COMMONWEALTH OF AUSTRALIA

JOINT COMMITTEE

of

PUBLIC ACCOUNTS

Reference: Internet commerce

MELBOURNE

Friday, 14 November 1997

OFFICIAL HANSARD REPORT

CANBERRA

JOINT COMMITTEE OF PUBLIC ACCOUNTS

Members

Mr Charles (Chairman)

Mr Griffin (Vice-Chairman)

Senator Coonan	Mr Anthony
Senator Faulkner	Mr Peter Baldwin
Senator Gibson	Mr Beddall
Senator Hogg	Mr Broadbent
Senator Watson	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.

WITNESSES

JOINT COMMITTEE OF PUBLIC ACCOUNTS

Internet commerce

MELBOURNE

Friday, 14 November 1997

Present

Mr Charles (Chair)

Senator Watson

Mr Anthony

Mr Beddall

The committee met at 9.05 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 Committee 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 public hearings on this matter in Canberra and in Sydney. The inquiry will focus on the international competitiveness of Australia's small and medium sized business 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 via the Internet.

The JCPA's 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 those growth opportunities and be a world player. Currently the global value of goods and services transacted over the Internet is estimated at $3 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, Australia's small and medium enterprises will be exposed to greater competition from overseas retailers advertising their goods and services on the Internet. At the same time Australian 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 imported otherwise 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 a 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 framework for consumer protection and the protection of intellectual property, government industry assistance programs and the opportunities 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 Canberra during December. Today the JCPA will take evidence from Australia Post, Coles Myer, the Australian Society of CPAs, Arthur Andersen, and the Australian Bankers Association. Before swearing in the witnesses I will refer members of the media who may be present at the hearing to the committee statement about the broadcasting of proceedings. In particular I draw the media's attention to the need to fairly and accurately report the proceedings of the committee. Copies of the statement are available from secretariat staff present at this hearing.

GROSSER, Mr Christopher, Group Manager International, Australia Post, GPO Box 1777Q, Melbourne, Victoria 3001

RYAN, Mr Gerry, Corporate Secretary, Australia Post, GPO Box 1777Q, Melbourne, Victoria 3001

CHAIR—Gentlemen, thank you for coming on this wet and dreary morning. We have received and read your submission. Would you like to make a brief opening statement before we ask you questions about these weighty issues?

Mr Ryan—Yes, Mr Chairman. I will try to keep it brief. Mr Grosser has authored our submission and I expect that he will respond to many of your questions this morning. Our short opening statement does two things. It presents some salient facts from Post's perspective and makes some quick observations on them. The facts: firstly, we fulfil obligations under international treaties, to which our government is a signatory, to provide international postal services covering letters, packets and parcels. We handle almost 12 million inward packets and parcels annually. Just over one million of those are parcels—that is, they weigh two kilograms or more—and they are separately screened by Customs. Some 10½ million are packets, upon which Customs provide a proportion check, and I think that was elaborated on in their evidence.

Our primary role is to deliver these articles speedily and reliably. We assist Customs and AQIS in their tasks by providing facilities, by opening and repacking items, and in some instances by collection of duties or taxes at post offices. We employ some 90 staff on barrier functions. We estimate that the total cost in handling, processing and delivering inwards parcels and packets to us is around $30 million per annum. Our incoming parcel and packet services are offered in competition with DHL, Fedex, UPS carrying the majority of urgent express parcels.

Parcel and packet volumes entering Australia annually over the past six years through our system have remained relatively static. For example there was something like 11.6 million in 1991-92 and 11.8 million in 1996-97. So the impact of Internet commerce in terms of net growth in our volumes is not yet evident. Australia's levels for formal declaration are on the low side. Australia, as you indicated, Mr Chairman, has a limit of $1,000, the UK £600 on air cargo and £2,000 on postal items, the US $1,250 and Canada $1,600.

I just make a few brief observations on those facts. Firstly a decrease in thresholds would increase clearly our costs and would introduce some delay in deliveries. Obviously we would require, for example, additional storage facilities and, secondly, customers who would normally pick up items from post offices, from a local post office, would presumably have to go to locations where Customs are in attendance, so there would be some delay and inconvenience factor involved there. Secondly, a reduction in the formal entry threshold, say from $1,000 to $250 would increase our handling costs for some 20,000 articles.

We have indicated in our submission that in principle we would prefer an increase in the formal entry threshold, bearing in mind that we are on the low side internationally. We have cautioned also against a lowering of thresholds without a thorough analysis of relative costs and benefits, and we are sure this committee has that issue very much in mind, and we note that, as Customs put it, in considering the issue of costs and benefits we need to work out where those two curves, if you like, interact, and in that respect we are assisting Customs in a survey of postal items at our Sydney facilities to secure a better understanding of the revenue leakage from the $50 tax-free threshold.

In conclusion, we would assure the committee that our objective is to contribute towards optimising inward goods clearance, both in revenue collection on the one hand, cost containment from our perspective, and minimising delays in getting goods to our customers. That concludes our opening statement.

CHAIR—Thank you very much. In your submission, talking about the formal entry threshold and the $50 collection concession, you said it has:

. . . proved to be a practical and adequate regime for collection of duty and sales tax.

You have said:

In Australia Post's experience, this view appears shared by users of the international post.

Are you talking about Australian users, international suppliers? Can you expand on that?

Mr Grosser—Yes, I can. The comment was made in regard to no real problems from international users of the Post. In fact, we get support from both Australian customers and those overseas who use the post coming into Australia. We certainly don't seem to have any major problems with regard to Australian customers complaining bitterly about the process of admitting items through the post in Australia.

CHAIR—Do you have discussions with other jurisdictions? I noted that Gerry just commented on some stats with respect to England and the United States and Canada on their air freight and parcel post entry dollar values and customs limits. Do you regularly talk to other jurisdictions on these issues?

Mr Grosser—It is an interesting question, and in fact this particular committee prompted us to gain some information in this area. It is an area that is not discussed regularly between postal administrations and comparisons generally made, but I think in the world of increasing global commerce and the use of a post as one of the mediums in that area, this particular information is going to become more prevalent I think in postal discussions. Certainly we sought information, once we had made a submission, and asked our colleagues in a number of the developed countries to offer us information about the various levels that apply in their jurisdictions with regard to formal entry thresholds and what might be duty and tax-free limits, or concessions that might apply.

CHAIR—I noted that Gerry made the comment, something to the effect that the impact on Australian incoming parcels from Internet trade has not yet become apparent—that is, that there is no major impact to date apparent from the number of parcels coming into Australia. Have you discussed that issue with, say, the Canadian colleagues or UK?

Mr Grosser—Only in very general terms. We have sought no particular information from them in regard to whether they have experienced a major growth in their outward items coming to Australia, for example, because of Internet commerce. It is very difficult for a postal administration, when it talks about the numbers, to attribute items to Internet commerce or whether in fact they are due to perhaps the traditional areas of direct mail approaches being made between countries. It is an area that is very difficult, just because you are seeing items coming through, without knowing your customers intimately.

Mr Ryan—Mr Chairman, as I understand it in our communications with other postal administrations on this issue—and it has been explained why we are seeking information—none have initiated advice that the Internet has led to substantial volume increases. That is not to say that some aren't occurring, but none have said, 'Oh, yes, we've noticed a major increase and we're attributing it to Internet commerce.'

CHAIR—Some people who have talked to this committee have said very clearly that Australia, I think, has the second largest take-up of PCs per head of population of any country in the world, but estimates are made that our take-up of actual commercial transactions on the Internet has not tracked that experience. Have you formed a view from your statement that the impact on postal items coming into Australia has been negligible, that that is so, or that any increase in Internet is only replacing traditional mail order?

Mr Ryan—We have only got the most general of indicators. The volumes are not rising, and that suggests to us that Internet commerce has not yet led to a net increase in volumes. There may be some displacement of the method of ordering, but it is not evident from material we get access to, I am afraid.

Mr BEDDALL—I think that is fairly self-evident around the world—that everyone is talking about; it hasn't yet quite happened—although it would be interesting if someone like the United States Customs Service, if they have seen any impact from, say, amazon.com, the big book store, which, according to all the evidence we have had, has had an amazing success rate. I think what this committee is concerned about, if and when—and I think more when than if—commerce on the Internet becomes secure—that means people are confident they can transact their credit card across the Net—that then you will have a situation where the tax base of any country is captive to the Net. The real problem being that the thing about tax is where it is domiciled and if you are buying elsewhere then it is replacing that. There is also the fact that Internet commerce is not mail-order by electronics, it is quite a different marketing tool.

How do you think Australia can redress the tax bleed that will happen on the wholesale tax system or a GST tax system—it doesn't make a difference which one it is—on the items of $50 to $100 or $200 which will be those that will no longer be bought in a shop but be bought on a worldwide net if, as you suggest, the thresholds go up. I understand why the thresholds will go up on Australia Post's point of view, because that is a burden on you, but there is the big danger of the tax base bleeding. Have you thought about some of those issues? They are not your responsibilities, they are Tax's responsibilities, but you are going to be the administrator of some of that.

Mr Ryan—I must admit our focus has been on rather cost to us, and we share your view that the administration of taxation and customs and excise are the responsibility of others. Our job is to cooperate with them in whatever regime is established by government. So it is really not an area in which we have expertise and not an area that I could offer an informed view on this morning.

Mr ANTHONY—Perhaps just going back a step, you have supplied us with a flow chart here of the 12 million items that come through the mail exchange. In that flow chart you have a number of sequences. One is the free area; there is general examination which I gather makes up 90 per cent of parcels. So what percentage is actually free?

Mr Ryan—I will certainly have Mr Grosser deal with that specific question but would it also assist the committee if he took us through the main elements of this chart?

Mr ANTHONY—I think it would, yes.

Mr Grosser—Yes, we thought it would help the committee get an understanding of the processes that are involved in the handling of particularly parcels in our international mail centres. This particular chart deals explicitly and almost exclusively with parcels, and you may recall that Gerry mentioned that these were items weighing two kilograms and more; these are not lightweight packets.

In this particular chart you find from the major streams, air and surface, that they are both brought together and Customs screen every item. They look at every item, they consider what further action to take, based on the address it is coming from and the declarations made on the outside and any values that are indicated on the goods. At that stage they may actually send the item down the free chute, and so there will be nothing further that they need to do with that particular parcel.

Mr Ryan—To answer his question, what sort of percentage would that be?

Mr Grosser—In regard to the proportion that would go down the free chute, in response to the question that you raised, by far the major part—we estimate here in the vicinity of 80 per cent—of all parcels would go down the free chute.

Mr ANTHONY—General examination is 10 per cent on your flow chart there. You have got 90 per cent of parcels transferred to free chute, so—

Mr Grosser—There is about 10 per cent in that area and there is about 10 per cent that go down the commercial area. It is of that order. There are elements that are referred at the first screening stage to quarantine, to the dog area and, as I say, under community protection where in fact you are getting very much into the area of AQIS, the Quarantine Inspection Service.

Let’s just deal with those elements and we will go across to the chart. What we are trying to explain is there are three key areas of their attention: in the first screening process all the items pass before them. They separate out the frees, they take about 10 per cent, as I mentioned, to this general inspection area where in fact that is further broken down and again a major portion of that is sent away free. All the items that go into the general examination area in one way or another are examined by x-ray, a secondary screening process, or the items are opened. They are of course compared with any declarations and the duties and taxes that might have to be paid or assessed.

In the commercial area, commercial parcels are separated out at that very first stage of screening, and they are sent down another path where the commercial parcels are examined. In many cases it is done purely by examination of the declarations. In most commercial areas, as we find in the areas of our competitors, the declarations made by companies are based on commercial documentation, which must be enclosed with the actual documentation consigned with the parcel. So there is a very good way of realising the value of the contents and usually a very good description of the item.

There are a number of ways of handling the process but in the main, under the commercial parcels area, customers actually come to a Customs area located at one of our facilities and pick up the items by paying the requisite duties and taxes to be paid, and any fees that Customs might impose for the process.

If I can talk for a moment about the general examination area, I mentioned there—and these are, I might add, parcels mainly destined for individuals or delivery to residences. But the major portion of that, in the vicinity of 75 per cent, are screened free. The other 25 per cent are sent through to post offices after the requisite duties have been determined. Where there are duties and taxes to be paid, a notification goes to the customer to call at their local post office to pay the actual taxes and duties before the item is released to them and the money is remitted by Australia Post through to the Reserve Bank.

This presents the chart for parcels. I am sure your question could then be posed, ‘Well, what about the other side? What about all those other items called packets, the lightweight items?’

Mr BEDDALL—I am no good at weights and measures, so two kilos is what?

Mr Grosser—Two kilos is about 4½ pounds.

Mr BEDDALL—So a book—

Mr Grosser—A good book is definitely half a kilo, maybe four books.

Mr BEDDALL—We are talking about a substantial package—that is what I am trying to get through.

Mr Grosser—It is a substantial package. If you are talking about CDs, for example, to give you another comparison—I know you have talked in other areas, particularly with Customs, on CDs.

Mr BEDDALL—How many CDs are in two kilos?

Mr Grosser—A CD in a small cover, one of those plastic covers, weighs about 100 grams. So you are talking about 20 CDs, not one.

Mr BEDDALL—Yes.

Mr Grosser—Someone might order one or two CDs from let us say America. The items would come into Australia as a lightweight packet. These items are not flat, so they cannot be processed through our letter processing areas, and decisions have to be taken about the processing mechanism. Bags of letter class mail, which contain letters and these lightweight items, come into our airports around the country, particularly into Sydney where about half our international mail volume is processed.

At those locations Customs actually screen the bags from the various countries they come in from on what they term a ‘risk assessment profile’. They establish all the criteria for doing this and there is no physical examination of the contents at that location. But they will separate out a large number of bags which will in fact go for subsequent inspection and detailed inspection at the international mail centre. But a large proportion—and generally, against the risk assessment profile—about 85 per cent, are cleared free. Fifteen per cent in one way or another are referred through for further examination.

So your difference in processing—in one scheme, the heavyweight items—an individual assessment of every item. In the area of packets it is one of screening against this profile. In fact they would be able to pick up from their screening of the detailed component indications of items on which duties and taxes must be paid compared to those that go screen free.

Mr ANTHONY—This flow chart is with parcels, so we are talking about effectively 80 per cent come through free and then another 10 per cent. Effectively, 90 per cent are coming through the free area, and 10 per cent go through all these different checks, whether it is quarantine, dogs or whatever. In the below 2 kg what would be the percentage there? Is it 95 per cent that just normally comes straight through?

Mr Grosser—Eighty-five per cent normally comes straight through and they are cleared usually at the airport facility. Fifteen per cent come through and, of course, a large component of those letters, which are separated out.

Mr BEDDALL—So they are also screened by dogs and—

Mr Grosser—They are screened by dogs at the airport; they bring the dogs over the items. Again, they have this risk assessment profile which requires them to take certain bags out of the stream and say, 'Yes, they must be fully investigated by Customs.'

CHAIR—But you do not do that at Clyde with the containers.

Mr Grosser—Were you talking about sea containers coming in?

CHAIR—Yes.

Mr Grosser—It depends on the arrangements with Customs. As I understand it, they do.

Senator WATSON—Not only do you want the legislation annulled that produces the threshold for formal entry back to $1,000, because the legislation required it to be reduced to $250—that was 1 April 1997 and there was an extension to 1 April 1998—not only do you wish that to go back to the original $1,000, but judging from your comments that Australia is really on the low side what do you think is a more appropriate figure in expediting your work?

Mr Grosser—In terms of our work, I think Gerry has already indicated that a substantial number—and we are talking here of 20,000 or more items—would be affected by the lowering of the threshold to $250.

Senator WATSON—That is right, yes.

Mr Grosser—You might say in the great scheme of things that is not a lot. It is roughly something like about two per cent of our total parcel volume out of the million items. In effect, what 20,000 does to us is about 10,000 extra handled at Clyde, at the IMC facilities, that have to be stored—20,000 items we are talking about and we are talking about two per cent of the total parcel volume. I mentioned that about half of that number would be affected at Clyde, at the international mail centre there. We would need to store the number of items at the facility and we would require our customers, the recipients of the item, to call at the facility and to process the item in conjunction with customers.

What they would be required to do is to pay a fee for the processing by Customs, usually, in their circumstances, a manual entry, if they don't have a broker do it, by electronic means. I think you have already discussed with Customs the various fees that apply between manual and electronic entry systems for that particular form of entry, plus they may be required to pay a brokerage fee.

Our particular position on raising that threshold is really in the interest of the costs that the recipients have to bear on items passing through the post or in fact going into other schemes as well. Our particular position on it is that we would like to see that threshold, certainly in consideration by this committee, raised.

Senator WATSON—But you have also got a major logistics problem, haven't you, at Clyde?

Mr Grosser—We have got a major logistics problem at Clyde. The location of Clyde in particular is an item—for example, you can imagine a parcel coming through that was valued in excess of $250 and coming through to a resident living in the north of Sydney, somewhere like Palm Beach. They would receive a notification from Customs indicating that an item had arrived in Australia and was being held at Clyde and there were duties and taxes to be paid. Could they please call at Clyde, and in the case where the limit was lowered to $250 they would be required to complete the formal entry documentation.

I suggest to this committee, if they haven't seen it, to have a look at the formal entry documentation. At the moment it is particularly complex; it would be very difficult for, I think, any individual to complete it without the help and assistance of a broker. There are, in particular, important aspects of clearance, like which particular code or harmonised code of the customs classification system did the goods belong to. So there are difficult processes that are required and it would require the recipient to pay—and I think Customs have made an estimate in this regard—brokerage fees are generally around $60 per item.

So the impost might be on someone receiving goods valued over $250 very quickly a figure of another $100. So our position very much is that we would ask this committee to consider these aspects very carefully.

Senator WATSON—There is also a second logistics problem regarding the space that you have available at Clyde, in terms of handling this incoming mail, that would have to be separated.

Mr Grosser—You are quite correct. I think the committee has had the opportunity of examining our Clyde facility, and I am sure the chairman's question earlier was based on the experience you gained from that particular location.

Senator WATSON—So you want the return to the thousand. Mr Ryan indicated that other countries have a somewhat higher figure than even the thousand. What sorts of figures are you throwing to the committee?

Mr Grosser—If I had to make a stab at a figure, and certainly one in mind, $1,500 seems an appropriate figure.

Senator WATSON—Mr Ryan, would you concur with that?

Mr Grosser—But there are many matters that need to be considered in that area.

Mr Ryan—Senator, it is a judgment in our view for the product manager, and if he feels that is an appropriate figure, I am really not in a position to demur from that.

Senator WATSON—We just wanted a unanimous sort of approach.

CHAIR—$1,500, but with what duty and sales tax free limit?

Mr Grosser—Our position on raising the threshold of the duty and tax free limit is nowhere near as strong as it is about the formal entry threshold. I would have to say in all the deliberations of this committee, if it were to decide, in conjunction with the other authorities, that the current level is appropriate we would welcome that outcome.

Mr BEDDALL—We have had evidence that the Canadians—I think you said they were $1,600—

Mr Grosser—For formal entry.

Mr BEDDALL—But their dutiable rate is $20. They have actually come down. They have increased one and lowered the other in order to tackle this problem.

Mr Grosser—Yes.

Mr BEDDALL—Would that sort of approach be balanced, would you think?

Mr Grosser—That is one approach, but there is another approach taken in the United States. Let me add there that their threshold is $US200, in conjunction with the $US1,250 formal entry limit. One other point I should mention about the Canadian system that may not have been mentioned to you is that in Canada for ad hoc entries—in other words, items coming in for an individual, someone who only occasionally has access to items coming in—there is no formal entry limit applied. So in fact, in their case, while there is maybe a $20 tax-free limit that applies at the bottom end, they do not require them to go through the formal entry process, so they are saved the costs of actually paying for brokerage and the additional customs fees that might apply in their country.

Mr BEDDALL—You could understand why the United States would not be very keen about that, seeing 85 per cent of Web sites are US-based, and they are going to be providing the world with all the goods, so they would be keen for everybody to adopt their standard.

Mr Grosser—I am sure that is true. An interesting point that we have noted, too, in the United States, and this may again reflect their attitude to what they would like to see the rest of the world take on, is that they have no federal and state taxes applicable to direct mail order merchandise entering the country, so in fact they have got a regime which not only looks to Internet, but it also looks to direct mail.

CHAIR—I want to get this absolutely clear on the record now. You would support a $1,500 screen-free value limit and a $50 value limit for Customs and wholesale sales tax on both air freight and sea parcels?

Mr Grosser—Indeed, that is our position, if the term that you used at the beginning is the $1,500 formal entry. You said 'screen-free'. Formal entry limit, yes, indeed.

CHAIR—The second question going with that: you said in your submission it is understood the postal threshold, which is legislated to go down to $250 from 1 April 1998, remains under review and there is a possibility it now may be retained at its present level of $1,000. Can you tell us where that information comes from?

Mr Grosser—I can offer the comment that it came informally from Customs. It was in discussions with them with regard to this particular Internet commerce inquiry, and they said that there was a view prevailing that legislation may be brought forward to keep the present level of $1,000 for a further six months, during which time this committee and others would bring some weight to bear on outcomes to be adopted at a later time. So there seemed to be a case or at least a six-month extension of the current limit.

CHAIR—My understanding is the legislation says that on 1 April it happens—bang—that's it. I am not aware, and can you make us aware, of any formal process under way to amend that?

Mr Grosser—No, I can't. The only formal process that would take place I believe would be in the customs area, in fact, where the original work was done regarding the proposal to extend the limit of $1,000 for an extra year. In fact, the $250 limit on formal entry was supposed to apply to post from 1 April 1997. There was a one-year deferment brought about by a very strong lobby group, and that caused the limit to be extended for another year. The lobby group primarily came from small business, who would be greatly affected, they felt, in the lowering of the limit, and our current indications here are that there is some work going on to extend the limit, but in terms of a formal position, no, I cannot bring your attention to it, Mr Chairman.

CHAIR—I suspect obviously it is historical, but is there any logic behind this differential between air freight and sea freight?

Mr Grosser—Is your question from the point of view of Customs or from our point of view in terms of processing?

CHAIR—The $1,000 versus $250.

Mr Grosser—I think you will find the $1,000 does not apply differentially to sea and air freight. A $1,000 limit applies to post exclusively, but if you go to any other cargo operator you will find that their air and sea freight is in fact judged under the $250 limit. What you have is a differential which applies only to post.

Mr BEDDALL—So DHL would be $250 and you would be $1,000?

Mr Grosser—Correct, and of course you could understand an industry lobby which says these levels should be changed. Mr Chairman, could I make an additional comment here, just to enlighten the committee on the $1,000. I think Senator Watson mentioned the 1986-87 position of the $1,000 limit coming in. There is a differential that applies, and it historically was not always so. The $1,000 came into being I think in 1986, or enacted in 1987, as a result of—I understand, and I need to be corrected here if I am wrong—an Industries Assistance Commission report looking into the effectiveness of the processing through post and the customs facilities.

It had regard to the difference in the way that people consign items to post, compared to consigning them to the general commercial sector of the DHLs, the Fedexes and TNTs, and we found that a lot of the customers, as opposed to the ad hoc customer, are not the regular commercial senders, and that in that regard they are not the ones that have access to the general regime of a broker in-house or a broker within the facility. And also the way that our competitors operate is somewhat different. They generally pay the duties and taxes that are payable as Customs, clear the items, and then invoice the customer. So it is, if you like, after the event that the items are cleared through their processor.

In post it is a different regime. In post the recipient clears the item through Customs by paying the appropriate duties and taxes. Post does not and, historically in many countries throughout the world, has not played the role of broker.

Mr BEDDALL—One of the pieces of evidence we got which may be a business opportunity for Australia Post was freight forwarders were sending 5,000 shirts, which was the example, purchased overseas to Australia. One consignment comes in, but each one is sent to an individual person, so they are distributed in Australia. There is no sales tax payable because they are all under the threshold. Have you had any approaches or are you aware of anybody saying, 'Well, this would be a good little business for Aussie Post'?

Mr Grosser—I know of one particular case where in fact it is very good business for Aussie Post. To offer specific comment, there is an international cake supplier which uses that particular example that you have just expressed. In fact, it is a company which exploits this particular, if you like, opportunity throughout the world. It generally ships cakes in large surface mail shipments by container load. Each item is individually addressed, so the items under customs regulations in this country are judged individually and not as a total consignment. Each item falls below the tax- and duty-free threshold limit, and so each item doesn't have to pay any duty in tax. But if you looked at it as a total consignment, you would have to say, 'This total consignment should bear duty and tax,' and I am sure this is an issue where the Taxation Office and Customs Office have this matter under close examination.

Mr BEDDALL—That is one area where the Internet will give a big opportunity, because using the example quoted on amazon.com that book supply—even though books don't—that is probably not a good example—

Mr Grosser—Books are not a good example.

Mr BEDDALL—No, but with any other, CDs or whatever, there would be a great opportunity, and one I think which will be exploited worldwide under the Web.

Mr Grosser—In a practical sense, too, Christmas cakes have essentially a common delivery date, and they can be ordered a couple of months in advance, and you can actually bring the orders together and then ship container loads. I think if you are looking at the competitive advantage of Internet over other forms of purchase of goods, you have to offer something that has to be in terms of price and service, and generally the transactions that you are looking at between the retail purchase of the good and that Internet purchase are quite different. I am not too sure that I would be prepared to wait six to eight weeks while someone shipped out a book if I really wanted it. The incentive in terms of price differential would need to be significant.

Mr BEDDALL—There is also the availability factor, where the publishing cartels are going to use the books, even though in terms of tax they are not a good example, but in other things they are a good example, where the international publishing cartel says, 'You must buy all your books through the United Kingdom,' when it can be up to two or three years before a book that is available in the United States becomes available here—so there are those opportunities. It is the same, say, with CDs, with the availability of out-ofstock or older type CDs that would be available in the United States because of the size of the market, but may not be available in Australia, and there are some examples of that.

Mr Grosser—I think you are exploring some niches there where you would have to say that Internet trade is a very effective means to access a world or global supply system which is not available in this country. I think if you are making comparisons about items that are available in the country with those outside of it, you really are saying, ‘In the area of CDs, I know that I’m fully equipped with a store close by, which seems to have everything I need, and I can’t find a reason to go to the Internet to purchase a CD.’

Mr BEDDALL—Pretty soon you will be able to download it.

Mr ANTHONY—I understand the reasons you want the threshold raised. It would certainly be simpler for Australia Post. The fears amongst a lot of small retailers, of course, is that if the threshold was raised, then it would put a lot of small retailers out of business. How do you respond to those types of comments?

Mr Grosser—I can understand some of the concern, and I wonder whether the retailers are really responding to that or to the possibility that this $50 duty tax-free level might be raised. The commercial entry level, if it is raised—and I am sure you are going to hear from Coles Myer later this morning on this very issue—let’s assume from $1,000 to $1,500, what will it do in terms of affecting the actual retailer or group of retailers? In looking at it, it just changes the paperwork, the brokerage fees, and in fact in some instances the customs fees that are applicable.

To me it seems that small business, in particular, would welcome a move to raise the commercial entry level in terms of formal entry, but at the same time they would be required to pay all the necessary duties and taxes that are applicable. Again, I am not sure of the concerns that they are expressing, whether they are directed solely to formal entry. I think they are expressed on a wide front, so they are taking in this $50 level at the same time. I find it is a confusing issue, in reading some of the material that has been presented to the committee, and I think it is an area that needs to be fully explored. Certainly, from our point of view, when we come back to that formal entry level, there are some real benefits in it for business to raise the level.

CHAIR—Can I say to you that the one group so far—they appeared before us in a former hearing—that was most adamant that the current limits were hurting their business was the Australian Fishing Tackle Association; in fact, they want the limits to go down, both the duty and customs, and the total screen-free dollar value limit. If we were to lower it, say, to $20 or something, have you made any estimates of the cost to Australia Post to try to accommodate all that, recognising your lack of storage facilities at Clyde, and what other impacts that would have on your airport operations as well?

Mr Grosser—Yes, Mr Chairman. We have tried to make some estimates, and they are somewhat crude at this stage. I think as the further deliberations take place following the customs survey that is currently under way, there will be more information coming out from that at our Sydney facilities, which will help us in trying to pinpoint the effect with some greater clarity. Let me give you an example. As you bring down the thresholds—and we are talking about the $50 limit here, not the commercial formal entry threshold—you are exposing more and more articles to say that, yes, they should pay some tax or duty, in which case the instance of wanting to see more items, examine their contents, goes up somewhat proportionately.

We have said just in lowering it, say, to $25, effective work at our facilities would probably go up more than twice the level because you are trying to expose more and more articles all the time to examination. We are currently handling a million parcels through the scheme that you have seen. The small lightweight items are, if you like, handled through the process and risk assessment profile mentioned earlier, but at the end of the process we might be talking of a lift of, say, one million items going through the system to maybe three million or four million items going through the system out of the total of 12 million. With three million or four million items going under close examination, the costs could more than double.

We have 90 staff employed in our facility serving Customs, and the Australian Quarantine Inspection Service—Customs I am sure will report on their costs—but certainly with a lowering of the $20 limit, storage facilities, the whole process, the congestion that would occur is significant and would lead to delays.

CHAIR—On the other hand, Coles Myer cite a KPMG study which shows that revenue lost by the $1,000-$50 threshold was approximately $25 million a year. Do you accept that figure or reject it? Can you comment, if that is true, on how much it would cost you to recover that between you and Customs?

Mr Grosser—We have no information to confirm or deny that estimate. In fact, I think only the information coming out from the current Customs survey will help clarify what the revenue leakage figure might be, and I know that we are all going to have to look forward to the end of November to get some answer on that area.

Mr BEDDALL—Do you have an annual cost now, what it costs you to police overall, the cost of doing $1,000 and $50?

Mr Grosser—In terms of overall costs, Gerry has mentioned that the costs of processing and handling of all the packets and parcels and their delivery is about $30 million. We do not have with us a very detailed assessment which breaks out just the cost within our processing centres. In that area, if the committee wants that information, I am sure that we could glean some estimate of the cost of working through that with our 90-odd staff and the various elements of the processing to come up with a figure. But, as a quick estimate—if I can just use something off the top of the hand in terms of figures—it has got to be more than $10 an item, and the possibility of $15 or $20 in the overall processing of items. When you are thinking about the actual opening, the physical examination which is done by Customs, the closing of the items, the identification, the sealing, back into the stream or being held in storage, more duties to pay or release out to a post office, more duties and taxes to pay, when you look at the whole process you could easily be talking in the vicinity of $20 an item.

Mr BEDDALL—You don't do that for every item.

Mr Grosser—We don't do it for every item, but I did mention in my earlier comment that, given a lower threshold of $20, we might be doing it for three million out of the 12 million items, and you only need multiply three million by $15 or $20 to suddenly find how the figures start to rise.

Senator WATSON—What about $40?

Mr BEDDALL—If there is a description on the parcel, you don't always open it up. Obviously you would make an assessment and what the tax and duties are.

Mr Ryan—Customs make the assessment, and if they seek to have it opened our staff do so and then repack it after the assessment has been made.

Mr BEDDALL—You aren't doing a million of those a year, are you?

Mr Grosser—If I can respond to the question, no, we are not opening a million items a year, but Customs are screening and looking at a million parcels a year, and they are looking at them individually. Some of the parcels are assessed, as I said, in the commercial area. You may recall that chart: there was a commercial stream. The commercial area can be assessed on the documentation that is included with the parcel.

Mr Ryan—Mr Chairman, if it assisted, we can provide the committee through the secretariat with an assessment of current costs of handling and some projections on increased costs as—

CHAIR—May I say to you, Mr Ryan, we would welcome that information.

Mr Ryan—Yes. Subject to your concurrence, we would probably like to provide that on a commercial-in-confidence basis.

CHAIR—No problem.

Mr ANTHONY—If you haven't got the information now, perhaps you could submit it, as to what you anticipate the actual cost would be if the thresholds were reduced to a couple of different levels, and also the $50 fee, if that was reduced. That would be important evidence for us to have, to know the actual projected costs.

Mr Grosser—Certainly, and what we will try to do, Mr Anthony, in fact—as Mr Ryan has already indicated—is assess our current costs and try to come up with some projections of what the impact would be within the facilities on the specific issue of processing items that require duties and taxes to be paid.

Senator WATSON—Obviously a movement of $50 to $25 is going to affect a lot of items. What happens if you moved it for revenue purposes from $50 to $40?

Mr Grosser—From the parcel side, probably not a lot. But it would depend on the investigations that Customs are currently doing with regard to the lightweight items, and the majority of the material comes in as lightweight items. They are going to come back with some information which might help us in answering your question. Off the cuff, I haven't got a specific answer. I have been trying to make some crude assumptions in our discussions today, but we must await this information to really try to provide some clarity to some of our projections.

CHAIR—I thank you very much for coming today and for your submission. We look forward to your additional information. May I also say that we did appreciate the opportunity to visit the Clyde Mail Exchange. It was most informative. And, with respect, those containers get opened and they go on the conveyor belt—there ain't no dogs and there ain't nobody; they just go on the conveyor belt—and somebody decides which chute they go down—full stop—every container.

[10.18 a.m.]

CURTIS, Mr Thomas Alexander, Manager, Customs and Trade Services, Coles Myer Ltd, 800 Toorak Road, Tooronga, Victoria 3146

CHAIR—I now welcome the representative from Coles Myer Ltd to today's hearing. Tom, thank you very much for coming to talk to us today, and thank you for your submission. Would you like to make a brief opening statement to the committee before we ask you questions about your formal submission?

Mr Curtis—Certainly. Thank you. May I begin by saying that Coles Myer welcomes this inquiry into the Internet commerce as a positive attempt to try to raise awareness of the issues and look into the future of Internet trading. We appreciate the opportunity to appear here and provide further comment today. Our written submission discussed some of the taxation aspects of cross-border Internet trading which impact on the retail industry.

Generally speaking, our submission argues in favour of an equitable treatment of all imported goods, regardless of the medium by which the import sales transaction was negotiated. Any business advantage gained due to the non-payment of import duty or sales tax is likely to discriminate against Australian business, and this position appears not inconsistent with the principles that were outlined in the recent ATO report *Tax and the Internet*. However, Coles Myer reserves its position on the broader issues of Internet commerce pending further consideration. For this reason, our submission and my comments today will be specifically restricted to the single issue of the taxation treatment of imports.

Our experience generally has been that there has been a great deal of uncertainty surrounding the whole issue, and a number of assumptions, some of which we would challenge basically on the premise that there is no hard evidence. Perhaps, through our discussion, that can come out today.

CHAIR—Thank you for that. I noted that in your submission you talked about a balanced solution. You said something to the effect:

It is difficult to avoid surmising that, without careful reassessment of our taxation regime, the much-anticipated growth of Internet trading will adversely effect the Australian retail industry's sales and profit in relation to import of goods and distribution of services via the Internet.

You say it is a short-term problem, but you went on and said:

Whatever long-term solutions may be devised, the fact is that action in the short term is becoming increasingly urgent. Coles Myer believes that denial of the benefit of the threshold to commercial consignments is an early step which needs to be taken and it appears that additional personnel in the assessment activity would generate far more revenue than they would cost, as well as making a material contribution to community protection.

Can you give us some evidence for that?

Mr Curtis—It is a difficult issue to look at and speculate. There are obviously winners and losers in every type of transaction. Through Internet shopping, there is the potential for trade diversion, first of all, away from retail into the Internet medium. There is also the migration of certain aspects of the supply chain going from as they exist at the moment into an offshore type environment. I'm sorry, can I ask you to just rephrase the question?

CHAIR—Yes. You say you believe that denial of the benefit of the threshold to commercial consignments is an early step that needs to be taken. In other words, you want to reduce the screen-free limit. Is that correct?

Mr Curtis—Correct.

CHAIR—You want to reduce the screen-free limit, so increase inspection activities by Australian Customs, increase the paperwork and increase theoretically the amount of duty and sales tax paid and, at the same time, signal to the rest of the world that we are putting back up protectionist barriers. Is that correct?

Mr Curtis—I would look at it slightly differently. We are not saying that we are raising protectionist barriers. What we are asking for is pure equity. At the moment, if there is a high tax-free threshold then that opportunity will allow a number of goods to come through. Linked with that is potential lost sales at the retail level. You mentioned before, and it has been noted in the KPMG report, that there is approximately $25 million worth of leakage through the system. If that $25 million relates to a general tax rate of 10 per cent, we are looking at $250 million lost retail sales. If it is higher, if it is a 20 per cent tax limit, taking into account sales tax and a little bit of customs, then we are looking at a much higher figure, over $500 million worth of sales lost at the retail level.

At the moment an advantage is provided to people who configure consignments, whether it is done overseas or through the Internet by somebody based here, so that they can come through the customs barrier and miss that tax net of paying the customs duty and the sales tax that all major imported supply chains are burdened with. At the same time, when you look at the threshold for making a formal entry, all commercial importers have to pay a cost then to the cost recovery program initiated by Customs, which is very significant. They have to go through all the processes and fight all the red tape, which are embedded costs in their cost to sell goods, and the cost recovery regime, in equity, should be applied to all importers.

One suggestion we could make would be that these same duty concessions are broadened and that all sales tax and customs duties are eliminated on imports. That would be going down a true free trade path. If that is not acceptable, then perhaps we have to go the other way in the terms of equity and say that the exemption should be completely eliminated, everybody subject to the same level of tax and duty. In that case, there would still be an opportunity for people with bona fide access to concessions, such as somebody who has sent you a gift from overseas, a bequest, a medal or something like that. You could still approach the relevant authorities and claim that type of concession. It doesn't eliminate that. All it does is bring us back to the same playing field where the same costs and the same taxes are imposed on all importations through the customs barrier.

Mr BEDDALL—Mr Curtis, can I follow through on that point. I think you were here when Australia Post was giving us the example of the Christmas cakes.

Mr Curtis—Yes.

Mr BEDDALL—Obviously Coles Myer supplies, through their food outlets, Christmas cakes. Isn't the argument here that everybody selling to the Australian market should pay the same tax rate, and in fact somebody who is doing that is using a loophole to avoid tax, and therefore has a price competitive advantage over the Australian wholesaler or retailer, and rather than increase competitive protectionist barriers, we are actually making everyone pay the same? I think this is probably one of the major issues which is going to face the Internet commerce, particularly in goods; not so much services but goods. If you take the $1,000 and make it $10,000 it doesn't matter. It is the $50 that maybe should come to zero. The arguments that Australia Post and Customs put forward against it are the logistic arguments rather than an equity argument. Is that a view you would share?

Mr Curtis—I can understand what they are saying, but I get back to the cost recovery issue also. There is equity in that. If it is a logistical argument then perhaps we should look at that. I think I may have heard you mention earlier that there can be an automatic tax impost on perhaps consignments under a certain value. That may be another way of looking at it, but we have had anecdotal evidence also that there is some fairly widespread misdescription and undervaluation. Unless there is some form of very strict monitoring, that cannot come up in any estimates because it is by definition inestimable. It has escaped the net. It has beaten the system.

If there are such practices going on, then that is obviously eating away at the retail sales also. Everything that eats away at retail sales can be attributed through this Internet trading to lead to what they call disintermediation. Disintermediation would affect not only the jobs of people actively and directly involved in retail but all the service industries as well. That is cleaners. That is advertising. That is everybody on this side of the customs net, because everything associated with retail is only employed on the basis of continued profits and growth in the retail industry, so if those jobs are exported then so are all the jobs that proportionately rely on them.

That goes even further. If you look at the case for a CD, if you go into a store today and you want to select a CD, you can browse, you can do all sorts of things, but basically you are assured of the quality. If you want to browse on the Internet, the only thing you will be asking is, 'Is it the group I want?' You know what you are going to buy as a product. My understanding is that if you click on the right button and order your CD and make payment, that CD is packaged, shipped out through an express courier or via mail, it comes through the customs barrier, it may or may not attract duty, if it comes in under the threshold it won't attract sales tax, and it is delivered.

If that is delivered at a lower price point than you can get it in your store today—without going into the copyright issues—you will buy over the Internet. If that happens, there is not only dis-intermediation but you are encouraging the purchase of the foreign pressed Cds over the locally pressed Cds, and that sort of impact can flow through into other industries as well, I would suggest. So dis-intermediation is wider than pure service industries. It can affect manufacturing industries.

CHAIR—I gather from your comments that you would like to put the barrier back up again?

Mr Curtis—I wouldn't say 'barrier again'.

CHAIR—Shall we surround the continent in a brick wall?

Mr Curtis—We are quite prepared to compete on a level playing field.

CHAIR—Myer Direct sends me catalogues once every three months. I buy from Myer Direct. It used to be—

Mr Curtis—Inch Cape or somebody, was it?

CHAIR—Was it? It doesn't matter anyway. Do you send Myer Direct catalogues to clients in the United States?

Mr Curtis—At this stage I don't think we do, but we do to New Zealand.

CHAIR—And do you have an Internet Web site? Do you market your products for sale overseas?

Mr Curtis—At this stage I don't believe we do, no. Myer Direct is a good example in many ways though. Myer Direct has a very firm and very vibrant policy of promoting Australian product. If you have a look through that Myer Direct catalogue, you will see predominantly the goods are marked underneath 'Proudly made in Australia', particularly the clothing items.

CHAIR—May I suggest to you that the shirt I am wearing I bought from Myer Direct and it is made in China.

Mr Curtis—Some is, yes.

CHAIR—Almost everything in the Myer Direct catalogue is.

Mr Curtis—The last time I looked at it, it wasn't.

CHAIR—It used to be called Lands End, by the way.

Mr Curtis—Lands End, correct.

Mr BEDDALL—I believe that should be a zero tax threshold, because if you have to pay wholesale tax on a shirt bought either through Myer Direct or through Myers or through the local Tom Cobbleigh store, why should that shirt not attract tax if it comes through overseas purchasing? The argument has been in the past that it is too difficult to get one-off items, so it was only a small amount, but if Internet commerce takes off the way it is, people will shop on price. I don't care if they buy on price and the item is cheaper because it is cheaper, but if it is cheaper only because it is avoiding Australian tax, then that is a disadvantage to Australia. Isn't that the sort of measure we have to put in place?

Mr Curtis—I agree totally. That is an advantage. It is purely tax-driven for a certain business process or a certain element of the business community.

Mr BEDDALL—We have had evidence from people in the Fishing Tackle Association who are internationally price-competitive. They do compete on price and are in fact often cheaper than their US counterparts. But we have also had evidence from the Jewellery Association that says all doom will come because they will face cheap imports, but they are not internationally competitive. So they are commercial things that will happen.

Mr Curtis—Yes, I think it is a difficult one and it is very dangerous, as I said in the beginning, to put a simplistic approach on it. For instance there is a lot of anecdotal evidence in some of the reports, like the ATO reports suggest that Internet commerce is going to be restricted, initially at least, to several items, several product lines, like Cds, books, software. Walmart in the US, which is one of the largest US retailers, has just opened up a Web site with 80,000 products available. That suggests it is going to be much larger than just a couple of very specific easily transportable product groups.

With a wider product range there is another issue that comes up, whether we are talking about branded product or generic product. If you want to buy a generic product, a T-shirt with no brand name there is really no advantage to you as a consumer looking for it on the net. You won't know about the quality, you won't know about the size, the fit, all these sorts of things, or even the colour. However, if you want to buy a branded product, whether it is an electronic good or a piece of apparel or, as we said before, a CD by a certain group, because it has that brand name you are fairly certain of standards being met in relation to those aspects. So all you are doing, as you said before, is shopping for price, and if that can be offered, for instance, by a manufacturer overseas, it cuts out all that middle chain.

Senator WATSON—Mr Curtis, do you intend to set up your own Web site, somewhat similar to the overseas example you just gave us?

Mr Curtis—I believe we will look at setting up a Web site. We have signed an agreement with Peapod and we are looking at the opportunities, but as I said in the beginning, at this stage we are still researching the viability.

Mr BEDDALL—The disadvantage for an Australian Web site is Walmart is on the US Internet, and unless you are on that Internet it is going to be very hard to find Coles Myer, even if you want to, from the US, isn't it?

Mr Curtis—I would agree with that, yes.

Senator WATSON—By the same token we were told by the Antiquarian Booksellers Association that they have expanded their business dramatically. A large percentage of members of their association have expanded their sales in a time when retail sales and book sales particularly in their area, old books, was declining. Instead they have got a growth industry because they went out and established Web sites and are selling all over the world. They are happy with everything being screen-free, and they intend to compete internationally. But Coles Myer is telling us that we need the barriers back up again and you are not really sure whether this international business opportunity is viable or not.

Mr Curtis—I must have misled you. I am not saying whether it is viable. We are looking at it from our business perspective and researching it, when we should enter, how we should enter, if we should enter. Those questions haven't been answered yet, because there is uncertainty about a number of aspects and it is a business proposal that needs quite a lot of assessment. As far as books are concerned, anybody who is selling books really wouldn't be terribly concerned about thresholds because books, to my understanding, are duty and tax free worldwide under the Florence Convention, so there is no impact on them.

But it is not a simple situation where we can look at everything and lump it together. Within retail sales over the Internet I think you have to look at each product category, whether it is electronics, whether it is homewares. For instance, would you go and order a fridge over the Internet and if you did obviously you would want to order it from Australia because the transport costs of getting a fridge ordered from the Internet from the States would be a killer. So it is something we have to divide up and look at individually for specific groups.

Our issue today is looking only at cross-border Internet trading, and whilst you are using the word 'barrier' I would prefer to say equity with the way we are treated at that barrier.

Mr BEDDALL—Can I get that right, because Coles Myer is not arguing for any additional impost.

Mr Curtis—No.

Mr BEDDALL—Just the current impost be applied. If you import all the shirts for Mr Charles you pay the duty.

Mr Curtis—That is correct.

Mr BEDDALL—If he imports it from the manufacturer, one-off, he doesn't.

Mr Curtis—He gets an exemption from that duty; he gets a special privilege, if you like.

CHAIR—But that is true today. The evidence that we have is everyone has told that Internet's commerce is having virtually no impact so far in Australia, and you are suggesting that already for some reason your business is suffering because some clothing items and other items come in through either Australia Post or through commercial chains with the $50 screen fee limit and it is causing you loss of retail sales.

Mr Curtis—There is potential loss. We are getting anecdotal evidence from our suppliers, such as the Fishing Tackle Association. We are getting a lot of feedback from our suppliers. It is something we can't measure because there are no areas where you can capture those sort of statistics at this stage. Now, whether Internet trade has a big impact on the way we do business today, tomorrow and the day after, I personally think it will have a big impact. But again we are not talking today, as I understand it, about Internet trade; we are talking about tangible goods ordered via the medium of the Internet. We are not taxing the Internet as a medium itself, only the goods that come through.

Senator WATSON—Mr Curtis, you indicated that you are looking at the feasibility of setting up your own Web sites.

Mr Curtis—Yes.

Senator WATSON—Following on from that you would be aware that Australia

Post is looking at some encryption arrangements which could go under the name of Key Post or some similar name. Have you participated in that and how will you interact with that sort of arrangement providing security to people who can provide their credit card over the Net in an encrypted form?

Mr Curtis—Senator, I will have to defer on that, because that is an area that is looked after by some of our IT people.

Senator WATSON—Could you give us a paper on that?

Mr Curtis—I could ask them, certainly.

Senator WATSON—I think it is part of this wider debate that obviously is going to evolve, and I would imagine you could well be key players in that whole arrangement, because you could well be one of the big users. If you could give us a paper on that, that would be great.

Mr Curtis—Can we get specific questions on that afterwards and I will follow it up for you.

Senator WATSON—Thank you. The security arrangements we are particularly interested in.

Mr BEDDALL—Going back to what you were saying before about brands, in fact there is some argument that probably merchandise trades will be in fact much less than 50 per cent of the Internet trade; it will be services rather than software et cetera. But because of the need to know what you are buying, it then becomes the premium end of the market that will be traded on the Internet, isn't it, rather than, as you say, the T-shirt range.

Mr Curtis—That is right.

Mr BEDDALL—So it might be that the top-of-the-range Italian suits will be traded because you know the brand and you can put measurements in and they come out the other end. It won't be the $199 one from Lowes.

Mr Curtis—Most likely, correct, yes.

Mr BEDDALL—So in fact it becomes almost an elite shopping network in that sense, doesn't it?

Mr Curtis—In one way it could be elitist, but I think we have also got to remember that you have your brand names, for instance, in sporting goods; that is a good one.

Mr BEDDALL—Yes.

Mr Curtis—Adidas, Nike, Puma, Reebok, they dominate the market globally, and that is what all the younger consumers, particularly, are after. That is an ideal medium for them to go and shop for the latest shoe, the latest T-shirt. But branded goods need not be in the luxury category.

Mr ANTHONY—When you mention the competitiveness of the tax regime with the items coming through the Internet which don't pay that, you talk about the need for a careful reassessment of our taxation regime in your submission. What suggestions would you make about the current wholesale sales tax system?

Mr Curtis—Perhaps very broadly just a couple of comments, it would be our view that there are certain biases in the current tax regime: first of all against suppliers of goods there are no equivalent taxes imposed on suppliers of services, and secondly towards high tax rates which are making Australia uncompetitive on the international scene. Therefore we would favour a rationalisation of the tax system which could be categorised at the moment as being inefficient, it has multiple rates, it is narrowly based and it is targeted at selected goods rather than services.

We would also favour a lowering of the overall tax rate on individuals. If one looks further at the current debate on tax reform, I guess one of our concerns that is shared with a number of businesses is that if any type of GST does result from that tax reform process, we would be concerned about the compliance costs, and in that regard we would seek as much as possible to make sure that it is a very simple system, that it has a single rate, if possible, and it provides for a minimum of exemptions.

Mr ANTHONY—Do you have any view about the rate and how it might be implemented?

Mr Curtis—Not at this stage. I think that is probably part of the whole tax reform process which, to my understanding, we are involved with.

Senator WATSON—The problem is, the higher the rate the more the inducement to go onto the Internet. This is where you have a problem with your Cds which have a high sales tax.

Mr Curtis—Correct.

Senator WATSON—So the lower your GST or consumption tax, the less likely people are going to take advantage of the differential taxes between Australia and overseas.

Mr Curtis—I guess another impact, which I haven't worked into any scenarios, is that there will be those items which are hit with a tax under GST which previously were not. So there would be, if you like, a levelling out of tax rates across products and that would have another impact on the way people look at goods in ordering through the Internet.

Senator WATSON—It raises questions as to whether there could be implications if it is to sit at too high a level.

Mr Curtis—Correct.

CHAIR—If there was a broad-base consumption tax and it was at a relatively low level, and considering the wholesale sales tax and combined duty at the moment, with duty still falling—on most of the stuff except clothing—to zero before long, if that regime was in place would that change your view about the $50 screen-free limit?

Mr Curtis—I don't think it would substantially. We are still after an equal competitive position, not a competitive advantage that is provided to a particular group because of loopholes in the tax regime, if you like.

CHAIR—So even in the long term, goods entering the Australian marketplace or services entering the marketplace via the Internet, you want to see somehow taxed at the same rate that internal goods move around Australia are taxed. Is that correct?

Mr Curtis—Correct. So we are all in the same environment and are treated equally.

CHAIR—Regardless of the cost.

Mr Curtis—You mean the cost imposed on government to apply that tax?

CHAIR—The cost imposed on the community.

Mr Curtis—At the moment, as I said before, when we bring goods into the country through the Customs Service, through their barrier, we bear the cost through their cost recovery program. Again in equity that same principle should be applied across the board, one would imagine.

Senator WATSON—In terms of Internet sales, would it be easier for people such as Coles if the tax was attached to the payment, rather than to the delivery of goods?

Mr Curtis—Cross-border trading?

Senator WATSON—So there had to be a declaration through the banking system or payment system, that this was in respect of imported goods. Could you get your equity that way? I'm just trying to overcome your problem of getting a more level playing field. Obviously the banks mightn't like it.

Mr Curtis—I am not really sure, I haven't really considered that but that is obviously a huge one for the finance industry, yes. I haven't really considered that. We have always traditionally looked at the tax as being imposed on the goods, not the financial flow of cash. I guess that opens up other opportunities; you would have money flows going all over the place not linked directly to particular goods which may be imported.

Mr ANTHONY—With Coles Myer at the moment, just refresh my memory, what percentage of every dollar spent goes through that organisation?

Mr Curtis—I couldn't give you an accurate figure.

Mr ANTHONY—Is it 15 per cent?

Mr Curtis—I have heard figures of about 30 per cent, but I think that is a bit exaggerated. As a corporation, to put it in perspective, we have over 150,000 Australians employed and we have over 1,800 retail sites, so that is a heavy investment.

Mr ANTHONY—So might we conservatively say 25 per cent of disposable income goes through Coles Myer somehow.

Mr Curtis—Retail sales, not disposable.

Mr ANTHONY—Retail sales.

Mr Curtis—Yes. You have got to remember a lot of that is supermarkets as well.

Mr ANTHONY—Yes, sure.

Mr Curtis—I don't think we would be looking at that as coming within the ambit of the cross-border trade.

Mr ANTHONY—So when you look at your supermarkets relative to other retail goods, what percentage is your supermarket? Is it half?

Mr Curtis—You are asking all the hard questions now. Let me have a look for you.

Mr ANTHONY—We are talking about Internet. Just being a bit more elementary, back in the supermarket it would be zero, wouldn't it?

Mr Curtis—I would say so, yes—at this stage.

Mr ANTHONY—So following this through, one of your concerns is that obviously Internet sales are going to potentially take away from your bottom line, and of course small retailers. The problem that we have is that at the end of the day it becomes not just the threshold issue but policing it.

Mr Curtis—Enforcement.

Mr ANTHONY—Exactly, through enforcement, and obviously if we were to have a much stronger barrier, as you advocate—a quasi tariff barrier or whatever—then it means greater enforcement, which means greater cost. Would you foresee perhaps that large retailers—of which you take 25 per cent of the dollar—may wish to make a contribution to increase policing at the barrier, to therefore protect your market share, because it has got greater policing at Customs or Australia Post? Would that be a scenario perhaps that you may wish to entertain to maintain your market share?

Mr Curtis—I don't quite follow how it can be protecting our market share. What we are doing, as I said before, is asking for there to be no tax advantage which we cannot have access to, that provides for this medium of bringing goods in, which will lead to lost sales, lost jobs, et cetera. If you are talking about a pure contribution, we are making our contributions now. We are talking about the retail industry. I have just said, we have over 150,000 employees. We probably have one of the highest payroll tax bills in Australia, whereas small retailers don't have that type of tax burden through various concessions.

At the moment in any business we go into, we are subject to the laws, to the rules and to paying any costs associated with that. What we have at the moment is a system which doesn't impose any of those costs, and if there are any costs associated at the moment, I guess the question is, where are they absorbed within Customs at present? If there has to be extra resources put into it, and there is a true cost recovery program, then those costs must be recovered from that particular program, not from another program, otherwise it is just cross-subsidisation.

Mr ANTHONY—But at the end of the day, no matter what the thresholds are or the tax regime, it comes basically down to enforcement, doesn't it?

Mr Curtis—To a certain degree, and if some of the anecdotal evidence we are getting back about undervaluation and misdescription is correct, then isn't it a fair premise that we should have more enforcement in that area?

CHAIR—Isn't it true, though, that what you are putting to the committee really isn't about the inquiry, it is not about the Internet, your complaint is with the current taxation regime, which allows a concessional entry for goods below $50 combined sales tax/wholesale duty, also sales tax and excise. You are not really talking about the Internet.

Mr Curtis—Not the Internet as a medium.

CHAIR—You are not happy with the current regime. Is that correct?

Mr Curtis—No. I think what we are talking about is trade via the Internet, so it is obviously connected with the inquiry. That is why we answered in relation to the terms of reference. Part of the debate we have seen in the papers is, 'Okay, there will be no new taxes on the Internet.' That is fine, but if the goods delivered via the Internet aren't taxed, then you are opening up a whole new supply chain that comes into Australia and undercuts existing business through this tax advantage.

CHAIR—Is it a new supply chain or is it perhaps just changing the number or relativity of goods that are already purchased from overseas through other mechanisms—that is, like mail order, that is Myer Direct, which appears only to operate in Australia, except you do some trade, you said, in New Zealand.

Mr Curtis—A little bit with New Zealand, yes. We will compete on any footing, as long as it is equal. If this regime continues then, yes, perhaps we will have to consider very seriously whether we enter it, but would that mean a lot of the resources would have to be located offshore and that we would simply use Australia as a place through the Internet as a catalogue and delivering direct to customers? As new opportunities arise, as new technologies arise, they create opportunities that weren't previously existing. The whole business of transport and logistics has been changing rapidly over the past few years. The Internet has been a bonus to that, and electronic trading generally, enabling us to reduce a certain amount of paperwork. But what we are talking about here is more than just a subtle shift. It is a greater shift that has impact right through our retail industry.

Mr BEDDALL—There would be nothing to stop Coles Myer, in this brave new world, from going off to the Cayman Islands, establishing a Web site, zero tax. Chairman orders his shirt through Myer Direct Web site. It comes from China into Australia. Coles Myer will still make its margin, probably make a better margin.

Mr Curtis—It may well do, if we configure it correctly, if that is what you want us to do.

Mr BEDDALL—No, I am just saying that is what the consequence can be.

Mr Curtis—Is this a business plan we should look at?

CHAIR—I have got different kinds of concerns here, with both the tenor of your report to the inquiry and your evidence today. I really feel that Coles are saying, 'We're only having a look at whether the Internet is a viable medium or not, but we already think it's going to affect us adversely,' but I am advised that your major competitor is already on the Internet in Australia selling from their supermarkets to homes on a regular basis, where you can order your shopping list on a regular basis every week. You get so many litres of milk and so many packages of Weetbix, and whatever, and then you can add new items that you want, and it is delivered to your door every week through the Internet. And you aren't there yet.

Mr Curtis—Correct, we aren't there yet. That report appearing in the newspaper, I think, is related to a small trial in Western Australia. Is that correct?

CHAIR—I thought it was Queensland, but I could be wrong.

Mr Curtis—Queensland? It could be. There are a number of trials that have been going on around the world in a number of technologies, such as home shopping through the television, et cetera, and as these new technologies are trialled and the response rates come through, we will monitor them and assess the viability and how and when we wish to enter the market. Obviously at different times you enter the market, there are different advantages, there are different costs. Unfortunately I am not part of that strategy, so I can only report the facts, which is today we are not selling on the Internet but we are considering the opportunity.

CHAIR—When you talked about sales tax, customs duty and excise, talking about products being sold on the Internet, you said for the normal supplier of direct selling or mail order middleman, there is plenty of capital and revenue available to provide systems and guarantee certainty of product delivery and security of payment arrangements. You seem to imply that there are security payment arrangements which are lacking with respect to Internet sales. I don't know whether you want to comment further on that.

Mr Curtis—I think that feeling is existing with a lot of customers at the moment, but I am sure it will change, first of all as new technologies come up with the new Visa cards and Amex cards that they are working with, and as people become more accustomed to the process of making a purchase over the Internet. In fact, that is one of the three things that Walmart looked at when it went the extra step and put 80,000 items on the Web. It looked at people's experience. They had made an initial one or two purchases for something small, and found they could manage it. They found they were capable personally of going through that whole transaction, and they found they could locate the goods they wanted. So those things are probably part of a public awareness, a public pick-up of the technology, and as that advances with the new encryption—if that is what it is called—for ensuring safe payment, then yes, I think it will grow from there.

CHAIR—May I say thank you very much again for your report, Mr Curtis, and thank you for answering our questions. We hope to finish our inquiry next April or May, and we will certainly be happy to send you a copy of our report.

Mr Curtis—Thank you.

[11.15 a.m.]

KENT, Mr Andrew, Director IT and Communications, Australian Society of Certified Practising Accountants, 170 Queen Street, Melbourne, Victoria 3000

McKENNA, Mr Michael, Executive Director, Australian Society of Certified Practising Accountants, 170 Queen Street, Melbourne, Victoria 3000

CHAIR—I now welcome representatives of the Australian Society of CPAs to today's hearing. Gentlemen, thank you for both your submission and coming to talk to us today. Do you have a brief opening statement you would like to make before we start asking you intense questions about your submission?

Mr Kent—The only statement I would make is that some things have happened since we made the submission, so we will have a further addition to it, but I think we can start on what we originally submitted.

CHAIR—Will that be today or later?

Mr Kent—Yes, I have got a short document for you.

CHAIR—We will authorise that for publication later. In your submission, what I think you said was that on-line catalogues are now the major source of growth on the Internet. I was a bit surprised that we are talking about goods as being the growth area rather than services.

Mr Kent—That depends on the definition of 'catalogue'. It is the method of business we are looking at, rather than the actual type of goods transacted. On-line catalogues are being used for service, sale of service, and electronic goods and hard goods, so in our definition of on-line catalogues we are taking all of those various forms of goods and service delivery into account. We are really looking at what type of business this is emulating. That is how we have broken the various business sections down.

CHAIR—In your submission, talking about the US Treasury white paper, you said:

> If recommended, the emphasis of the tax system shifts from source-based taxation to resident-based taxation. That is, from the location of the income-generating activity to the location of the income-generating entity.

You said you are not certain it is the right approach, but you recognise that the approaches taken must be consistent internationally. Could you expand on that in some depth, please.

Mr Kent—There are two main forms of taxation, one being on income and one being on transactions, essentially, being sales tax or whatever. The US Treasury white paper recognised that whilst the location of the transaction and the location of the participants and so forth were sometimes difficult to determine or relate back to traditional tax law, the location of the individual and the residency of the individual or the individual entity were always certain. It was a similar sort of argument to saying that a child should always be named after the mother because you always know who the mother is. It was just they were really addressing the uncertainty of the potential participants.

In looking at that, that is flowed through, particularly taking into account the general approach for neutrality in tax, being that anything done on line should be the same as anything done off line. So if you sell a pair of socks on line, it should be treated the same as if you sold a pair of socks off line. Neutrality in tax treatment is underwriting a lot of the tax treatment throughout the world as to how this thing will be taxed. If they do change this, it will change a lot of the underlying tax structure for a lot of things. Really it is far too early to tell whether or not this is a good idea. So that is why we are saying we recognise it as an issue. We are not sure that it is the right thing, because the implications for it are so wide and varied that we have no real way of telling at this point whether or not it is a good idea.

CHAIR—We understand that international discussions are going on at a rather rigorous pace at the moment about some of these issues; like, for instance, a company perhaps physically located on mainland Australia with a Web site generated in the Cayman Islands and downloading information, say, in the United States or Canada or England. There are huge implications regarding the transfer of funds electronically, and the locational aspects, where they reside, how they come back, and how you treat those funds in a tax sense or how you control them or even know what is happening to them. Have you got further comments about all that, and are you participating in these discussions, or sitting on the fringes?

Mr Kent—I am actually in another role that I have, and that is the technical support for the International Federation of Accountants IT Committee. I am the nominated person to look after international tax issues on the Internet on that. In way or another we are very much at the core of that. Just in resolving some of those issues, one of the reasons we presented the paper in the way it is done, in breaking those business models down, is that if you can align the type of business you are doing over the Internet with one of those business models, a lot of the taxing and regulation issues fall out quite neatly.

If, for instance, you are looking at say a cartoon site which has advertising and so forth, then you simply say that is part of the media model. What they are really doing there is gathering ads on the basis that they are attracting an audience and so forth. There are quite clear cases of this sort of thing happening before with TV stations located in Canada largely transmitting into America, and where should the revenue reside and so forth? So a lot of these things have been tested by international law before, based on these models. So in the case of a media model, it is based on the location of the actual studio.

The only clarification that needs to be made then is whether or not the studio is where the server resides or whether it is where the entity resides. The general approach to that is, it is where the work is done, so it is where the Web staff are. If it is staffed primarily in Australia, then that is considered to be the location of it. So a lot of these issues fall out quite neatly if you can align it back to a predefined type of business. Another one is the on-line catalogues. We have looked at catalogues again. Mail order catalogues have been around for a long time, so if you actually relate retail activity back to catalogues, a lot of the issues fall out.

There are test cases saying a catalogue is seen to be a form of advertising, a form of solicitation, and the actual location of the sale, et cetera, is deemed to be where the fulfilment takes place, or, rather, where the order is generated, processed and sent from. So, again, a lot of those issues fall out in the retail side of it if you can relate it back to a predefined business.

Mr BEDDALL—So you are saying that is where the tax is payable?

Mr Kent—At the moment if we say it is a mail order catalogue, then the international tax ruling on that is that the tax is payable where the order is taken and processed and where the goods are sent from. It is obviously a lot clearer if the warehouse and the order processing operation are in the same country. At the moment that is generally the case. That is then deemed to be the country of origin and the point of sale.

Mr BEDDALL—What about the implications, then, for the rest of the world outside of the United States? Because I think something like 85, 90 per cent of Web sites are domiciled in the US, Web supply networks in the US. I mean, no wonder the US is keen on the Internet. They will be the only ones getting revenue.

Mr Kent—You look at where this thing started from. The Internet came from America. It has grown fastest in America, therefore it is primarily in America. That does not mean that other countries can’t take a much larger slice of the cake. I think if we assume that Australia is going to be a victim of the Internet, then we will inevitably be that. I think we need to start trying to position Australia as a powerful player in this. If you look at some of the aspects as to why you locate your Internet site somewhere—which is in fact some of the additional material we are bringing along here—there are things like the legislative system in which you operate. If you are going to have any sort of lawsuit, I would much rather face that in Australia than in the US.

You have got to look at some of the tax treatment. Australia’s tax system is not very friendly to the Internet at the moment. You have got to look at the culture, the language of the place, the skill set and so forth. There is no reason why the majority of the Internet is going to remain in the US, just because that is where it started from. If you are delivering hard goods, it is much cheaper to deliver them out of Australia than it is to deliver them out of the US into Asia, for instance. There are a whole lot of reasons to say that the Internet business is not going to stay in America. Certainly it started there. Certainly they have the lion’s share of it. But that doesn’t mean it is going to stay there.

Mr BEDDALL—Aren’t they going to have a competitive tax advantage over the rest of the world? We keep hearing how everyone has got a goods and services type tax except the United States, but nobody actually mentions that a fair bit. If we impost a GST on all goods and services, as the Europeans have, as most of Asia is now moving towards, then once more won’t we give a competitive advantage to the United States?

Mr Kent—It would give them a much greater competitive advantage if we slug everything with a wholesale tax before it goes and cops a sales tax in Europe and so forth, as well. I think if we are out of alignment with our tax treatment, then we are in a much worse position than if we come into alignment. As for no sales tax in the US, there is no national sales tax but there is a sales tax by just about every state in the US.

Mr BEDDALL—No GST.

Mr Kent—If you actually look at the end point, most people in the US are being slugged sales tax on Internet goods because of the state in which they are. So there is no national sales tax. There is sales tax in most states. If you look at the end consumer, yes, they are paying sales tax. I think a lot of these issues need to be brought together, to set Australia up as a good place to set up an Internet site from. The US is really struggling with a lot of the authentication issues and so forth because of their privacy laws. Australia is actually much better positioned in that regard, so as far as dealing with an authentic business and business authentication, Australia is much better placed to actually get that right. We are well down the track to be well positioned in this industry.

Mr BEDDALL—Apart from the Deputy Prime Minister’s famous Web site, how many more have we actually got? Is there evidence that what you are saying is the ideal world is actually happening?

Mr Kent—You mean are Australian businesses taking up on this?

Mr BEDDALL—Yes.

Mr Kent—We have got quite a few good sites. The CPA’s own site is the best accounting site in the world, and is well recognised as that.

Mr BEDDALL—And is currently tax-exempt.

CHAIR—If you do say so yourself.

Mr BEDDALL—It is currently tax-exempt, isn’t it?

Mr Kent—Because we are a professional body.

Mr BEDDALL—It is a service, yes.

Mr Kent—The GST is an issue. I think Australia is looking at how it taxes everything, and it has got to look at how it taxes everything in regard to the Internet as well. This is a major growth area, and it needs to be considered in the overall picture.

Mr ANTHONY—That's the sixty-four million dollar question, Andrew. You have mentioned in your submission that the Internet should be taxed, but not at a tax rate which impedes growth. What have you got in mind, and how do you do it?

Mr McKenna—Aren't we saying more, though, that we shouldn't be taxing the Internet per se, but we should be taxing business the way it is done? Whether the business is done on the Internet, or through the mail, through the fax, or over the counter, the same basic tax principles should apply, and there shouldn't be an extra tax because you are using a different medium to do the business.

Mr ANTHONY—I suppose the issue, as you have pointed out, is where do you capture it?

Mr BEDDALL—Where is it domiciled?

Mr ANTHONY—That is right, and what do you capture?

Mr McKenna—That was the point I think that Andrew was trying to make earlier, that if you are receiving the orders and processing the orders in Melbourne, the income is therefore earned in Australia, in Melbourne, and taxed in Australia in Melbourne. If we have got a warehouse in Hong Kong and we are doing all the processing in Hong Kong, then the business would be being done in Hong Kong and taxed in Hong Kong.

Mr ANTHONY—This is the issue from a Commonwealth point of view. Clearly you would locate in a low tax country, you would be in Hong Kong with your warehouse, and that is where you would process it. That is what would happen. I appreciate those arguments that you have got, but when it comes down to those goods being delivered directly to me or through an intermediary, the tax revenue is being collected by someone else, and good luck to them, but it is not for us.

Mr Kent—Again there are two main forms of taxation revenue. One is income based and one is transaction based. Clearly if you swing the balance of that towards income based rather than transaction based, then on individual transactions that is better. You have to get that balance right. I don't have the magical numbers to say, 'These are the numbers that are right,' but you need to look at the overall picture on that.

Mr McKenna—As a broad principle in terms of taxation, the taxation reform issues that are being addressed at the moment must address our taxing system so that we are internationally competitive. We have some special requirements in this country. We have got a social security system that has to be funded. Some countries don't have one and so they will always enjoy a tax advantage in that regard. But we have to get as close to being internationally competitive as we possibly can so that we can trade cross-border competitively. One of the advantages of the proposed GST as a form of tax is that the exports are not taxed to the same extent, so that we can be internationally competitive.

Mr BEDDALL—But tax is a zero sum game.

Mr McKenna—Yes.

Mr BEDDALL—If you are reducing tax on services so you are internationally competitive, this is an argument for increased personal tax.

Mr McKenna—I don't think the current government is talking about it actually.

Mr ANTHONY—I don't think you are either.

Mr McKenna—I think we could be.

Mr ANTHONY—I guess what we are saying is the balance has to be right, but I think there is a problem when your transaction tax is based at a wholesale level and then you get slugged again at a retail level further down the line. I think the closer we come into line with other players, the more competitive we are going to be. Wholesale tax is clearly uncompetitive. That is a form of transaction tax. It just happens earlier in the process and, rather than swinging the balance between income tax and transaction tax, perhaps we should just bring our transaction tax more in line with what is happening internationally.

Mr McKenna—I think what we are really suggesting though is that we should make the system attractive for organisations to set up their sites and their Internet businesses based in Australia, so that we have got a larger pool of income on which we can earn tax. If we tax the transactions and all the Internet business goes offshore, we are going to have a shrinking business tax base, so we are going to be losers.

Mr ANTHONY—Following that argument, what is the take-up of Internet throughout, say, South-East Asia?

Mr Kent—It varies considerably. For some people it is hardly available. If you look at Malaysia, for instance, whilst they are bragging about their IT corridor, there is a delay of some six to nine months for the average person to get an Internet connection because it all has to go through—well, the family.

Mr McKenna—The one Internet service provider you mean, Andrew.

Mr Kent—Yes, quite so.

CHAIR—Is that in the mother's name or the father's?

Mr Kent—So that is a clear restriction on it. Hong Kong is going quite well at the moment, but China is obviously held up by a lack of telecommunication infrastructure. So it varies throughout Asia, based on the infrastructure and the form of regulation and the availability.

Mr ANTHONY—So what you are advocating is that we have a window because of our high IT infrastructure here, and, notwithstanding that the US is the leader at the moment and will be for a while, we can perhaps capture some of that market, so it really comes down to whatever is the tax regime we structure here?

Mr Kent—No, it doesn't come down to just the tax regime. The tax regime is one component of it. Certainly we do have a window of opportunity. It is something we should take up on. It would be nice if we had better telecommunication links into Asia. A lot of our main links are actually via the US, so we become almost a satellite to them. I think we should invest in some links out the other side of the country. I think that is actually on the agenda. It is something to consider. But, no, taxation is one of the things. I think we have to get four things right. The tax is probably the one that is hardest to get right.

But the other ones we have to get right are: we have to look at law and order relating to the Internet. Our legal system is clearly ahead of the US in terms of complexity, liability and so forth, so we need to streamline that and to understand that better, and educate people better on the advantages of being in Australia for that reason. On language and culture, Australia is very well placed. We are an English-speaking country. We have a large number of languages within the population that can be handled. We are a developed country. The culture is generally in line with international law and so forth. You don't have to pay bribes in Australia to get things done. Australia is generally a good place to do business.

The third one is tax. We have talked about that. The fourth one is reputation. We have to do something about marketing Australia to the rest of the world. .com.au has to mean something. I think it is a government role to start pushing that. It is going to be, in terms of electronic commerce, the primary brand name for the country. The government should take ownership of that brand name, protect it by appropriate legislation and support, and market it to the rest of the world as, 'This is the place. This is the sort of address you want.' Iceland is doing very well simply on the basis that it has got '.is' and people like that because it is catchy. We can certainly do better than that if .com.au means something. They are the four things we have really got to get right. We can't just sit back and expect people to come to Australia if we don't tell them why they should be here.

Mr ANTHONY—The other issue, transfer pricing, happened predominantly through the 1950s and the 1960s and it is happening now with some of our northern neighbours, who own most of the abattoirs and everything else here. If we follow that path, there are obviously advantages. No-one is disputing that. Will we just be setting ourselves up for many of these companies then to even have a greater transfer of pricing because of the medium they can operate in?

Mr Kent—Transfer pricing is an issue that was raised by the US treasury in their white paper, particularly transfer pricing of services. It is certainly a difficult problem in things where you don't know quite what you are transferring. If you look at copyright, which is really the international transfer of ideas and intellect, copyright is tariff-free throughout the world, in terms of that as a sort of predecessor. The other thing is that the value of an idea or its ilk, unless it is actually translated into royalties, is an extremely difficult thing to put a value on. How much do you value a good idea?

So in terms of transfer pricing of ideas and intellectual property, it is a very difficult thing to do, and I don't think we are going to be seeing that for some time. I think in terms of the transfer pricing elements on some of these things, the first ones which are going to be aggressively attacked by government in terms of positioning throughout the world I think will be gambling, No. 1. If you can get a very low rate on international gambling, then that is going to provide some incentive for people to set up their site here because there is no reason they would set it up anywhere else. But it is going to be a very cutthroat business trying to attract some of those things to Australia. We have to take a longer-term position on them.

Mr McKenna—If I could try and interpret that, what you are saying is that the value of intellectual property is the royalty or the income stream that is earned from that intellectual property, and where that income is earned is usually reasonably easy to determine.

Mr Kent—Where it becomes a problem is when you get organisations, for instance, like the big six, which are in most countries, and there is no reason why the big six can't get their Indian partners to do certain parts of the work and the Canadians to do some other parts and some Australians to do some other parts, bundle that together and sell it to the client. It is going to be very difficult for any government to actually determine the value of the various components which were done if that contract is done on a fixed-price basis, unless you start looking at internal transfers. So for international organisations transferring intellectual property, it is going to be extremely difficult. Let's say Australia designs a car which is then manufactured, et cetera, in the US. What is the transfer price on that design? Those sort of issues are almost impossible to actually track.

Senator WATSON—No doubt you have seen the ATO paper Tax and the Internet.

Would you like to comment on that?

Mr Kent—I think I have got it with me. We have actually made a comment on that to them.

Senator WATSON—Would it be possible to share that comment with us?

Mr Kent—Certainly. We are disappointed with the tax office's approach. Not so much on their neutrality; we think that is the right approach. It is not so much on what they think should be taxed and shouldn't be taxed. It is more on their approach on making sure that the tax is paid. We think it is going to scare people off. We think business is going to go offshore because of it. There are a number of things in their recommendations that the tax office is putting their hand up to do themselves which we think would be better done by other people.

Senator WATSON—Such as?

Mr Kent—Such as authentication. I'm sorry, I would like to look at it. What I would probably prefer to do is to provide you with our response to their proposal.

Senator WATSON—That would be good, yes.

Mr Kent—We have got that written down.

CHAIR—We would appreciate that very much. Thank you.

Mr Kent—So we have got that. I will do that on the detail. But the main problem we had was their focus on making sure they captured the black economy in its entirety. We think that that is going to push a lot of legitimate business offshore, and that is our concern with their approach. As to what they think should and shouldn't be taxed, they are fairly much in line with the US. They haven't actually clarified their position on things being delivered digitally, so, for instance, anything you receive down the line the US has said should be tariff-free. It makes a lot of sense for them as a major exporter of entertainment and software, but Australia is a major creator of the same thing. While we are not as big as the US, there is no reason why we shouldn't take a similar line to those.

Also from an international point of view, the original position put in the US white paper would require a major change to international accounting standards and international copyright law. By saying it is tariff-free, it requires no change to either of those two. So IFAC, the International Federation of Accountants, is very much in favour of President Clinton's approach to that.

The Australian Tax Office is not clear on their position on that. It would be good if they were a little clearer. But our main problem with it is the methods they intend to use, or the recommendations made on the methods they intend to use to go about ensuring that all the tax is paid, and that everyone who is participating can be identified and so forth. They are very much pursuing a black economy, and we think that it will push people offshore.

Senator WATSON—Is there a possibility that we should be pursuing the avenue of international tax agreements containing provisions for the taxing of Internet transactions? Is that the way we should go? Or should we use some other route? Obviously we have got to have some sort of international protocol or arrangements to capture this revenue somewhere along the line.

Mr Kent—Once again, in terms of tax and most of the other things, the Internet is merely another method of doing business. If we relate them back to traditional forms of business, then most of our existing tax arrangements are sufficient. The issue actually becomes getting some authentication as to who the participants were, to getting some clarification as to what was actually transacted. Existing law says that if you are earning income from whatever the source you have to keep track of the transactions. So most of the existing law already copes with all that stuff. What it doesn't cope with is how you are identifying who you are actually trading with. That is an authentication problem, and it is a problem that most businesses want solved anyway. The tax office is not alone in wanting to know who it is dealing with.

Senator WATSON—So they should be dealing with existing law rather than international agreements?

Mr Kent—Authentication is a bigger problem than just for the tax office. Everyone wants to know who they are dealing with.

Senator WATSON—Yes, that is right.

Mr Kent—Authentication is being addressed by a number of people. I guess our general feeling on it is that people want to give the tax office as little information as they possibly can, but they are quite happy to give other people, trusted third parties, information. So, for instance, people are more prepared to give credit card companies information about who they are and where they are dealing from and so forth than perhaps to the tax office, because they think it is perhaps more in their interests to do so. Similarly, they are quite happy to tell Australia Post where they live, et cetera, and Australia Post has stepped forward in Australia on authentication, and the AICPA have stepped forward in the US on organisational authentication.

All we are saying is, let the authentication be dealt with by someone other than the tax office, because we think that issue can be resolved, and let the tax office use those forms of authentication rather than scare people away. That is just one of the issues. But we will give you the response. The general thing is they are chasing the black economy in trying to ensure that we lose no money to the Internet, and we think that they have gone too far.

Mr McKenna—There is a risk of shrinking the cake rather than growing the cake, and I suspect it is a case of having a bit of a loss of a large cake, or no loss from a very small cake.

Mr Kent—Yes.

Mr BEDDALL—We have received some evidence about the EEU's proposal—which seems to be typically European—to charge the frequency of the transaction, like the gigahertz or whatever.

Mr Kent—Do you mean they are looking at taxing it?

Mr BEDDALL—Could we be that lucky that they would do something like that?

Mr Kent—They are not all in agreement. The one that is closest to going through is e-mail tax, but already there are a number of Internet solutions to getting around that, which is again, I think, why any form of tax needs to be well away from the technology. We need to get back to the business and say, 'Okay, this is the business unit, this is the form of income.'

Mr BEDDALL—Yes.

Mr Kent—So with taxing e-mail, there is already a loophole, you can already get around it.

Senator WATSON—In terms of authentication you suggest it should go off to independent providers. Should we provide the tax office with the means whereby the can get access generally or specifically to these information providers in the authentication process?

Mr Kent—Certainly they have got access to a number of these things through their stand on things now. If you get audited for tax you have to show all your transactions in detail, whether you are a milk bar or whether you are BHP. That same principle applies to an Internet provider. They have to show all their transactions. It is part of the law. So why introduce something new? Why scare people off by introducing a new form?

Senator WATSON—You think the existing laws are quite adequate in terms of authentication by the people who use the Internet?

Mr Kent—The existing laws are sufficient in terms of the onus being on the business to say what transactions occurred and with whom. I think those laws are sufficient. I don't think we need to introduce anything new.

Mr McKenna—So really if we have got a situation where a law-abiding citizen is doing the right thing in determining who they are dealing with, and are prepared to make that information available as required by the current legislation, for the tax investigation powers and so on, that should be fine, and we shouldn't probably confuse that any further. I think we should then possibly have a slightly stronger approach to those people who are not necessarily law-abiding, and put the resources into chasing the crooks rather than making it difficult for all the honest people.

Senator WATSON—But we have got to have legislation that enables you to chase the crooks across the world. That is the problem.

Mr McKenna—That then gets into the arrangements you have internationally, and I suspect with the general globalisation of business that is becoming an issue that is being addressed. We have been working for 20 or 25 years to try to get an international set of accounting standards where there is commonality across the world. I suspect the Internet will be a driver for tax authorities to talk more internationally. I suspect there will also be a move in the corporate regulation area in the same direction.

Getting outside of all of that, the environment is an area on which there has to be international agreement, because if someone pollutes in one country—Indonesia sets their forests afire and it pollutes the whole of the Malay Peninsula—it is an international problem, it is not simply a national responsibility. So there has got to be a lot more international cooperation and coordination of activity.

CHAIR—I will change the direction slightly. One of the issues that we have now got to come to grips with is the $50 duty, excise and wholesale sales tax concession on goods entering Australia under a single order. The Australian Fishing Tackle Association do say that their industry has already been materially harmed. Coles Myer this morning said that their industry is being harmed—the retail industry in general—and predicts doom and gloom. And you predict in your submission to us that on-line catalogues is the fastest growing market segment on the Internet. We would like to know your view of the $50 screen-free limit, the effect of the Internet with respect to that, and commercial trade in Australia generally.

Mr Kent—Do you want it specifically on the $50 screen-free limit?

CHAIR—Yes, should we raise it, lower it, or eliminate it?

Mr McKenna—Why was it put in place for the first place? Probably for administrative ease and it wasn't worth chasing the tax and the revenue that you are going to collect on transactions under $50.

CHAIR—Well, we don't know. We suspect so.

Mr BEDDALL—Absolutely right.

CHAIR—And Australia Post and Customs both tell us that it costs a fortune to police these things, in both paperwork, loss of time, loss of opportunity, and personnel—the whole box and dice.

Mr McKenna—What are we trying to fix by addressing this problem? You can say, 'Leave it as it is, we hear the fishing tackle people.' We have been aware for some time that they have got a problem, and the retailers have got a potential problem. I would suggest the solution for the retailers and the fishing tackle industry is to become an Internet provider, and sell, rather than fiddle with the system.

Mr BEDDALL—But they don't manufacture.

Mr McKenna—But they can still trade.

Mr Kent—The value a retailer adds to the chain is to provide a relationship with a customer where the customer is happy with the retailer. We as a professional body are becoming a retailer to our members because we have a good relationship with them.

Mr ANTHONY—But what they argue is that, with the sales taxes, or the wholesale taxes and everything else, they can't compete.

Mr Kent—Again it is a problem with Australia's tax system being out of sync with the rest of the world.

Mr ANTHONY—It is back to that problem.

Mr BEDDALL—With the United States.

Mr Kent—If Australia is concentrating on the transaction side of it, Australia is concentrating on wholesale tax. It is basically a hidden tax. Most people don't know they are paying a transaction tax. The rest of the world has a sales tax. If those things are out of sync it is very bad for Australia.

CHAIR—If we bring in a GST, one heck of a lot of your members' clients, who today provide services, are going to be paying a services tax. When their services come under attack over the Internet, does that then make them less competitive with overseas firms?

Mr McKenna—As I understand GST, they wouldn't be paying a GST on exported product or services, but they would be paying tax on the income they earned.

CHAIR—Yes, because at the moment the majority of on-line trade, goods and services, on the Internet is sourced out of the United States. That is correct? We all agree on that?

Mr McKenna—Yes.

CHAIR—Then they have an advantage, and so they are coming in now at prices, whether competitive or not, with onshore firms who wouldn't have a clue, but if we impose now a GST on those firms, are you going to come back to us in a year's time and say, 'Look, you made our service industry uncompetitive because of Internet trade, where we didn't have a tax before and now we do in terms of domestic sales and services competing with incoming Internet services'?

Mr McKenna—You are talking about the under $50 stuff, really, because the rest of it should be caught.

CHAIR—No, not with services.

Mr Kent—You are asking, will a GST impact on our ability to export over the Internet?

CHAIR—That is not the question. Will it impact on our domestic service industry being able to compete with overseas firms through Internet transactions?

Mr BEDDALL—Your package to your client base will carry 12½ per cent GST—

CHAIR—Or 10 or seven.

Mr BEDDALL—Whatever—but your package sold out of the US, your own package, won't. Aren't you therefore uncompetitive because of the domestic tax arrangement that comes in?

Mr Kent—There is more to the cost structure than simply tax. You are saying it is wearing more tax coming out of Australia than in the US. The thing is still going to get here.

Mr BEDDALL—I am talking about a downloadable accountancy package that you can put in the computer. You can sell it out of the US, just as you can out of Australia. It can be located in the US, loaded onto the computer system in the US. Sell it to me in Australia and, because it is an export out of the US, no tax is payable. You try to sell it in Australia from Melbourne to Brisbane and a 10 or 12 per cent GST is payable. Doesn't that then immediately put an impost on the Australian industry? It is the same package.

CHAIR—That is the point I was making. That is the question I was asking.

Mr BEDDALL—Because these things are moveable. It is software that is moveable.

CHAIR—Are you going to come back to us in a year's time and say, 'You've made the accounting industry uncompetitive because of the Internet'?

Mr Kent—Are you going to put GST on every single item?

Mr BEDDALL—Yes.

CHAIR—Yes. Well, this is a hypothetical question.

Mr BEDDALL—It is a financial service. You would have to.

CHAIR—No, whether Australia has a GST to replace the wholesale sales tax is a hypothetical question. Let's say it is at 10 per cent. As my colleague David says, there is no tax on that accounting package today, so you are competing on an equal basis with the Yanks. Tomorrow you have got a 10 per cent GST, the Yanks have zero rated export but they don't have GST anyway, and all of a sudden you become 10 per cent less competitive. Are you going to come screaming, 'You've made us less competitive because of the Internet'?

Mr Kent—There are a couple of issues on that. I don't think we will come screaming. The first is that surely something created in Australia for Australians should have some value added to it? If you look at accounting packages, which is the example you have given, there are 300 accounting packages in the Australian marketplace. Only about 50 of those were actually created in Australia. Most of the really cheap accounting packages come in from overseas, because they have a higher market size and therefore can be sold at a lower unit cost. Australian accounting packages still compete because they are made for Australia and they suit Australian conditions, so there should be some value adding in that side of it.

If an Australian company such as Attaché, one of the more famous accounting software products, says, 'Okay, we're going to do all the development in Australia and then sell it off a server out of the US'—which is an example you gave—'so that we don't have to pay GST,' the income stream still comes back to Australia, but there is a lack of tax revenue for the tax office. So if you are looking at international competition in terms of how are Australian products going to compete with overseas products, they need to be adding some sort of local add-on value in order to be doing that.

The other point is, are you going to actually put a GST on the types of goods that come in electronically? Are you going to put a GST on everything, or are you actually going to just say, ‘All right, we’re going to take these hidden wholesale taxes, look at where they currently exist, and just move them up the chain a bit and call them sales taxes.’

Mr BEDDALL—It is called a goods and services tax. The argument for a GST is that there is almost no exemption, and that it applies to services.

Mr Kent—I know that is the argument for it.

Mr BEDDALL—All the accountant groups have been arguing for it. Your association argues for it.

Mr McKenna—We have argued for a broadly based consumption tax, not necessarily a GST.

Mr BEDDALL—Call it that or whatever you want to call it. Call it a retail tax.

Mr Kent—A retail tax?

Mr BEDDALL—It is the same thing.

Mr Kent—A retail tax is slightly different.

Mr BEDDALL—It is a point-of-sale tax, not a sales tax.

Mr Kent—But if you simply looked at where wholesale tax currently exists and shifted it up the chain and called it a sales tax, then what threat are you actually causing to the industry? You are actually making exporters more competitive.

Mr BEDDALL—Yes. We are not arguing that.

CHAIR—But you do understand the question I was asking you?

Mr Kent—Yes, I understand. The point is, Attaché might well like to sell their software out of the US back to here if there is no sales tax on it.

Mr BEDDALL—That will make them internationally competitive.

CHAIR—If you extended that argument, if we adopted a GST or a VAT, or whatever you want to call it, which then puts us in line with the whole of the rest of the developed world except for the United States, then basically the whole world, if the tax was high enough, ought to be moving all of their operations to the United States.

Mr BEDDALL—Why do you think Bill Clinton thinks it’s a great idea?

CHAIR—So we all move to the States, do we?

Mr BEDDALL—Or the Cayman Islands.

Senator WATSON—Isn't it true, though, while we might talk about this global village, in terms of indirect taxes they are essentially a developed world or a European model? The area that we operate in doesn't have too many indirect taxes or GSTs or, if they are there, they are very low. This is the problem that we face.

Mr McKenna—Singapore has one of three per cent or something.

Senator WATSON—Yes. It is no use having 12 or 15 per cent if Singapore, Japan and the rest of the world are going to have three or four per cent. That is where the business will be done. That is where it will come out of.

Mr Kent—Transaction taxes, whether they are wholesale or sales tax, have a negative impact on international competitiveness for each individual transaction.

Senator WATSON—What I am saying, though, is that it would be bad if we fell in with the practices in Europe, because that is not our area of competition. Our area of competition is coming from the north.

Mr McKenna—And our potential market.

Senator WATSON—Yes.

CHAIR—You said Australian taxes are not competitive with respect to the Internet, or something like that. Can you tell us which ones?

Mr Kent—It is largely looking at the wholesale tax.

CHAIR—The other thing you said when talking about on-line catalogues, which I thought was absolutely fascinating, was this:

Taking the high level of economic activity and employment associated with the retail sector this—

on-line catalogues on the Internet—

represents a potentially catastrophic economic and social upheaval.

Could you expand on that, please.

Mr Kent—Sure. I can actually give you an article on that one. It will take a while, but it is basically a comparison with what happened with the change in the transport industry, moving from horse and cart to car, which took 40 years and resulted in a Depression, and looking at the figures on that. Again, I will provide you with the article on this. At the moment the default employer of people, young people particularly, is the retail industry. If you look back to the turn of the century, it was agriculture. When you change the way that retail sector works, and you start saying that for most commodities you don't actually need a store or a shop assistant, therefore you don't need a building and you don't need to transport people to the building and so forth, what we are looking at is a major shift in where people are employed and how they are employed.

The other major part of that is that whilst the retail sector and the amount of goods sold retail will remain pretty much the same because people are still going to want the same amount of goods, the people involved in that process will change dramatically, and the people who are currently involved in that process may not necessarily be able to transfer over to the new one. For instance, someone who is very good with horses does not necessarily make a good mechanic. The same thing applies to retail. Someone who is very good on the shop floor may not necessarily be very good at electronic retailing and is not necessarily able to transfer that skill set across.

So the background to that statement you refer to as fascinating is that the end result of this—and we are not saying it is going to happen in two years or whatever; I would say it is probably going to happen in half the time the transport change did, which is about 20 years—is that you are looking at a major shift in how people are employed and where they are employed and what skill sets they require. This is not a problem just for Australia. If this happens, if this thing goes this way, then we have got a major and fundamental change to the economic structure of the country. That is what that is about.

CHAIR—Is that in your view—and using your word 'catastrophic'—why people like the Fishing Tackle Association and Coles Myer want to put the shutters back up again?

Mr Kent—It is a similar reaction.

Mr McKenna—The red flag and the bell in front of the motor car.

Mr Kent—Yes.

Mr BEDDALL—No, that is not fair or true. What they are saying is, if I buy a good from overseas through the Internet, I should pay the same tax as is paid if I buy it in Australia, or we should abolish the taxes in Australia so that it is a level playing field. I think that is a more accurate reflection of what they are saying.

Mr McKenna—Yes, that is legitimate. We have got to be internationally competitive.

Mr BEDDALL—Yes. You are giving a competitive advantage to the overseas supplier, which you can't do if you want to remain competitive.

CHAIR—Except they don't have to pay for freight.

Mr BEDDALL—Yes, they do. They import the shirts.

CHAIR—Not necessarily.

Mr BEDDALL—Your shirt came from China.

Mr ANTHONY—Have you done any projections of what you see down the track happening in retail sales or the shift in employment demographics?

Mr Kent—One of the recommendations we put in the paper was that some work should be done. If someone had done some work around the turn of the century as to what was going to happen when you took away the horse and cart and all the support infrastructure around that and replaced it with tractors and motor cars and so forth, and said, 'Okay, this is where the skills shift is going. This is where the new industry is,' then whichever country had done that would have had, firstly, a much gentler Depression and, secondly, would have been well placed to make the most of that. All we are really saying is this is the long-term outcome of this shift in economic activity. Let's have a look at it. Let's get the country organised for it before it happens, rather than have a lot of pain and suffering a little bit further down the track.

Mr McKenna—So really you are calling for some fairly serious scenario planning?

Mr Kent—Yes.

Mr BEDDALL—Taking the retail sector as a classic example, the reality is that 20 years ago it was a very different sector to what it is today. Predominantly now retail is destination shopping, enclosed malls, et cetera, whereas 20 years ago it was strip shopping centres and major capital cities. I think you are probably right that it may not even take 20 years. It is not necessarily my generation or even your generation, it is the one that is 10 years old now. In 10 or 20 years time this will just be second nature. They will grow up with it to such an extent that they won't even question the technology.

Mr ANTHONY—Are there any key recommendations in the Goldsworthy and Wardle reports that you would want to bring to the attention of this group?

Mr Kent—We are supportive of the general principle and general thrust of the

Goldsworthy report. I am not actually familiar with Wardle, I'm sorry. There is nothing I would particularly like to raise on that.

CHAIR—I have one last question if my colleagues are all done. In talking about on-line catalogues again—and you said you have made such a recommendation—you say:

The government should commence work immediately on understanding and predicting the likely nature and timing of this change.

You are talking about the horse and cart and all of that. Why the government? Why not the retail sector? Why on earth is it the government's responsibility to determine what is going to happen in the marketplace?

Mr Kent—If everyone ends up on the unemployment line, the government is going to pay the bill, the government is going to be the one looking after the social upheaval and the government is going to be the one that has to address most of the problems. The actual retail owners are simply going to change the method by which they do it. They are going to set up a Web site instead of setting up another store in Chadstone. So the retail sector is not going to be the one that feels the pain. It is going to be the actual citizens of Australia, and the government who pays the bill, so we think it should be the government.

CHAIR—You also say:

The government should also provide advice and financial assistance to exporters who utilise the Internet as a means of supporting and extending their overseas markets.

What are we proposing here? Do we want to go back to government running business and enterprise again?

Mr Kent—No. It is more that this is an embryonic industry and some governments throughout the world are providing support for new players in the industry.

Mr ANTHONY—Can you give us some examples?

Mr Kent—Malaysia is an example, where they are throwing quite a lot of money at—

Mr ANTHONY—Even though it takes you six months to get on.

Mr Kent—Well, that is for the individual Malaysian citizen. There are different ways of doing business in Malaysia.

Mr BEDDALL—But closer to Australia's ethnic roots, Wales and the Republic of Ireland are also doing a lot of this.

Mr Kent—Yes, there are quite a few. India is making rapid advances in this area. They have got some advantages Australia doesn't have, in terms of the amount they have to pay people employed in this sector. I think Australia needs to think about being well positioned in this. It has got a window of opportunity and it has to make the most of it. That might require some government assistance.

CHAIR—Are you aware of any US government assistance to Bill Gates?

Mr McKenna—Probably the opposite actually!

Mr Kent—It depends whether you consider US government departments buying Bill Gates's product as assistance or not.

CHAIR—No, when he started.

Mr Kent—When he started, no, but IBM gave him a good deal of assistance.

Mr McKenna—I think fundamentally our broader principle is that government should help to create the environment where business can get on and do what it has to do, rather than trying to pick winners and so on. That's the broad philosophical approach that we would take. I think the word 'assistance' is probably more to make sure that we have in fact got the environment right for business to get on with business, and we don't want any impediments in the way.

Senator WATSON—In terms of 2.1.7 of your submission, Global servicing, I see a possible loophole that you could unintentionally create when you say:

The ASCPA does not think that [it] is appropriate to attempt to introduce transfer pricing on service elements.

When you go on and give your examples, I can see 'transfer of ideas, or intellectual input', but if you are just talking about service elements it can give rise to a situation where there can be a lot of international input in terms of giving opinion and providing interpretation of the law and interpretation of accounting, et cetera, which would escape tax scrutiny if it could be argued that we shouldn't have a transfer pricing arrangement on service elements, because the Internet could be a very useful medium for such a transfer.

Mr Kent—True, but you have to look at how practical it is to do anything about that.

Senator WATSON—It is the service area which is the area of greatest growth. One of the reasons why we are having a loss of some tax revenue areas is because people are utilising services more—knowledge is power, et cetera—and these are the growth areas. If we are going to keep these elements free of the taxation net collection mechanism, then we are going to limit our powers quite severely.

Mr Kent—Again, it comes back to a balance between income taxing and transaction taxing. Australia at the moment is a major exporter of consultants, of intellectual capital in that capacity. Those consultants earn income. Income is taxed, generally in Australia, because that is where the Australians are resident and that is where they are, so it depends on where you're trying to capture this.

Senator WATSON—But if you are going to have Singapore and Malaysia essentially providing the information, where the transaction comes from—they write to their contacts in Malaysia or Singapore, the information comes from Singapore, et cetera, but essentially the conduit is indirectly through Australia—then there is a major problem and there is a loss of jobs. Obviously, Australians can go and work in Singapore, that is true, but the taxation revenue is not picked up, because obviously if they work there six months or more, we don't get too much of it at all, because it's taxed in Singapore.

Mr McKenna—If you look at that in the broader context, though, Senator, Australia is an attractive place to live and work.

Senator WATSON—That's right.

Mr McKenna—People are going to want to do that.

Senator WATSON—Yes.

Mr McKenna—If we taxed the income where in fact it is earned, à la the residence, are the people who are providing the service or—

Senator WATSON—Yes, but that is Singapore, because that is where the opinion comes from.

Mr McKenna—The opinion might come from Singapore, but if it is delivered to an Australian through an Australian medium, the Australian medium—

Senator WATSON—No, not necessarily. It is very hard to prove.

Mr Kent—What scenario are you concerned about?

Mr McKenna—You mean if I want legal advice, I go to the Singapore office of my Melbourne legal adviser and get the advice there?

Senator WATSON—You could have it once removed quite easily.

Mr McKenna—But it is very hard to get legal advice over the telephone. You like to do it face to face and understand things.

Senator WATSON—You might actually do that in Australia, but the final opinion gets telegraphed to Singapore, and that is on the Singapore letterhead.

Mr Kent—But again you are looking at taxing the transaction. What we are saying is for most intellectual capital type things—royalty, be it whatever—that ends up with an individual or an entity and is taxed as income.

Senator WATSON—Yes. I am not talking about the examples you give, but when you are talking about taxing services, there should not be transfer pricing on services. I think you are opening up a minefield for tax avoidance, which would put a lot of transactions offshore.

Mr Kent—I guess our view is that if you tighten this net too closely, people will go offshore to avoid the tight net, and we would rather have a larger slice of the cake than catch all of the crumbs.

CHAIR—Gentlemen, thank you very much for attending and for your prompt answers. We hope to finish our inquiry by next April or May or June. We will certainly send you a copy.

Resolved:

That additional submission by the Australian Society of CPAs dated 14 November 1997 be accepted as evidence and authorised for publication.

CHAIR—Is it the wish of the committee the document entitled Flow chart—incoming international parcels, and presented by Australia Post, be taken as evidence and included in the committee's records as an exhibit? There being no objection, it is so ordered.

Luncheon adjournment

[1.20 p.m.]

STOLAREK, Mr Anthony, Managing Director, Tax Competence, Arthur Andersen, 360 Elizabeth Street, Melbourne, Victoria

WALSH, Mr Damian, Partner, National Head of Indirect Taxes, Arthur Andersen, 141 Walker Street, North Sydney, New South Wales

CHAIR—I now welcome representatives of Arthur Andersen to today's hearings. Thank you, gentlemen. Would you each in turn state your full name and the capacity in which you appear before the committee for the purposes of Hansard.

Mr Walsh—Thank you, gentlemen. My name is Damian Walsh. I am a partner with the firm of Arthur Andersen. I am a tax specialist, but I am also the head of our information technology and telecommunications focus group for the firm.

Mr Stolarek—My name is Tony Stolarek. My title is Managing Director, Tax Competence, and my capacity is in my role as distributor of tax technical material within Australia, and locater of tax developments around the world.

CHAIR—Thank you very much, gentlemen. Thank you for your submission. Would you like to make a brief opening statement before we ask you questions about your submission and other issues.

Mr Walsh—Thank you, sir. I am sure that much of what we have to say you will have heard before. They are fairly common themes in the business community, about the development of electronic commerce, and the implications of electronic commerce for the tax system in particular. Needless to say, I will repeat that electronic commerce is obviously still in its infancy, particularly the Internet developments. We really regard electronic commerce as the current stage in the development of how we do business, locally, nationally, and globally. It is simply an evolution in the way we do business, via the telephone, the fax machine, and the telex machine before the fax machine, and now the Internet is simply a further stage in the evolution.

There is no current evidence, as far as we can see, that electronic commerce is a threat to the revenue currently. Indeed, there is no evidence that electronic commerce will in fact be a threat to the revenue. We therefore have a fairly simple message that we are trying to deliver through our submission and through our presentation today, and that is, don't rush. Electronic commerce is in its infancy. There is no evidence that the tax system is under threat at the moment. Let's not jump at perceived threats by introducing ill-conceived legislation or regulatory restrictions that may have the effect of either constraining the development of this very important aspect of how we do business as we move forward or, alternatively, creating problems that are not yet perceived.

Secondly, I would like to say that I think we should make every endeavour at this stage of the proceedings to try to identify what the real issues are. Let me give you the simplistic example here. It is the example that comes up time and time again. Music CDs get ordered over the Internet. It seems to be the flavour of the month. If sales tax does not get paid on the music CDs that are ordered over the Internet, it has nothing to do with any failure in the sales tax legislation. It is purely an administration problem. If the Australian Taxation Office, Australia Post and the customs department cannot deal with small transactions, it is an administration problem, not a problem in the legislation. It does not require a legislative response. It requires an administrative response. I just put that forward. It is the oft-cited example of the sorts of revenue erosion that will come from an expansion in the use of the Internet to do business.

Let's find the real issues. Let's focus on the real issues and deal with them. That is a theme that we need to adopt across the board. Any measures that we do feel are necessary must be designed so that they don't constrain the evolution of electronic commerce. Importantly, let's not constrain electronic commerce with ill-conceived regulation or punitive tax measures. Let's be consistent as between the regulatory bodies, and that is not only in Australia, but internationally, of course, and not just tax, but other involved regulatory bodies need to sit down, understand what their respective concerns might be.

We need to meet electronic commerce with a common response. We also need to win consensus with the governments of our major trading partners, such that we don't end up making Australia the least favourable place in the world to do electronic business. And let's not be opportunistic. Let's not use the evolution of electronic commerce, let's not use the current debate about the tax measures that are required to deal with electronic commerce, as an opportunity to introduce other measures that have nothing to do with electronic commerce, and that will have far-reaching tax implications.

By way of an example, let me cite the tax office's recommendation in its report on tax and the Internet, for example, the current exemption known as the tax advantage computer programs exemption, which effectively exempts computer software from sales tax. The tax office has recommended in its report that that exemption be removed. That has nothing to do with electronic commerce. It has nothing to do with the electronic commerce debate. Simply because it is about software doesn't mean that it is about electronic commerce. It is not. It is simply an exemption that is in the sales tax legislation. It has been there since December 1988. Whether it goes or not requires a government policy decision, but not under the guise of electronic commerce. I cite that merely as an example again.

Let's not be opportunistic. Let's not introduce changes to the tax system that will have far-reaching impact and that may have little or perhaps even nothing to do with electronic commerce. There are other examples in the area of sourcing of revenue, international tax rules and so on, that have exactly the same implications. In addition, any tax changes that are introduced to deal with electronic commerce must be neutral as between the way we do business. If buying and selling goods through the normal distribution channels is taxed in a certain way, buying and selling goods over the Internet should not be taxed in any different way.

We are quite satisfied that the existing tax structure is adequate to deal with most of the concerns about electronic commerce, and we would suggest that if measures are necessary after the appropriate consultation takes place, it is really a question of refining the taxation rules rather than redefining them. Thank you.

CHAIR—Thank you for that. In the course of your discussions, you said that the existing tax base is not really impacted by Internet commerce. I would advise you that the Australian Fishing Tackle Industry Association—and I am sure that you audit and/or provide accounting services to some or many of their members—and Coles Myer—and I don't know if they are on your list of companies or not—yes, they are.

Mr Walsh—Yes.

CHAIR—Both of them expressed great concern that increase in purchasing through the Internet would cause erosion of their retail businesses in Australia by virtue of the taxation concession, the $50 screen-free limit on duty, wholesale sales tax and excise, for goods entering Australia. They suggest if that is not revised downward, they will suffer very great harm to their businesses. I would appreciate your comments.

Mr Walsh—Again, it is an administration issue. I would agree that if many people start to order small quantities of goods over the Internet, then it is quite possible that that will have some marked impact on Australian retailers, but in terms of tax revenue there is no erosion of the tax base, except that those small quantities are allowed to come in for administration purposes free of duties and taxes. It is an administration move to require Customs and the tax office not to deal with small value items.

CHAIR—With respect, it is by statute.

Mr Walsh—In the customs legislation. It is not by statute in the sales tax legislation.

CHAIR—Regulation, or whatever it is.

Mr Walsh—All right, yes.

CHAIR—But still, it requires action by parliament to deal with it.

Mr Walsh—All right. Again, it is a perceived threat. I should make the point here that at this stage we don't know how the volume will increase of this type of business, but

I can order the same goods, and enter into exactly the same transaction over the telephone. I can ring up a supplier in the US or elsewhere and give them my credit card number over the telephone, and some days later I will receive through the mail the CDs, the book, or whatever. I can do the same with a fax machine. So again, I would just make the point that this is not a function of the Internet necessarily, or electronic commerce necessarily. I would accept that telephone and fax machine is also electronic commerce, perhaps, but these are not issues that are restricted to electronic commerce. They are common issues from other means of achieving the same thing.

CHAIR—But if the Internet becomes the direct mechanising catalogue, and that allows greater and greater dispersal of trade by electronic means, you still have no concerns for your companies about the screen-free limit?

Mr Stolarek—Our concern is that the screen-free limit may require adjustment, but we see that as an administrative requirement, and in fact the screen-free limit reduction to a lower level may in fact be facilitated by electronic commerce, so we are in agreement with measures which will assist in protection of the revenue base. These measures may include, for example, international measures to reduce screen-free limits and to put in place standard documentation in an electronic form on parcels and remittances of that nature, and we are totally in agreement with that, but our key proposition, if you will—leaving aside that procedural issue which of course is relevant in revenue terms—is there is not a fundamental impact on our tax system in a design sense that arises out of electronic commerce.

We have seen, all of us, the growth of international catalogue sales, the growth of international facsimile sales, and the growth of international telephone sales that have occurred out of global magazines and global trading. All that electronic commerce does, or Internet commerce does, is increase the volume of those amounts. But, as I say, our proposition is that action on the screen-free limit may be required, but that is fundamentally an administration measure which we don't disagree with. It is not an issue that requires the fundamental redesign of Australia's tax system. That is our point.

CHAIR—Just look at it another way. The biggest problem in that area is not the duty, because on both items the duty is very low, and it is probably not excise to any significant extent. The majority of the problem is undoubtedly wholesale sales tax, and you are saying that there is no structural reason for us to change from our current wholesale sales tax system if the world undertakes more global trading as a result of the Internet.

Mr Walsh—No, I don't think we are saying that at all, with respect. The point we are making is that if there is a change that is required to the screen-free limit of getting goods into the country—

CHAIR—No, I am talking now about wholesale sales tax.

Mr Walsh—Wholesale sales tax is essentially the issue here. Goods are subject to sales tax if they are imported into the country.

CHAIR—But you said there is no structural reason why we need to look at our tax system because of the Internet. If there is increasing trade and we have a wholesale sales tax regime which makes us uncompetitive with other countries, wouldn't that be a cause for looking at change?

Mr Walsh—I can't see the nexus there, and it is certainly not an electronic commerce driven nexus. Our wholesale sales tax system may be undesirable, it may be inefficient, and it may be economically distorting—and I would suggest to you that it is all of those things—but that is nothing to do with the electronic commerce. That exists through ordering goods with a written purchase order, and physical importation and distribution through normal channels. It is not an electronic commerce issue. The only issue here is those very low-value imports that escape the tax because of the administration, be it by regulation or whatever, that allows the goods to come in and not have the rules applied to them.

Mr BEDDALL—Let us take a little quantum leap into the future, but not that far in the future. No doubt Arthur Andersen is part of the great tax debate in Australia, and has a view on what we should be doing. Say the government moves to a broad-based tax of some sort, and abolishes the wholesale sales tax system. All of a sudden such things as services are caught up in the broad-based tax. I am assuming Arthur Andersen provides some sort of software packages, accounting packages to its client base. All of a sudden that is now subject to a 10 per cent, for argument's sake, broad-based consumption tax. The major competitor in electronic commerce is the United States of America, where these sort of taxes won't apply.

Doesn't that then place at a disadvantage the domestic Australian market, in the sense that Arthur Andersen of Florida could sell the package on the Internet to me in Brisbane minus the goods and services tax, whereas if I bought it from Arthur Andersen Melbourne, a goods and services tax would apply? Then this brings about the fact that the tax base, which is now being broadened, actually becomes narrower.

Mr Walsh—This is somewhat hypothetical of course, because we haven't seen the design of the chosen Internet tax base—

Mr BEDDALL—Let us go back to John Hewson's model then.

Mr Walsh—Okay. Most VAT regimes globally will pick up, either by a reverse charge or by some other imposition, exactly the effect that you would pay the GST or the value-added tax or the broad-based consumption tax on the services when they are acquired, and in addition to that it really doesn't matter anyway unless you are selling those services to an exempt customer, such as a bank. But any business is going to on-charge GST on its sales, and if it doesn't get an input credit for something that is purchased, then that doesn't offset the liability that it has. So the answer is that, no, it is not likely to have an effect at all, either because the exempt customer is going to be required to essentially charge itself GST on the acquisition of the software package from Arthur Andersen Florida, as in your example—

Mr BEDDALL—All the movement on the Internet on the taxing regime is at source, where it is generated from, and that would be generated in Florida. Why would a foreign-based supplier charge Australian GST?

Mr Walsh—They won't.

Mr BEDDALL—Yes, that's my point.

Mr Walsh—They won't, but the Australian business will charge—an Australian business will effectively not escape any GST liability.

Mr BEDDALL—I am unclear on this. If I bought the computer software package which I downloaded on my PC—

Mr Walsh—Into your business?

Mr BEDDALL—Whatever. I buy an accounting package, and I buy it on the Internet. Where do I pay the tax?

Mr Walsh—When you sell your services you will charge GST on the full value of your services to your customer. You will get an input credit for all of the GST you have paid on import.

CHAIR—But he hasn't paid any.

Mr BEDDALL—I haven't paid any.

Mr Walsh—If you haven't paid any, then you get no credit for it, so you're paying full GST on your output. A value-added tax ultimately only taxes the final value of the goods, because it is a flow-through. It is a multi-stage tax. Every input becomes a credit.

Mr BEDDALL—Yes, but if I have got a thousand clients and it has cost me $200, I mean it is a pretty broad spread that I am not recovering, isn't it? The revenue is still forgone.

Mr Walsh—No, it is not forgone. It is not forgone at all, not under a value-added tax regime. The revenue will not be forgone. It will simply mean that you won't have an offsetting credit to offset against your output. The revenue is not forgone. I could illustrate it for you on a board if you wanted to see it.

CHAIR—Can I put it to you another way. I am an individual and I decide to buy, for my own household purposes, an accounting package. Today if I buy that from you, I don't pay any tax.

Mr Walsh—That is right.

CHAIR—If I buy it from the US I don't pay any tax. If I buy it from England or Germany I don't, because exports are zero rated.

Mr Walsh—That is right.

CHAIR—Now, tomorrow you—Arthur Andersen—are competing over the Internet. Where today there are tax-free bases everywhere; tomorrow you have to pay a GST, or your client does, for that package, whereas I can buy it over the Internet without any GST, because it comes in zero rated. Are you clients going to be happy about the imposition of a services tax? Will it make them less competitive?

Mr Walsh—I don't know that that is the issue, again with respect. Every other jurisdiction that has a GST faces this at the moment. If we have a GST—and at the moment it is at best hypothetical, and at best the lead time is probably another 2½ to three years before it is actually going to be implemented—we can build in the necessary design functions to make sure that there is not the revenue leak.

CHAIR—It is not revenue leak. It is the fact that it will make us as uncompetitive as the Europeans versus, say, the Americans.

Mr Walsh—Arthur Andersen doesn't have any competitive problem in Europe. Europe has a value-added tax regime. The United States doesn't. Software can be supplied from the United States to a European customer in exactly the way that you are describing, and it simply doesn't happen. So let us not jump at perceived problems that aren't real, because one of the points that I made is, let us find the real issues. Let us not, with respect, make them up.

Mr BEDDALL—We are not. Let us go to your paper where you say:

Companies often attempt to structure their business in such a way that will allow them to take advantage of the lower rates in Portugal, Germany or Luxembourg.

They are countries that have GSTs, so they are moving to structure their business so that they take advantage of the lower rates.

Mr Walsh—Right.

Mr BEDDALL—So it means, what, we have to set our rate low? Isn't that a function of the tax system, the differential rates?

Mr Walsh—Differential rates is an issue, yes, as are differential income tax rates or corporate tax regimes, as to where companies locate their business around the world. They are design issues in tax systems that go well beyond electronic commerce. The US, state by state, neighbourhood by neighbourhood, have different rates of retail sales tax. They seem to exist just quite fine, thank you very much. But when I lived in New York I could go up to Connecticut and buy clothes without sales tax because children's clothes were free of sales tax in Connecticut. But I did most of my shopping in New York City because it was more convenient.

Mr BEDDALL—That is the point we are trying to get at. It is now going to become—not maybe in the next five or six years, but the next 10 or 20—much more convenient to shop in very different ways, and that will have impact. That is all we are saying. If you can buy internationally at the best possible rate, why wouldn't you do that?

Mr Walsh—At the best possible price?

Mr BEDDALL—Best possible price. What we are saying is, if you have a high tax system in Australia—because we have a social system to support, which our neighbours in the north don't—and we have, no matter what rate of tax it is, higher tax at a higher rate of tax, then the advantage is that tax advantage gives the price advantage, doesn't it?

Mr Walsh—No, it won't, if what you are talking about is the transactions taxes like sales tax or a GST or customs duty, or whatever. And to the extent we are talking about physical goods, they are not going to escape anything unless they fit in underneath some administrative screening level where they just don't get subjected to the law. The legislation itself is not going to have any impact there. As Mr Charles pointed out, though, with services that could be different, if services are going to be acquired over the Internet in some way that whatever we end up with as our new broad-based consumption tax, in some way that it doesn't pick them up.

But as I said before, a value-added tax regime will always pick up ultimately the tax on the gross transaction in Australia, even if the input is not taxed. That is the beauty in fact of a value-added tax style of tax over and above the single stage type of tax; that if you are missed at one level, you get it at another, and you get the whole value, unless you are missed at the very last transaction.

Mr Stolarek—We do support, as we set out in our submission, that reform of Australia's tax system overall is on the agenda and needs to be considered. I think the thrust of our submission is that electronic commerce, while it has relevance, doesn't raise unique issues that are not present elsewhere in our tax system; that is to say, the fact that we support and agree with observations that the Treasury has made that services, in most ways, are not taxed in our system, and so on. So that is all agreed. And our key proposition is that the formation of electronic commerce policies and the impact on the tax system needs to be part of the broader tax reform agenda.

The only issues that electronic commerce raises fundamentally in itself are the small transaction issues, and identification issues. Otherwise, the issues are in common with the development and sophistication of our economy and its internationalisation. Electronic commerce vis-a-vis Cds and fishing tackle raises no different tax issues to a mail order purchase of fishing tackle, to a fax purchase of fishing tackle. That is our proposition.

Mr BEDDALL—I agree. I think the problem that people are concerned about is the quantum of it.

Mr Stolarek—Yes.

Mr BEDDALL—Just looking at the Internet as some sort of electronic catalogue is probably the wrong way to do it. It is a whole new methodology of merchandising.

Mr Stolarek—Yes.

Mr ANTHONY—In your submission you talk about the situation in the United States where naturally the states have different taxing regimes, and what you are saying here is:

There are real issues about the location of electronic commerce activity within the US, and potential exposure to multiple sales tax and, indeed, income taxes.

Could you just elaborate on that to the committee. In the US, which is the home of the Internet, is there a concentration in some states vis-a-vis others? Then you also recommend in the next paragraph that the federal government, as part of the tax debate, tax reform review, should identify customer groups—that is, the participants in electronic commerce—to look at ease of administration. Maybe you could just elaborate on that as well.

Mr Walsh—Dealing with the first issue, Mr Anthony, I think it is too early to tell at this stage whether electronic commerce is really going to be attracted to one US state versus another. Everything is so much in its early stages. There is a perceived threat, and it is picked up in the various seminars and inquiries that we have made, and some of the reports that have been issued in the US, that—much as we were talking before about the current US state-by-state sales tax structure—the state income taxes and state sales and use taxes are difficult to administer where you have cross-border transactions. That is a current issue, and is likely to be exacerbated as electronic commerce grows further.

You will also be aware that in the US there is a thriving mail order or catalogue sales-type business, and it hasn't really ever caught on in Australia. Another issue is, Australia is not actually inclined towards mail order except for novel situations like the Internet. At this stage, I think, Mr Anthony, it is simply too early to determine. We certainly have no evidence that any particular location in the US is being favoured over another location within the US tax structure for the location of Internet centres or Web sites.

Mr ANTHONY—I don't want to labour this point, but it is an important point in your submission and also in your document here at the conference you had at Miami. There are a number of issues but, basically, how does the Commonwealth ensure that we don't have an erosion of our tax base through electronic commerce? These issues must be being grappled with now by state jurisdictions within the US, because of the different regimes they have, which are far greater than in this country.

Mr Walsh—Yes.

Mr ANTHONY—So they are obviously having erosions in a lot of their tax bases, which has been occurring through mail order anyway for a long time, but it is obviously becoming a lot more prevalent there. I am just wondering, through your expertise, what action have some of those state governments been taking to minimise that erosion? In California there is, I think, six per cent VAT now, or whatever. How are they trying to regulate that, or to maintain it, vis-a-vis other states who obviously have a huge advantage, whether it is mail order, or the new frontier, which is electronic commerce?

Mr Walsh—The answer is that I don't know exactly what any one state is doing. I would suggest to you that they are in much the same situation as the rest of the world in trying to grapple with how to deal with electronic commerce under the tax regimes that they have. I am not aware of any specific measures that have been taken in any state in the US at this stage to try and change their state and local tax system to deal specifically with electronic commerce.

Mr ANTHONY—What do you think of what they are doing in Europe now with the tax and these other proposals?

Mr Walsh—My view is that none of that is realistic. I am not absolutely sure, but I think Telstra have given evidence already to this committee, and I suspect that they have suggested that the concept of taxes and so on is really not feasible.

Mr ANTHONY—Yes. I think most of us would concur with that.

Mr BEDDALL—We hope the Europeans implement it.

Mr Walsh—Yes, so we can see how it goes.

Mr Stolarek—I think the key issue arising from this, Mr Anthony, is the need for accelerated interaction and cooperation amongst revenue authorities. We support strongly the fact that Australia, through the tax office, is working in the forum of OECD. As Damian says, we can’t be categoric and encyclopaedic at this stage, but the key issue that has arisen out of the US is that, in the US, the states which have, as you know, a combination of sales tax, use taxes and income taxes, are variously seeing Internet and electronic commerce as an advantage. Some are positioning themselves to in fact reduce their tax regime on electronic commerce. Others are considering revisions of their tax regime, potentially along the lines of use taxes. Others, at this stage, are adopting a neutral position. By and large, no states are acting precipitately yet because of the infancy of the industry.

The major focus internationally has been on cross-border international issues, but we did raise it because we were conscious of the fact that, even in Australia’s tax reform debate, electronic commerce and the impact of cross-borders within this country could potentially become a similar issue to that which arises in the US. But the key issue that we wanted to emphasise is the fact that individual nations and individual states need to consider their competitive position before they rush off and make ill-considered tax measures.

It is significant, I think, that in the US none of the states has come out with a strong array of measures at this stage. They are all in fact cautiously considering what everyone else is doing, and that is notwithstanding this electronic commerce is much more developed in the US, with Compuserv, America On Line, and so on. They are all still cautiously considering how they can act in a coordinated manner.

CHAIR—Some have told us, and we have had some submissions that talk about FID and stamp duty as being impediments to Australia taking up some of these opportunities on line. Would you like to comment on that?

Mr Walsh—I think the answer perhaps, Mr Charles, is that financial institutions duties and stamp duties are an impediment to doing lots of business in Australia, and as between states in Australia where the rates are different. I suspect they will also be an impediment in doing business electronically. But I think, again, they are issues of far broader concern than simply electronic commerce. I think that, to the extent that any tax is an impediment to doing business generally, it will be an impediment to doing electronic business as well.

CHAIR—Every tax is an impediment, isn’t it? Or should we have zero taxes?

Mr Walsh—No, I don’t think that every tax is an impediment. I think that as long as you can achieve tax neutrality and avoid the economic distortions in the tax base, then tax per se shouldn’t be an impediment to doing business.

Mr BEDDALL—We don't trade predominantly with Europe or the United States. We trade predominantly with Asia. You have got a bit here on harmonisation. Seventy per cent of our exports are to the Asian region.

CHAIR—Imports.

Mr BEDDALL—Exports.

CHAIR—Imports from the states.

Mr BEDDALL—Imports, yes, but I am talking about exports. If we are continuing to grow our trade with the Asia Pacific region, and harmonisation becomes an issue because of the movement of electronic commerce—I think we get bogged down a little bit about T-shirts and fishing tackle. I think, from evidence we have had to date, the majority of commerce on the Internet is going to be services rather than goods. Will that put pressure on our tax system to harmonise with the lower tax states of our region?

Mr Walsh—I think, again, the answer is we are suffering considerable pressure because of that at the moment. You have only got to witness the outflow of manufacturing industry to Asia, because of cheaper labour rates, and perhaps cheaper tax regimes as well. Again, I don't think that electronic commerce is going to be any different to that. It is hard to see immediately how the different tax regimes in Asia are going to impact on how business is done electronically. To the extent that you can locate the source of your revenue in a low tax jurisdiction for income tax purposes, and escape any other rules that would bring that revenue back to Australia for taxing purposes, then, yes, you will achieve a tax advantage by locating the business somewhere else. That is the reality now.

If electronic commerce makes it easier to do that, in the sense that you might be able to source your revenue at the source of your Web site, then perhaps it becomes easier to relocate the source of your revenue. It is not an issue that is common to electronic commerce. There is lots of business that is currently done where the income that is generated from that business is sourced outside of Australia.

Mr BEDDALL—I suppose my point is, it is going to be much easier to do it, physically relocating a manufacturing plant, or all those sorts of things. There are a number of things happening like virtual government, and all those sorts of concepts are now being tossed around. I agree with you, we don't have to panic and rush into this, but the way that the parliamentary process works, even if we decide to do something today, it would be five years before anything happened. So it is probably a matter of being a little concerned about the future.

Mr Walsh—Yes, I agree. One of the difficulties we face at the moment, and perhaps why I was just hedging a little bit there, is that some of difficulties we face with the electronic commerce issue, and the Internet and Web sites and so on, is that it is sometimes difficult to actually think of the examples of how you are going to, by simply creating a Web site in some other country, use that effectively to shift the source of your income outside of the country. It is actually not that easy to do. It might be very easy to set up a Web site somewhere, but in terms of shifting the source of income, it is not that easy to do. If the transactions are still going to take place here, if the goods are still going to be stocked in a warehouse down the road here and so on, it is difficult to shift that business, perhaps out of Australia.

Mr BEDDALL—I am thinking of something like say insurance policies. If I send off my trustworthy assistant to live in the Cayman Islands, located my Web site there, used the Royal Bank of the Cayman Islands as my banker, and sold insurance policies by the Web to Australians, underwriting with any major company in the world, then the money would go from Australia to the Bank of the Caymans, and everything would be domiciled there, wouldn't it? Is that a problem? Or does that get caught up somewhere along the line? You are actually dealing in something now that is not a physical good.

Mr Stolarek—Actually, insurance policies are an excellent example, Mr Beddall. Australia does in fact impose certain withholding taxes in relation to certain insurance policies. For many years, insurance brokerage has been managed and controlled out of other countries—Lloyds and so on—which required particular tax responses to be undertaken. The key issue, and we do recognise the point, is that the growth of Internet commerce and electronic commerce will make it easier to operate internationally. We agree that over time various procedural aspects of our tax system will need to be focused on, and the revenues of the world will need to address in a much more real-time mode unresolved issues of transfer pricing and intellectual property.

As you would be aware, the OECD, through its modern tax treaty network, has determined how countries share taxation on shipping profits, airline profits, and insurance profits, which are all very similar issues. So cross-border issues are dealt with internationally through a harmonised treaty network. Internet commerce obviously requires an allocation issue that needs to be resolved on a worldwide global basis. We support the process of harmonised cross-government interaction. The key observation that we make is that, from a competitive viewpoint for Australia, we as a country need to operate in a way that is consistent with the way other countries are acting.

Because, otherwise, what we risk, in fact—to return to your analogy, Mr Beddall—is that if Australia deals with insurance policies or any other product, any other taxation regime, unacceptably, then the entrepreneur will go to some other jurisdiction and will sell those insurance policies to South Africa or to the USA, and a business opportunity will be lost to this country. We agree that action in the medium term is necessary. We support the approach of the tax office and government to attend to this issue in international fora. We recognise that Australia's interests are not necessarily the same as those of every other country. We have our own tax base and so on.

But the key issue, as Damian stated in our opening comments, is what we see as a process of refining the tax rules with energy, rather than redefining the tax law completely. The absurd notions of a BIT tax, or tax-what-you-can notions, are inappropriate. What is required is focused action on our existing regime, that is carefully focused and acted on.

CHAIR—Arthur Andersen represents tens of thousands of small and medium sized businesses in Australia. We are told that Australia has the second largest take-up per head of population of PCs, but they were at least two years behind the Yanks in terms of take-up of Internet commerce by Australian business and with Australian consumers. How do you see us placed. Can Australian business go all the way? Are there opportunities for Australian business that they are not taking up? And, if so, why not?

Mr Walsh—We hear exactly the same evidence about the take-up of the Internet commerce, and I come back to the point I made earlier about the growth of the mail order business in the United States. The mail order business is proportionately very much greater than it is here in Australia. It is only catalogue sales. It is a cultural thing, I think, rather than anything else.

CHAIR—I am sorry, but that only touches a very tiny fringe of what we are talking about, because the largest trade on the Internet, respectfully, is in services. It is not in goods.

Mr Walsh—That is right.

CHAIR—The question for your clients—the small and medium sized businesses—is, are the opportunities there for them to take up, and what are the constraints? Why aren't they?

Mr Walsh—I think that the opportunities are certainly there. The biggest constraint in terms of taking up electronic commerce at the moment is generally regarded as the security issue, and the difficulties in dealing with security of information over the Internet. It is not regarded as secure. As a firm, we do not send anything that is confidential or even semi-confidential over the Internet, and that is simply a security issue. By the same token we have, as do many businesses, Internet structures that allow them their private electronic commerce networks that avoid some of those difficulties.

It is outside of the tax area for the moment, but to answer your question, I think the security issue is the single biggest concern. Perhaps there is also some issue in there about just who you are dealing with over the Internet.

CHAIR—Are our security issues different than those in the United States? Are we less secure?

Mr Walsh—At this stage I don't think the security differences are material at all.

There may be no differences at all. But maybe I will just come back to my earlier point, and say that perhaps it is just purely cultural.

Mr BEDDALL—If you have bought out of a catalogue, you have a culture of buying.

CHAIR—But the majority of trade is not in goods, it is services. Why are Australian businesses not trading with each other, between wholesalers and retailers, for instance, and importers and wholesalers? Why isn't more business and more inter-company work, policies and software and everything else, being done? Why are we not taking it up to the same degree that they are, when we have almost the same number of PCs per head of population? What are the constraints? Why aren't we getting there?

Mr Stolarek—Mr Charles, as you would appreciate, we are not electronics experts—

CHAIR—You are Arthur Andersen.

Mr Stolarek—but we can actually make some comments. In the US, as you may be aware, the slow development of national banks has resulted in alternative systems developing, with the use of credit cards and so on. The development of Compuserv and America On Line is providing their own secure payments mechanisms that are not truly Internet mechanisms, but they are secure. That, allied with the cultural issue—and Damian's point is actually quite strategic—has meant that the notion of mail order dealing through the secure networks, those two key ones, has been popular amongst the world at large.

If one leaves aside America On Line and Compuserv, the secure networks, and looks at the broader area of Internet commerce, then, as Damian outlined, the security issues in the US are similar to those in Australia. That is to say, one doesn't understand who one is dealing with. The opportunities for Australia are in fact to use our know-how. You will find in our publication at page 6 that Arthur Andersen has a service called EC Integrity, which is really geared to the development of securer identification systems in electronic commerce. I might add that we do accept and support totally the majority focus of the tax office's recommendations that understanding who you are dealing with, who that person is, and privacy issues, need focus in electronic commerce.

So one of our services and great opportunities out of Australia is to provide the software, the infrastructure, for electronic commerce systems. Australian banks and credit card companies and consultancies are in fact working hard in this area. As you would be aware, Web shops and similar software are enabling the notion of Internet shops to be made available in a box of software. That box of software at the moment is uncertain and unstable and, as a result, there is a great opportunity for consultancy services to be provided. So the integration and the advisory role that interacts into Australia's strengths in financial markets is important.

The disadvantages we have identified at item 4. Again, our proposition is that Australia does have this opportunity through our Ozemail and similar software, and so on, to be involved at the front end of Internet commerce. One disadvantage is, Mr Charles, as you would be aware, is our venture capital market makes it enormously difficult to locate suppliers of venture capital in this Australian economy. That is a non-tax issue, of course. As a result, a lot of people in the electronic industry are looking to the US, because that market understands electronic commerce in the capital markets. One can make some money there faster.

This is not strictly an EC issue, but one problem in Australia, particularly relevant for the start-ups in this area, is the way our capital gains tax works. If I was to set up an Internet service provider or a new electronic commerce provider in the US, and I was to sell it out to a major existing player, or to have an IPO in the US, there is in fact a preferable capital gains tax regime. In fact, further than that, if I had a unique piece of software and I was to sell my Internet business by way of a private sale, the purchaser of that software program in fact in the US is entitled to depreciate his intellectual property, to amortise it.

So the issues are not just tax issues, Mr Charles. As I say, it is a capital market that understands electronic business, it is in fact a capital gains regime that makes it much easier for an American small to medium enterprise to sell out, because they will keep 75 per cent of what they sell. In Australia the small to medium entrepreneur will keep, at the moment, 51.5 per cent of what he or she sells. That is a very large difference there. So that actually helps the culture in America of selling out, where the Australian entrepreneur for tax reasons always wants to hold, rather than to sell for a large price.

As I say, one of the important issues affecting this start-up area is, in the US the purchaser in fact is entitled to write off their intellectual property purchase over a number of years, whereas in Australia the purchaser of that Internet service provider has no write-off available for that business. These are, of course, partially tax issues.

Mr BEDDALL—Can I come back to one issue that you raised, and it was raised by the Internet Association of Australia, and that is this 'Who are we dealing with?' issue. They were quite adamant that they thought, in fact, identification should be a function of government. They thought the same methodology should be used as for a passport service; a 100-point check. They recognised that many firms, including your own, were out there because you had a methodology of identifying, in particular, companies. But what is your view on individuals on the net? The CPAs think it would be terrible if the tax office did it. I think that was their view this morning. But there may be an argument that such a thing as DFAT could do it because it has the expertise in doing passports.

Mr Walsh—Again it is outside of the specific tax, area but I would say that it is not a role of government to provide accreditation services. I think there is no reason why they shouldn't be provided by the emerging businesses that are being designed at the moment to accredit dealers on the Internet. I would ask the question, why should it be a function of government?

Mr BEDDALL—They were pointing out you could buy an identification now for $5, and what you got was worth $5. It is that question about establishing the integrity of the identification method. Maybe if it was, 'This is certified by Arthur Andersen, and we will carry all the financial burden,' then that becomes a very useable thing, but Mickey Mouse Identification Pty Ltd probably doesn't.

Mr Walsh—Yes.

Mr BEDDALL—It is about confidence in the Net. I think that is one of the issues that has been raised here, and has been raised before, that Australians are very sceptical about using this sort of technology because they are don't know who they are dealing with.

Mr Walsh—Yes.

Mr BEDDALL—With the cultural thing you are talking about in the US is, they have had 150 years of dealing with catalogue people, and admittedly that has been for goods, but now it is for services.

Mr Walsh—Yes. But actually there is another angle to that, and it perhaps ties into, again, the question that Mr Charles asked before. In the US there are many more private intranet services available for doing business. I had the opportunity to live in the United States for some five years, and five years ago I did all my banking with Citibank from my personal computer at home, everything except taking cash out because I couldn't get it out through my screen. But everything was done that way. I could by and sell shares. I could switch money from bank accounts into mutual fund accounts that weren't actually part of the mainstream bank. I could transfer money between accounts. I could pay credit cards. I could pay bills, as we can over telephone pay our Telstra account and some other accounts, or even by ringing up our bank.

Years ago we could do that over private electronic networks. You would just join up with Citibank's service. All of the banks were offering that service, and many of the other institutions you dealt with on a regular basis would offer that service as well. Now, in that case there are no security concerns at all. I had no concern at all about doing my banking by pressing buttons on my computer and hooking in through the telephone line into the bank's central computer, or whatever I did. I am not sure where it went, but I certainly got all the information I needed. I think actually, Mr Charles, that that is probably more the answer to your question. Five years ago we were already that advanced in the United States, doing those sorts of things in private networks, not over the Internet.

CHAIR—Okay. We are going to have to leave it there, or the next witness won't have an adequate amount of time to talk to us. I thank you both very much for your submission and coming in to talk to us today. We hope to finish the inquiry in April, May or June, and we will certainly send you a copy of our report.

Mr Stolarek—Thank you.

Mr Walsh—Thank you for the opportunity.

[2.30 p.m.]

ROBINS, Mr Ross Alan, Senior Analyst, Australian Bankers Association, 55 Collins Street, Melbourne, Victoria

CHAIR—We have received your submission, but would you like to make a brief opening statement before we ask you questions about it?

Mr Robins—Yes, thank you, Mr Chairman. The Australian Bankers Association welcomes the opportunity to assist the committee with its inquiry into the implications of the expected growth in Internet commerce. As we have outlined in our submission, the Internet provides both opportunities and threats for Australia. The task ahead is to minimise the threats and seize the opportunities. Of course, this task is far from simple. The ability of the Internet to break down international orders brings into question fundamental issues, such as our tax and regulatory structures, and the competitive environment in which Australian businesses operate.

This is certainly the case for Australia's finance sector. As you will be aware, the structure of competition in financial services has been changing . In the days when the industry was highly regulated, banking markets were local. No local branch meant no customers in that area. Today, the situation is significantly different, with institutions successfully offering products in areas where they have no branch presence. National telephone centres, which can service customers in any part of the country, are an integral part of the industry. The break from the face-to-face communication has already been made, and this is where the Internet also has a role to play.

The versatility of the Internet makes it an effective channel for the delivery of financial services, and Internet banking is expected to flourish early in the next century. However, the Internet will also expand current market boundaries, by providing a low-cost means to access offshore banking. This is where opportunities and threats for Australian financial institutions arise.

The opportunities arise by having a low-cost channel to reach offshore customers. The threat is that offshore institutions will also have a low-cost means to access our domestic customers. The banking industry is not opposed to this type of competition, and currently faces internal competition at the wholesale end of the market. However, if we are to compete effectively in this environment, the taxation and regulatory structures must change to facilitate rather than impede the government's policy of establishing Australia as a regional financial centre, second to Tokyo in the Asia Pacific, by 2000.

The Wallis inquiry has potentially addressed the regulatory issues, but there remains a large task ahead in terms of its implementation. However, the taxation issues need to be addressed, or there is no hope for this final objective to be achieved. The most immediate issue is the financial transaction taxes imposed by the states and territories. While these taxes are regressive, inefficient, and distortionary, it is their interaction with the Internet, and their impact on the international competitiveness of Australian financial institutions, which is relevant to this inquiry.

In this regard, financial institutions are a major concern. Simply put, the Internet will make the market for financial services international, and only Australian-based institutions will be subject to this tax. To the best of our knowledge, like taxes do not apply in any other country. The reality is that a transaction initiated over the Internet may cost a few cents to process, but be subject to up to $1,200 in FID if an Australian institution is involved. Avoid the Australian institution and you avoid the tax. The abolition of these taxes is necessary if Australian-based financial institutions are going to secure a competitive position in the Internet market.

Issues like this can only be progressed through fundamental tax reform, and we are encouraged by the government's commitment to this process. We also commend the state and territory leaders for putting transaction taxes at the top of their list of taxes that need to be abolished. However, it is important that forward-looking inquiries such as this identify the threats and opportunities provided by the Internet, so that the government and industry can work together to develop solutions that maximise the opportunities for Australia that arise from Internet commerce. Thank you.

CHAIR—Thank you very much for that. Last week, if I recall right, at hearings in Sydney, the Internet Users Association, in talking about why Australia has not yet taken up Internet commerce to the same degree that it has taken up purchases and use of Pcs, were particularly critical, and in fact, might I say, scathing, of Australia's banks for being slow to provide secure transactions systems on line. Can you comment?

Mr Robins—Yes, certainly. As we are all aware, the Internet is an unregulated market space. There are huge opportunities for fraud. We have to take that into consideration when considering what payment services can be offered over the Internet. It is not just a problem limited to Australia, it is worldwide. The credit card companies and the software companies have got together to develop systems which will facilitate payments over the Internet. Those proposals are commonly called SET, which stands for Secure Electronic Transactions. The first version of the software has recently been completed. Trials in Australia will commence early next year.

Once those trials start to link together, we should be in a position to offer a secure payment system. The emphasis is on secure, because it is no use having a payment system on the Internet which causes customers, either merchants or card-holders, to lose money.

Mr BEDDALL—Mr Robins, if I am a Citibank customer with a Citibank Visa card in Connecticut, I can use my Citibank Visa card to buy on the Internet. I can't use it in Australia.

Mr Robins—You can.

Mr BEDDALL—They tell us that the banks in Australia won't guarantee the funds, and that they themselves are carrying some hundreds of thousands of dollars worth of liabilities, whereas in the United States the Internet providers are not carrying those liabilities.

Mr Robins—I can't speak about the situation in the United States. They have a very fragmented banking system, so whenever you talk about the US banking system, there may be some banks offering different products to others. To the best of my knowledge, they treat mail order and telephone order payments the same way as Australian banks do, because it relates to the agreements with Mastercard and Visa, which are international agreements. Internet payments are treated as mail order or telephone order. The reason that occurs is, basically, you haven't got the card with the person in front of you to confirm a signature.

It is the same if you are doing it over the Internet or by mail or by telephone. Anyone could have picked up the credit card details from a previous sale, from finding a card in the street, from looking over someone's shoulder and writing down the numbers, and it is confirming that identity. At the moment you cannot confirm that identity over the Internet. The SET procedures will solve that problem.

CHAIR—Yes, but, with respect, you are talking about the future, and I am asking about the past. We know that we have the second-largest take-up of Pcs in the world, right behind the Yanks. We are also told by everybody, though, that we are two years behind in take-up of Internet commerce. When we ask people why, one of the leading reasons, time after time after time, is security of transaction. Why has the Australian banking industry been so far behind, when in fact on things like EFTPOS and hole in the wall we have been way out front, and Australians have accepted them?

Mr ANTHONY—ATMs, they are called.

CHAIR—ATMs if you want to be precise. Australian have grabbed hold of them with both hands and both feet. Why has the banking industry been so slow to give Australians a feeling of security on line, where your competitors in other countries have got on with it?

Mr Robins—We don't believe that the competitors in other countries have a secure system. SET will become the standard internationally. It is the one which Visa and Mastercard will stand behind.

CHAIR—So you are saying Americans didn't need security, and Australians think they do?

Mr Robins—No.

CHAIR—That accounts for two years lag time and take-up of technology.

Mr Robins—This is truly a system for payments on the Internet, as opposed to what I think Arthur Andersen were talking about. In America you have systems like Compuserv, which are proprietary. They can develop systems within that which solve the payments solution. In Australia we don't have those systems.

CHAIR—No, we are talking about Internet take-up, the take-up of Internet commerce.

Mr BEDDALL—If I use my Mastercard or Visa in the United States, outside of Compuserv and those other secure networks, then it is treated as a mail order, the same as if I phoned or whatever?

Mr Robins—That is the information which I have been given.

Mr BEDDALL—We might go back to the Internet providers and find out whether they need Compuserv, because it sounds logical if it is just treated as a mail order. Because in any mail order or phone business, until it is authenticated, the transaction doesn't exist.

Mr Robins—Yes. It is exactly the same. You are dealing remotely from the customer. How do you confirm the customer's identity? The last thing we want to do is be offering a service over the Internet which we promote as being secure, which is not. That is irresponsible.

Mr BEDDALL—As someone who left his Visa statement on the bank counter today, I am glad that there is some security, in case someone picked it up and used it.

Mr Robins—Yes. The worst case scenario is that you put a system up and it fails, and then you have got no confidence in it. That could be a serious setback. We don't apologise for wanting to get it right.

CHAIR—I understand personally—not the committee—from discussions that the National Bank intends to be on line with on-line banking services this month, or December at the latest. In your submission you said:

> Concerns regarding transaction security are being addressed, and as banks become satisfied with the security, the number of institutions offering Internet banking will expand.

How fast?

Mr Robins—That is an excellent question. The Commonwealth Bank is already on line with an Internet banking product. As you suggested, your information says the

National is this month or next. Westpac, National Australia Bank and ANZ all have plans for next month, or early next year, from what I have been able to gather. There are certainly more banks overseas with an Internet presence. I think part of that is the US experience, in terms of Internet take-up. But also there are a huge number of banks in the US. It is going to be a worldwide phenomenon, I think. Banks have solved the security concerns that they had, and as they are solved, they will come on line.

Mr BEDDALL—We heard from Arthur Andersen before, and I think you were here when we were talking about the gentleman who lived in New York who was on line with electronic banking on his PC. Electronic banking is something that hasn’t taken off in Australia, isn’t it?

Mr Robins—Yes. I am not sure of the reasons why. We certainly had products available. I can remember in a past life when I worked with Westpac, and that must have been 12 years ago, one of the jobs I had was to going around selling a PC banking product. It just never seemed to take up. I think it might have been that it was before its time. I am not sure.

Mr BEDDALL—Maybe Australians think they would rather go to a bank. The queue I was in today, you would wonder why.

Mr ANTHONY—Just following along that line, not directly in terms of this reference, one of the things that you would have seen is that it is cheaper now to use, as the Chairman says, a hole in the wall than to actually go into the counter. Whilst deregulation has been good for many consumers—and they are not really happy about the fees, but be that as it may—from discussions that you have had with some of the other banks that are currently introducing Internet services, or will next year, have you any idea what the variation in the fee arrangement will be? Will banks be encouraging people to go on line?

Mr Robins—One thing that the banks do not discuss with us as an industry association is their fees, and what they intend to do. I think we would get in quite a lot of trouble if we were involved in that area. All I can suggest is that in a deregulated environment you would expect that fees would in some respect mirror costs and, to the extent that the Internet will be a cheaper delivery channel, you may expect that the prices for Internet transactions may be lower.

Mr ANTHONY—Do you think there will be much difference in charges between on the phone or direct?

Mr Robins—Probably not. If you have got an automatic voice response for your telephone inquiries, it is a piece of hardware that is sitting there which is responding. You have got fixed costs that go with that. Your variable costs are very low. I think the same sort of situation probably occurs with the Internet.

Mr BEDDALL—Yes. One of the reasons for the high take-up of, as Mr Charles puts it, holes in the wall, is because banks have basically forced the change, haven't they? Front-line staff are nowhere near the numbers they were. I worked for the Commonwealth Bank when they still did the ledgers by hand—that is how old I am—but the staffing levels aren't there any more. Therefore things like cash transactions are being forced outside of the bank, and I suppose it is in the banks' interests to force on-line transactions; that is, paying accounts and bills and whatever. If you can do that through the Net, it is obviously a gain, another cost reduction in the physical infrastructure for banks.

Mr Robins—I don't think it is actually a case of forcing that so much. There was no concept when ATMs were first introduced that it was forced. The ATMs were a service which basically allowed customers to obtain funds outside the normal banking hours.

Mr BEDDALL—But now they close branches so you have to go to the ATM.

Mr Robins—Yes. Now perhaps that is an issue. But that is just an issue that has arisen from deregulation. As I said before, the fees that you charge to an extent have to reflect the costs that you are incurring. That is economically efficient. That is the way things have been going, and I don't see them moving back from that.

CHAIR—I understand that Mondex is likely to be introduced shortly, in early 1998. Is that correct? Is that your understanding?

Mr Robins—My understanding is it will be launched in 1998.

CHAIR—Do you think the take-up rate will be very rapid for that as the form of a smart card?

Mr Robins—I have no idea. I think that is one of the great unknowns.

CHAIR—It does, I understand, offer the potential to transfer money from a bank account to the smart card, from the smart card to your credit card, or to a global, unknown, cyberspace banking point, or any interchange between any of those, or some international bank or other location, or to download to clients or pay your parking meter with it, et cetera. That offers exciting challenges, doesn't it?

Mr Robins—That is certainly the potential. The market always has some say in what is going to happen with a product.

CHAIR—The Edsell didn't fly very well, did it?

Mr Robins—No, and whether people will accept having a piece of plastic with a chip in it in their pocket, rather than having physical cash, is a large question. Personally, I will.

CHAIR—I came to Australia with five or six supposedly international credit cards in my wallet, and found that nobody wanted to know them. That was in the late 1960s, early 1970s. Nobody wanted to know about them. Today our use of plastic would be probably as great as any country on earth, wouldn't it?

Mr Robins—Yes.

Mr BEDDALL—Thanks to the banks. It is called Bankcard. It is the greatest single marketing success in the history of commerce.

Mr Robins—We are dealing with a new product, and it is fundamentally different.

CHAIR—Okay, it is a real challenge, is it?

Mr Robins—It also relates to the number of merchants that you have out there that are prepared to accept the card, so you are going to go through an interim phase where you are going to need both. You won't be able to go all on to Mondex from cash, because not everyone will accept Mondex to start off with.

CHAIR—I accept that, but there are still merchants who won't accept credit cards, and most of them are out of business. What challenges do you see for expansion of Internet banking services for Australia's benefit, posed by our taxation systems or our regulatory systems?

Mr Robins—The biggest single challenge for Australia is FID—financial institutions duty.

CHAIR—I knew you would say that.

Mr Robins—There is no doubt about it. It is not going to be a factor so much at the retail market to start off with, but on the corporate side of it. A lot of the focus is always on what is going to happen with consumers and what is going to happen with retail customers, but at the end of the day corporates are large users of technology. Corporates are setting up their own Internet sites. They are the ones with the experience. They are going to have confidence in it before consumers will have confidence in it, because they are going to be dealing in it. They understand the technology.

Banks around the world are looking at developing corporate Internet banking sites. Some of those banks are going to use that to drive international expansion. When you look at it from a corporate customer's point of view in Australia, if we make a transaction of $2 million, we have got to pay $1,200 in FID that goes to a state government. How easy is that for us to avoid? Well, we maintain foreign currency accounts offshore now. It is no big deal. All of a sudden, all the communications issues in dealing with those accounts, with accessing that money, can all be done over the Internet from a screen sitting on the treasurer's desk.

CHAIR—So you are saying FID has forced cash into overseas locations?

Mr Robins—Yes. In the Coopers and Lybrand survey, a copy of which I think we have provided you with, and it is also quoted in our submission, corporate customers were surveyed, and I think something like 65 per cent indicated that they maintained foreign currency accounts offshore, and the main reason was FID.

CHAIR—How much is that costing Australia?

Mr Robins—I can't tell you the balance of the accounts, but if that is a trend which continues, it does cost Australia in terms of employment and in terms of jobs.

Mr ANTHONY—I am not familiar with the Coopers and Lybrand figures. I assume those cash reserves offshore must obviously have been all declared, and that is how they got those figures. Is that correct?

Mr Robins—The figures came from a survey of Australian corporates.

Mr ANTHONY—They end up paying a withholding tax on that. It is hardly worth while, is it?

Mr Robins—That is if the money ever comes into the country. If you are talking about a mining company that is selling product offshore in US dollars, why do they bother bringing the US dollars back on shore? The money can just stay out there, and they can meet overseas commitments from their offshore account.

Mr ANTHONY—What about the BAD tax, the debit tax?

Mr Robins—Debits tax is less of a problem in terms of international competitiveness, because it is linked to accounts with cheque access. The way we see it, cheques will become a thing of the past. There is a role for them probably in the next 10 to 25 years, but it will be a decreasing role.

Mr ANTHONY—So what do we do? We just get on-line and pay our accounts?

Mr Robins—Yes. Most people today use very few cheques. They are still used a lot in terms of businesses, but there is a new product being launched next week by the banks which is called BPay. That will be another product which will replace some of the cheque business.

Mr ANTHONY—What is that? How does that work?

Mr Robins—Basically you will be able to telephone your bank and just make a bill payment to someone you owe money to, be it an electricity company, be it Telecom, or be it your water rates. There will be a number on the invoice which you receive which you will just key in, and that will make the payment straight from your account to them over the telephone. That will also be connected to the banks' Internet sites as well, so you will be able to make those payments over the Internet. That sort of technology will replace cheques.

Getting back to the debits tax, debts tax will become less of a problem because it will diminish as cheque usage diminishes. The other aspect of international competitiveness is that the maximum debits tax is only $4, so at the end of the day a corporate probably doesn't mind paying $4 on a $2 million transaction. It is a lot different from $1,200.

CHAIR—Just as a matter of interest, with the telephone payment through your bank, what kind of audit trail do you as an individual get back on your statement?

Mr Robins—On your statement it will have who the payment went to.

CHAIR—Will it?

Mr Robins—Yes.

CHAIR—Right. Then you can forget about your cash, if you really wanted.

Mr Robins—It will virtually appear on your statement as a credit card transaction appears on your credit card statement. It will have who the money was provided to, the amount, and probably some serial number.

CHAIR—Mr Robins, thank you very much for your submission and for coming and talking to us today.

Mr Robins—It was a pleasure.

CHAIR—As you heard me tell the others, we will finish in May or June or something like that, and we will certainly send you a copy of the report.

Mr Robins—Thank you.

Resolved (on motion by Mr Anthony):

That, pursuant to the power conferred by section 2(2) of the Parliamentary Papers Act 1908, this committee authorises publication of the evidence given before it at public hearing this day.

CHAIR—Thank you.

Committee adjourned at 2.45 p.m.