place is a system which allows the use of intellectual property to be properly recorded, logged and rewarded. For example, we put up a site with new musicians a few weeks ago. Most of the downloading of that music occurred in the United States. Those artists are doing that to get exposure. But once they get exposed, they would like to collect revenue from those people.

**Mr BEDDALL**—From a tax base.

**Mr Ward**—From a tax base. At the point at which that music is downloaded, we can collect the money and the tax.

**Mr BEDDALL**—What I am saying is that the majority of transactions on the Internet will not currently be attracting tax.

**Mr Ward**—I know. I cannot see why that is the case.

**Mr BEDDALL**—Services.

**Mr Ward**—Yes, but most of it is free.

**Mr BEDDALL**—Yes, that is what I am saying; they do not attract tax.

**Mr Ward**—They do not attract revenue either.

**Mr BEDDALL**—For the government. The fears of the tax office about loss of sales tax are being overemphasised?

**Mr Ward**—Staggeringly overemphasised.

**Mr Fair**—Absolutely. But you have to say that a rider to that—and the report properly identifies it—is that the transfer pricing issues will become a lot more acute when local offices here do not need to actually sell anything because all they will be doing is talking to clients and saying, ‘Now you can download the software direct from our site in Silicon Valley,’ and the transaction will take place over the banking system in Silicon Valley, effectively. We will have a large number of businesses here that are expending money, but what they are selling and how their efforts relate to sales of their international parents’ products in Australia will be much harder to calculate.

**Senator WATSON**—My final question is related to transfer pricing—the very issue that you raised in your last couple of sentences. It has often been suggested today that the introduction of a GST would solve this problem. While it might partially solve it for some of the higher sales taxed items—your 22 per cent and your 32 per cent type items—if you have your GST at too high a figure in the region in which you operate, these transactions will be deemed to take place at a low tax regime through transfer pricing.

**Mr Ward**—Agreed.

**Senator WATSON**—This is the dilemma that we could well have with a GST. If we set it at 15 or 12 per cent and other countries in the region have it at six per cent, you can see where all your transactions are going to take place—not one would take place in Australia.

**Mr Ward**—Yes.

**Senator GIBSON**—Aren't we insulated a fair bit by the cost of getting stuff here?

**Mr Ward**—Yes, by physical transport costs. But there are things that do not have to be physically transported, of course.

**Senator GIBSON**—Yes, carried over the Net.

**Senator WATSON**—There would be a big leakage on services.

**CHAIR**—Do you think there is a good option for taxing air and water?

**Mr Cousins**—Wasn't it Monty Python who bottled the air and sold it to the air force?

**CHAIR**—Gentlemen, thank you very much. You have been most helpful indeed. We appreciate your views and your submission, and we would appreciate any further information that you care to send us. The committee will take some time to finish its report and we will make sure you get a copy.

**Short adjournment**

[4.33 p.m.]

**McNAB, Mr Paul Joseph, Private Citizen, 80 Findlay Avenue, Roseville, New South Wales 2069**

**CHAIR**—Welcome. In what capacity are you appearing before the committee?

**Mr McNab**—As a private citizen. I believe my submission has also been endorsed by the Institute of Chartered Accountants, although their submission may not have been received by you yet.

**CHAIR**—We do have your submission and we thank you for that. Would you like to make a brief opening statement before we ask you questions about it?

**Mr McNab**—Since writing it, I have wondered where it might go next. I am not sure whether you want to deal with this before moving on to that next conversation.

**CHAIR**—Where what might go next?

**Mr McNab**—To me, the submission suggests there is a problem and solutions are needed without necessarily giving you the solutions, which is what I have tried to think about since sending it. Do you want to deal with it for a moment, perhaps?

**CHAIR**—You say in your submission that you have very serious concerns about Australia's revenue base. I have to say to you that the majority of submissions have not really indicated such a great concern? Colleagues, am I right?

**Senator WATSON**—Some of them have been very narrowly focused. Our problem is to look at the overall picture.

**Mr McNab**—Perhaps if I offer you my perspective, as I see it, I think there is a big picture in all of this. To me, the approach of focusing on just income tax or just customs duty or just sales tax fails to see the big picture. To me, the big picture is that this entire exercise is a debate about how jurisdictions share the total tax available from global trade. If you look at it in that perspective, whether you take your dollar by way of customs or sales tax as the goods or services enter the jurisdiction, or whether you take a dollar from the reported corporate profits in the corporate income tax return, that is not perhaps the issue. The issue is how you get to a point where you are entitled to your dollar in the first place.

The indirect tax base and the direct tax base currently involve tests of physical presence as the starting point for their taxing rights. The majority of the high value movement in this sector to me is in the services sector. It is not so much the current volume of trade, it is the future volume of trade. If your current tax base does not tax



those sorts of activities it is not enough to say that you do not presently have a problem. The issue is that that part of the economy is growing quickly, so how long is it before you have a problem?

When you focus on it from that direction, the difficulty that I see is that the current tests that we operate in took the better part of 50 years to develop. If we are going to go through a process of taking 50 years to change the current tax base, that is a 50-year problem. What I see being needed is really a conversation about how countries share tax revenues from international trade rather than necessarily a focus on problems with collecting customs duty or sales tax or transfer pricing as such. To me, they are all just different ways of looking at the same problem.

**CHAIR**—Solutions?

**Mr McNab**—Interestingly enough, there are solutions being discussed but they are not being applied to this problem. They are solutions to deal principally with issues in the transfer pricing area. In the time since I sent this in, I can see four broad areas of possible investigation for solutions.

The first of them is a line of research proposed in the early 1990s by Professor Richard Vann of Sydney University. His work looked at problems with transfer pricing and recognised that, as you started moving into this sort of environment, you were going to have difficulties properly apportioning tax rights. His solution was to go back to the country of residence, examine the tax returns there, and come to an international agreement on how to split that tax return up between the countries with which the trade has been done. It involves moving to a formula basis for splitting international trade.

All these possible solutions have problems of one sort or another. Beyond describing a way of looking at it, I see this as a conversation in two parts. The first is describing a way of looking at the problem, which I think is valid; the second is devising a process for assessing what to do next. To me, the possible solutions are the ones I am going to run through. You get a situation then where you would want to evaluate with a tax economist which of them you would prefer in an absolute sense.

If you decide your order of preference, you then move back to the technology advisers and the diplomats to determine which of them you can actually achieve or what problems exist. When you bear in mind that all of them involve changing the ways that countries share tax revenues, it is clearly not going to be an easy problem to solve.

However, the existing international tax system arose out of exactly the same problems in the 1920s and 1930s. There was a dispute about how to share tax revenues between capital importing and capital exporting jurisdictions. An outcome was achieved which we have lived with for quite a long time. To me it is a little pessimistic, at the start, to say that this is too hard. In fact, to me it requires a process of deciding how best to

attempt it.

If I can go back to the four areas that seem to me to be apparent at the moment, the first is some sort of apportionment of revenues across source and residence jurisdictions on a formula basis. Vann's solution suggested having an international tax authority to actually undertake that process, and there are reasons why you might or might not do that. At the time, he was a consultant to the OECD, so it is interesting to see that sort of idea coming out of someone who has been involved in that forum.

In the 1980s, some of the US states, the most noteworthy probably being California, looked at a formula apportionment system in the unitary taxes. They had a lot of difficulties because it was unilateral, it was not a multilateral solution, but the difference between it and Vann is that Vann proposes some sort of taxing body to do this and the Californian model simply requires agreement on a formula, so there is a subtle difference between the two.

The second approach seems to be the approach that is by and large being pursued by the US and the EC in their opening comments in the area, and that is to take the existing international tax treaty structures and amend them piecemeal to incorporate tests of presence which will give you a taxing right in appropriate cases. I cannot see that that process is going to be any easier than the process of dealing with Vann's suggestions, because to me the jurisdictions that have the biggest amount to lose are the US and the EC, and their basic position has already been publicly stated in that they would prefer to see no change whatsoever. So they prefer a laissez-faire approach.

The third broad category approach is potentially a unilateral approach and, again, you can see reasons why that may be unacceptable, but it is quite interesting because the content and services area quite frequently falls under the areas of treaty protection, such as the royalty provisions. All of our current international treaties generally give us some taxing right in relation to a royalty payment.

If you look at the work being done in relation to copyright law, for instance, the field of coverage of that area of intellectual property is expanding. You would expect to see more of the payments passing out of the jurisdiction, falling under that definition and giving rise to a taxing right on our part. So you can see that there might be a theoretical solution which involves just expanding the coverage of our copyright law and pushing matters into those treaty articles that we already have.

The fourth solution that is certainly raised by the conversations currently, although it seems to be quite unpopular, is a tax of the sort proposed by Cordell in Canada and Soete in the Netherlands of a bit tax, which seems to be driven by Tobin's banking turnover tax. It appears to be just a variation of his proposal.

They seem to me to be the four broad approaches that are currently raised. If you

conceptualise the problem as simply an exercise in splitting up international revenues, they are the four solutions that appear to be currently raised. I would have thought if more heads were turned to the problem you might even expand that field, and your initial approach to me is to examine the economics of the proposals to determine which one you want in an abstract term.

**CHAIR**—Would not a bit tax be highly regressive?

**Mr McNab**—It has all sorts of problems, but the proposition is that all taxes are in a sense arbitrary and what you want to do is to find the part of the economy that is generating the most activity and impose a simply collected tax on it.

**Senator WATSON**—Taxes rule out Australia as an international financial centre.

**Mr McNab**—None of these proposals can be done unilaterally, particularly the bit tax. What I am putting to you is that you need a concerted program of international pushing to find what you want and to get out and sell it, rather than to simply attend OECD meetings passively, for instance, in the tax area when the bulk of the people around the table do not have the same interests.

**Senator COONAN**—We have enough trouble just reaching a relatively simple double tax agreement. It would be almost inconceivable that you could actually get to negotiate piecemeal by piecemeal under the treaty system with the countries you would need to.

**Mr McNab**—That is the gist of Richard Vann's paper. The solution is at the end of a two-part article that is 40 pages long, and the first 30 pages describe the current total breakdown of the international treaty system. It really is a problem. That was in the 1990s, before this problem arrived. To me, this is just further grounds for wanting to desperately do something about it.

**Senator WATSON**—Would you like to comment on the question that I asked the last witness about a level of GST in the area in which you operate?

**Mr McNab**—Yes. I am not a GST expert, unfortunately—or fortunately. All I would observe is that the EC is already having problems implementing a GST in relation to electronic commerce transactions.

**Senator WATSON**—They have such high rates, though. That is why.

**Mr McNab**—The principal problem was in relation to telecommunications carriers, because off-shore carriers—particularly US carriers who did not have a home GST—could deliver a service without setting foot in the jurisdiction, which meant they were able to compete quite aggressively with their own carriers. Their solution was to turn the tax

around and make it payable by the consumer as opposed to the normal GST framework of collection. While that probably works okay in the context of dealing with a very large corporate, it still suffers the same problem you get with sales tax and other indirect taxes in relation to small goods currently in the Internet. There is a collection problem. If you examined the EC experience you would get a list of problems generated by Internet trading in relation to a GST, because they are starting to appear there already.

**CHAIR**—Is this issue large enough to help destroy confidence in the system?

**Mr McNab**—In the GST system.

**CHAIR**—Or is it just a little tiny—

**Mr McNab**—I cannot answer that. The reason they acted in relation to telecommunications was that it certainly did affect it. European carriers were suffering very severely, so there was a need to act and change the basis on which GST operated. The change they made really knocks around the purity of the GST principles. So, yes, it had an impact of some sort.

**Senator GIBSON**—If we were going to introduce a broad based indirect tax here, we should give very special consideration to that particular problem?

**Mr McNab**—Yes, I would think so. I think there are authorities that can help you. As I say, dealing with European tax authorities, you would almost get a check list of issues, I would have thought. I know the commissioner spends quite some time dealing with other authorities, so it should be fairly simple to collect that sort of information. I have not attempted to compile one myself.

That is a slightly different direction or a step beyond my original letter I think but, without occupying a lot of your time, I thought that was the next direction.

**Senator GIBSON**—It is very interesting.

**Senator COONAN**—Could you expand at all, if you can, on the concept of perhaps using the copyright and the royalty provisions as some sort of model to structure some thinking about?

**Mr McNab**—I think it comes up in two contexts. One is it is already happening, and the scope of our copyright articles is currently expanding as the Copyright Act is. You can see that over the last 40 or 50 years if you look at what was protected by copyright, so there is no doubt that it is already occurring.

If you look at Professor Doernberg's work in amending treaties bit by bit, you will see that what he is often doing is proposing that similar sorts of tax at source rights be

introduced into treaties in relation to specific Internet commerce transactions—a bit like amending the GST to deal with the telecommunications transactions.

**Senator COONAN**—You would still have problems with source, though, wouldn't you, in identifying where that—

**Mr McNab**—Yes, you do. The test they tend to propose is jurisdiction. They tend to track cash flow, or payment value leaving the jurisdiction is the sort of nexus they look for. They tend to try to impose it by placing a legal obligation on the person or the organisation paying for the goods or services, so even though you might be—

**Senator COONAN**—As the collector?

**Mr McNab**—As the collector, yes. What you have done is you have disaggregated your collector, which is one of the reports made in the tax office report. In relation to a lot of consumer items, you are suddenly trying to collect small amounts from the entire population, so there is a problem. But, again, you need to step back and analyse where the likely volume of trade is. You may decide to live with that. The economics of it may be such that you are happy.

**Senator COONAN**—If you concentrated on large transactions rather than chasing every little bit—to coin a phrase?

**Mr McNab**—Yes, precisely.

**CHAIR**—On page 2 you commented that the ATO mechanism, 'in evaluating the likely impact of electronic commerce on the income tax 'tax base' tends to underestimate the potential damage'. Can you tell me what is wrong with the ATO's methodology and what better system you would prefer?

**Mr McNab**—In two parts: I think that the ATO approach is actually clever but still causes that problem. I have not seen anyone trying to estimate sensibly the impact of these changes on their tax base before, so the ATO document is quite clever in that respect. The reports coming out of other jurisdictions simply assert a problem; they do not try to find a methodology of dealing with it. The methodology they chose, though, was to just take the standard industry codes as best they could, apply them to the industry sectors which appeared to fall into the definition of 'affected by electronic commerce', check how much tax they were currently paying and decide that that was the amount of revenue at risk.

The difficulty I have is that the revenue base at risk is the new foreign vendors into Australia who are not necessarily paying tax here. To me, the growth in the relative size of that sector of the economy compared to the traditional goods sector of the economy is going to be disproportionate. You will see quite a rapid growth in services and

goods which are able to be provided remotely. If you simply focus on a static picture of what the Australian industry sectors involved are doing today—

**CHAIR**—But the goods still have to go by air, sea or—

**Mr McNab**—I think the value is in services, and I agree with the previous comments. Currently, for instance, I would have thought that the major issue in this area is the banking sector. It is quite interesting. To me, the transfer pricing area is more or less the same problem. If you check the tax cases in the last 50 years that deal with transfer pricing issues—I think there are probably two—they do not deal with the question of what was a fair price; they deal with administrative issues. So, there is a problem here, you would think, in terms of litigating and enforcing your transfer pricing provisions.

If you then have a look at the commissioner's general view that this is a major problem area and you match it up with the OECD draft on the area that came out in July which says 'It is such a problem, we have all turned our minds to it collectively,' you begin to conclude that, at least in that sector, the area is already a problem and getting worse. So, I do not think that sitting down and doing an SIC code of this sort on the three or four industries affected will not give you a picture of the whole issue. Is there any value in summarising all of that and giving you the cross-references in writing?

**CHAIR**—The four recommendations?

**Mr McNab**—Yes.

**CHAIR**—Absolutely.

**Mr McNab**—I am three-quarters of the way through. I had hoped to bring it today but I have not finished it.

**CHAIR**—We would appreciate that very much and we will accept that as an additional submission from you.

**Mr McNab**—Thank you.

**CHAIR**—We will distribute it to members and take it under consideration.

**Mr McNab**—Currently, they are the best I have got.

**CHAIR**—Thank you very much for your input. Certainly there are concerns. None of us actually know how big the issue is, but the more people who talk to us, the better idea we get of where we are and where we are likely to be.

**Mr McNab**—I think the basic message from me is that, if there is an issue and

you are going to wait 50 years, it will be big by the time you decide to see it or act on it.

**CHAIR**—I do not know about the committee, but I can accept that. Thanks very much.

**Mr McNab**—Thank you.

**Committee adjourned at 4.55 p.m.**