SUBMISSION TO THE SENATE STANDING COMMITTEE ON ECONOMICS INQUIRY INTO THE TREASURY LAWS AMENDMENT (GST LOW VALUE GOODS) BILL 2017

Chris Berg and Sinclair Davidson

Executive Summary

- The elimination of the low-value threshold for the Goods and Services Tax constitutes a new tax on inbound internet trade – that is, it will function as a tariff imposed on Australian consumers.
- The tax will raise very little revenue and will be expensive and complex to administer.
- The tax deviates substantially from the existing GST design.
- The tax is less a tax on consumption but on the reputation of foreign internet businesses.
- The tax is inconsistent with the government's commitment to deregulation, the promotion of international trade, and its innovation agenda.
- The tax rejects principles that the Howard government established in terms of deregulation and the promotion of international trade.
- The tax will do nothing to address the issue of high retail prices in Australia.
- While masqueraded as a tax integrity measure, this tax is clearly intended to operate as a form of protectionism.
- The tax will reduce competitive pressure within the domestic Australian economy, and (as a consequence) expose Australian consumers to government sanctioned higher retail prices.
- The tax will lead to Australian consumers substituting away from large reputable electronic distribution platforms to more disreputable platforms leading to higher rates of internet fraud and possibility criminality. Product safety and consumer protection rights are likely to be compromised.
- The tax has few safeguards to ensure compliance and remittance of revenue to the Australian government.
- The tax contributes to increased levels of regime uncertainty within the Australian policy environment.
- Parliament should reject the Treasury Laws Amendment (GST Low Value Goods) Bill 2017.

I INTRODUCTION

In his *Wealth of Nations* (1976), Adam Smith proposed four principles of taxation which still inform discussions of the structure of a taxation system today (Alley and Bentley 2005). Taxes should be imposed with regard to their equality, certainty, convenience of payment, and the economy of their collection. The Treasury Laws Amendment (GST Low Value Goods) Bill 2017 violates each one of these principles. It is levied unequally, distorting competition and purchasing decisions. The administration of the tax will be uncertain and subject the Australian tax regime to significant uncertainty. While the tax will likely be convenient to pay for consumers, it is likely to be highly inconvenient for the retailers who will bear the responsibility for remitting revenue back to the Commonwealth government. Finally, while the decision to require the tax to be collected by retailers reduces the cost of collection for the Australian government, the cost and logistic complexity of foreign firms collecting Australian taxes is likely to be substantial.

Currently imports into Australia purchased by Australian consumers are liable for GST payment at the border only if the purchase exceeds $1,000. By contrast, all goods and services purchased in Australia at Australian retailers (that exceed a turnover of A$75,000 per annum) are liable for GST regardless of their cost. The Bill eliminates the *de minimis* import threshold, making all purchases liable for GST whether they are purchased from firms inside Australia's indirect tax zone or not. The Treasurer has described the purpose of this bill to ensure that "low-value goods imported by consumers will face the same tax regime as goods that are sourced domestically" (Commonwealth Parliamentary Debates, House of Representatives, 16 February 2017, p. 1278).

It has long been recognised in Australia, however, that at a sufficiently low figure, the cost of imposing a tax at the border on low value goods is uneconomical, as, at some point, the cost of collection exceeds the revenue collected. The Productivity Commission (2011: 169) found that "In most scenarios estimated, total collection costs would still exceed additional revenues or generate net efficiency losses for the community". In this context, the Bill is structured to relieve the cost of collection from the Australian government. To do so, it places an obligation on foreign firms doing more than A$75,000 worth of business with Australian customers to collect GST on behalf of the Australian government for their transactions with Australian customers. Overseas firms will be required to "register for, collect and remit" GST to the Commonwealth. Further complexities have been added by the Bill's intent to target "online marketplaces" rather than individual suppliers themselves – the government has in mind here platform retailers such Amazon.com's marketplace service or eBay – and redelivery services, which on-forward goods to Australia from foreign firms that do not natively offer international shipping.

We argue in this submission that the complexity of this tax structure reflects a conceptual confusion about the nature of Australia's Goods and Services Tax and the significance of online retailing that could have substantial consequences for the integrity of Australia's tax system and Australia's reputation as a good international player in global tax administration. This submission follows from work we have done in recent years on the low value threshold GST (Berg 2015; Chung 2015) and on questions of Australia's position in the global tax regime more generally (Berg and Davidson 2015, 2017b; Davidson 2014; Zhang et al. 2017).

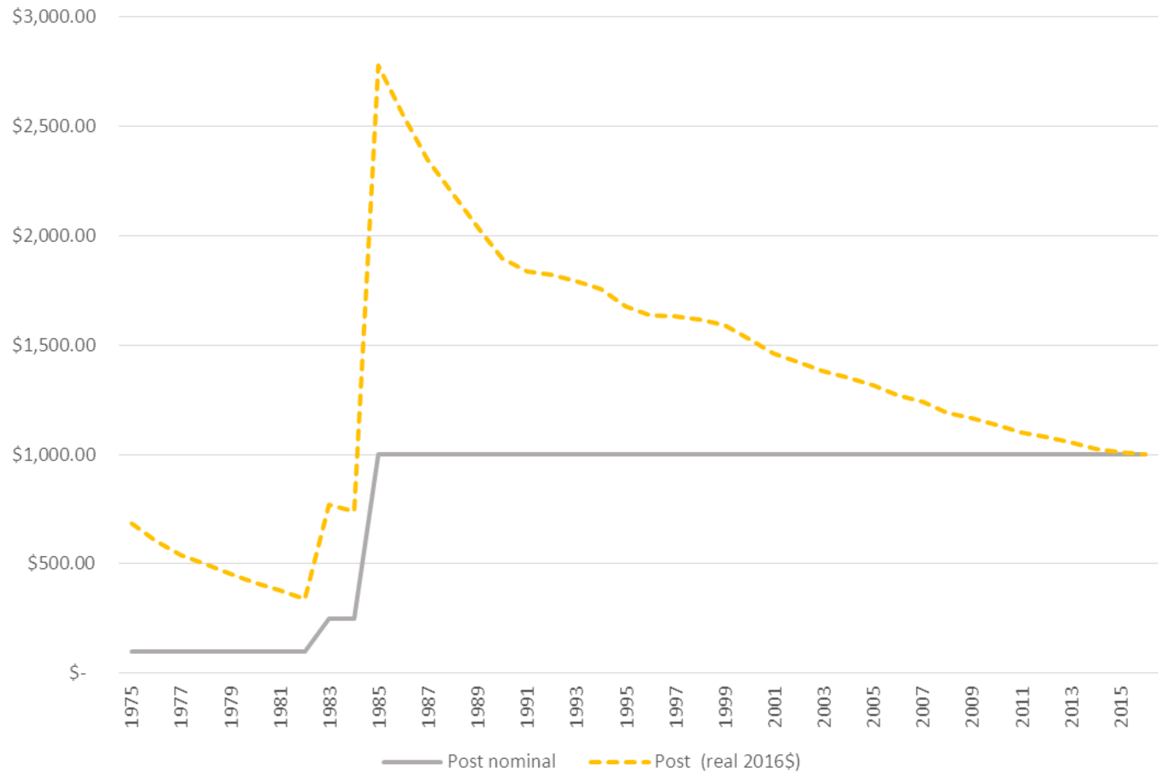
In this Part II of this submission we outline the origins and significance of the $1000 threshold. In Part III we outline the conceptual confusions behind the government's policy. In Part IV we outline some of the likely consequences of this change. In the conclusion we consider how this policy is likely to affect Australia's reputation as a good international player.

II THE PURPOSE AND ORIGIN OF AUSTRALIA'S LOW VALUE THRESHOLD

The A$1,000 low value threshold has its origin in the customs entry (screen free) thresholds and duty and tax free thresholds at which goods entering the country do not have to be formally entered through customs and at which goods are treated as duty and tax free respectively. In her survey of value-added taxes around the world, James (2015: 57) argues that thresholds are set with regard to "striking a balance between revenue foregone and administration and compliance costs". However the Australia thresholds have had a broader purpose than that. The Australian Taxation Office (1997: 7) has characterised the low value threshold as a mechanism to reduce the regulatory burden on international trade. The purpose of the low value threshold is "[a.] minimising delays in the delivery of mail and cargo, [b.] reducing the cost to business of importing low value consignments, [c.] determining a value below which it is uneconomical for [customs] to collect the tax and duty, and [d.] to facilitate international trade by minimising [customs] intervention." The relative cost of collection against the possible revenue raised by collecting revenue at the border is only one of four purposes of the low value threshold – rather, the emphasis is on keeping the burden of red tape low and encouraging, rather than discouraging, trade.

The low-value threshold has been adjusted over time, but does not appear to have any relationship to the cost of collecting revenue at the border. Figure 1 shows the duty and sales tax free threshold between 1975 and 2015 for post. Since the introduction of the GST in 2000, this has become popularly known as the low-value threshold for GST. Set originally at $100 in 1975 dollars, between 1986 and 2005 the threshold distinguished between goods which arrived by post and goods which arrived by means other than post (not shown). In 2005 the Howard government reconciled the two thresholds into the single $1,000 threshold that remains today.

Figure 1: Low value (duty and sales tax free) threshold for post, 1975-2016



Source: Australian Customs Service, Submission to the Joint Committee of Public Accounts Inquiry into Internet Commerce, 29 September 1997; own calculations.

The stable nominal threshold masks the substantial change in the real value of the threshold. As the Board of Taxation (2010: 46) noted, the non-indexation of the threshold, which has remained fixed since 2005 and fixed for goods arriving by post since 1985, "will reduce over time any potential bias in favour of imported goods over local goods of the same quality and value". The table shows the thresholds in 2016 dollars to show how significant that reduction has been. When the A$1,000 threshold was first set in 1985 it was the equivalent of A$2,780 in 2016 dollars.

Why was the uniform threshold fixed at A$1,000 in 2005? Complaints that online trading might compete with Australian firms subject to Australian sales taxes date back at least to the earliest parliamentary reckonings with the digital economy (Joint Committee of Public Accounts and Audit 1998). As documents released under freedom of information legislation reveal, the Howard government considered reducing the uniform threshold to A$500, and this was the position recommended by the Minister for Justice and Customs at the time. However, the prime minister rejected this recommendation at set the threshold at A$1,000. The explicit intent behind this decision was "the government's commitment to reduce the burden of regulation" (Howard 2005). As we have seen, the historical purpose of the low value threshold is not to maximise revenue to the Commonwealth but to reduce the compliance burden of customs and facilitate international trade. The Howard government decision was consistent with that intent.

III A SALES TAX IMPOSED ON FOREIGN SALES IS A TARIFF

It is important to understand that the Australian Goods and Services Tax is a value added tax (VAT). Value added tax is a form of sales tax that is levied on business sales at each level of production and distribution. It is applied to the sales price of goods and services net the cost of purchase and previously paid VAT. As such it is not a tax on gross sales or turnover but rather a tax on net sales. For more detail see Tait, Ebel and Le (2005). The government acknowledges that the GST is a sales tax by listing it as being a sales tax in the Budget Papers.

Value added taxes are usually described as being consumption taxes – this is based on the *assumption* that the tax is passed forward to the consumer. An important component of the VAT is that the government refunds the VAT that has been paid along the value chain until the final consumer purchases the good or service. Like most countries that operate a VAT, Australia employs the credit-invoice mechanism to keep track of the integrity of the tax. This entails a complex paper trail of invoices that can be audited by the tax authorities to minimise fraud. The Australian VAT is quite comprehensive with few exemptions (fresh food, education, health, government services). The other important point is that for-profit businesses only have to register for GST once their turnover exceeds A$75,000, and non-profit organisations only have to register for the GST once their turnover exceeds A$150,000. Finally consumer prices, in Australia, are quoted inclusive of GST.

In this section we argue that the proposed extension of the GST to low imported goods is not an integrity measure or a fairness measure as the government has suggested, but rather it is a new tax.

The key point to our argument is the following feature of the legislation (Explanatory Memorandum, pg.7):

> The reforms:
>
> …
>
> - treat the operator of an electronic distribution platform as the supplier of low value goods if the goods are purchased through the platform by consumers and brought to the [Indirect Tax Zone] with the assistance of either the supplier or the operator.

This is a stark divergence from how value-added taxes are usually constructed. Normally a VAT is a tax on net sales with the assumption that tax has been passed forward. This new tax is a tax on a business that facilitates trade between two separate parties. Imagine if instead of a buyer and seller trading on an electronic distribution platform they conducted their business over the telephone. If this Bill were to operate in a consistent manner it would then be imposing the tax liability on the telephone company.

To highlight the absurdity of the Bill, we make use of one of the examples set out in the Explanatory Memorandum (pg. 21).

> Wei is a resident of Hong Kong who purchases a piece of artwork valued at $700 from a supplier in Vietnam. The supplier arranges for the delivery of the artwork to his niece Li who lives in Australia.
>
> A supply of goods is a supply of low value goods if the customs value would have been $1,000 or less at the time when the consideration for the supply is first agreed. The artwork has a customs value of $700 and is therefore a low value good. The supply of this low value good is connected to the [Indirect Tax Zone], because it is a supply of a low value good that is purchased by a consumer and brought to the [Indirect Tax Zone] with the assistance of the supplier. Wei is not registered for GST and is therefore a consumer for the purposes of the GST law. The geographical location of Wei, being outside Australia, is irrelevant.
>
> Accordingly, the supply of the artwork is connected with the [Indirect Tax Zone].

At present the gift to Li is GST-free. It is proposed that the GST should apply to the gift. Yet neither the artist nor the purchaser is resident in Australia. Clearly the government have decided that having the gift held at Customs until Le pays the A$70 is neither financially viable nor practical. If Wei were to travel to Australia bringing the gift with him, it would remain GST-free and similarly were he ask a family member or friend to bring the gift to Australia it would also remain GST-free. It becomes taxable simply because it was brought to Australia with the assistance of the seller. The point to understand is that the tax liability is generated by the mechanism whereby the good or service enters Australia. (In this instance the artwork becomes taxable in Australia depending upon whether a related service, i.e. the transport of the artwork, is offered by the supplier.)

Now consider whether the artwork would attract GST if it were sold in Australia. If it was bought from a for-profit business with a turnover in excess of A$75,000 it would attract the GST. Yet if it were purchased from an artist with an income of less than $75,000 it would be GST-free. A Vietnamese artist with an income of greater than A$75,000 would be a wealthy artist indeed. The next point to understand then, is that this new tax brings foreigners into the Australian GST tax system where Australians would be exempted. This constitutes a discriminatory tax on foreigners that would not equally apply to Australians.

Imagine now that Wei bought the artwork from the Vietnamese supplier over an electronic distribution platform. Imagine further that the electronic distribution platform is a reputable business located in, say, the United States. This US firm is now liable for the Australian GST because a Hong Kong Chinese national traded with a Vietnamese national who transported a A$700 artwork as a gift to Australia. Again, if the artwork were transported to Australia via a family member or friend, the US electronic distribution platform would not be liable for the GST. The operation of the tax seems very arbitrary, and somewhat voluntary. Ironically, the new tax is being promoted as a mechanism to overcome arbitrariness. As Myer chairman Paul McClintock has argued (Durkin 2016):

> It's absolutely crazy that you pay different tax depending on where you buy a product from," Mr McClintock told the *Financial Review*. "We are now in a completely seamless market. You can sit in your home and order from one site and it's taxed, and another and it isn't. That's balmy. It's outrageous.

It is not clear, from the government's own example, that this new tax resolves the outrageous and balmy situation that Mr McClintock identifies. If anything it is now worse. (As an aside, we suspect Mr McClintock would never agree that his landlord should be responsible Myer's tax liabilities – yet that is what this new tax would imply were applied to his business).

Then there are questions as to the administration of the new tax. Let us assume for arguments sake that the reputable US electronic distribution platform does (somehow) collect the GST from Wei and passes it onto the Australian Taxation Office. Then the new tax will have operated as planned. But what happens if Wei and the Vietnamese supplier transact via a disreputable electronic distribution platform? This electronic distribution platform could, for example, simply not collect the GST or it could collect the GST and not transmit it to the Australian Taxation Office. What mechanism would the Australian Taxation Office have to enforce compliance with Australian law? How would the Australian Tax Office even know that a tax fraud had occurred?

Compliance with this law appears to be somewhat voluntary and arbitrary. The Australian Tax Office has no authority or power to audit any of the participants to the transaction nor is it likely to have any authority or power to audit the electronic distribution platform. To be clear – the example above is one given by the government to illustrate how the new tax is to operate. The fact that it is so easily reduced to an absurdity demonstrates the fragility of the rationale for the tax.

In this instance it is very unlikely that the Australian government would ever receive any GST revenue, unless it adopted the expensive and impractical policy of holding the artwork at Customs until the GST was paid. From the Australian government's perspective this would be case of tax avoidance or evasion. We discuss this in the context of Webley, Adams and Elffers' (2006) five factor model of VAT avoidance:[1]

- Sanctions and punishment: Generally the higher the probability of detection and punishment the higher the compliance with tax law. As we have suggested, however, the Australian Tax Office has little power to audit and enforce compliance with Australian tax laws when all the parties to the transaction are overseas and the electronic distribution platform has no connection to Australia. Strictly speaking the Australian government requires the cooperation of foreign governments to operationalise the new tax. Yet the Vietnamese government is likely to see the sale as an export (and not want to tax it), the Hong Kong government would have no interest as the transaction does not involve importing anything into Hong Kong, the US government, at best, would see this as an export, but most likely show no interest in the transaction beyond taxing the electronic distribution platform on its ordinary income under its own tax laws. To the extent that the GST payment from the electronic distribution platform constituted a deduction under US law, this could reduce the taxable in the US leading to a wealth transfer from the US to Australia.

[1] They appear to conflate the terms "avoidance" and "evasion". Strictly speaking tax avoidance is legal, while tax evasion is illegal.

- Equity: Perceptions of fairness are important in tax compliance. The extent to which either Wei or the Vietnamese supplier thought it fair that the Australian government tax the transaction would determine their willingness to pay the tax or declare the tax liability. We suggest that it unlikely that either party would perceive Australian taxation of the transaction appropriate.
- Personality: We do not have enough information in the example to speculate on how this would operate. Generally, however, those individuals who are more community minded are less likely to engage in tax avoidance and evasion.
- Satisfaction with tax authorities: Those individuals who believe that government money is generally wasted money are more likely to avoid and evade paying tax.
- Mental accounting: The issue here is how businesspeople mentally account for the GST. Those who clearly in their minds separate out the GST from the turnover are more likely to pay the tax, while those business people who do not clearly separate the money are more likely to (attempt) to evade the tax. According to the Inspector-General of Taxation (2015) 60% of tax debt owed to the Australian Tax Office was from the small business category. Of that amount 74% was owed by micro-business, i.e. businesses with a turnover of less than A$500,000. Clearly, small business (those likely to be employing an electronic distribution platform or selling Vietnamese art) do not clearly separate out the GST from their turnover.

Now it could be argued that the example we have chosen for our critique is trivial. Yet – it is the government's intent that the GST should apply in that situation. Consider a simple change – imagine that Wei is resident in Sydney, and he buys an artwork from a Vietnamese supplier and imports it into Australia. Much of our critique remains unchanged. If he was to contact the Vietnamese supplier by telephone it is easy to see the absurdity of making the telephone company liable for the GST. Yet the electronic distribution platform would be liable for the GST payment. The Vietnamese supplier is still brought into the Australian GST system even if not earning an income of over A$75,000. It may well still be the case that a reputable US electronic distribution platform is liable for the GST payable on a transaction that occurs between an Australian and a Vietnamese resident. Of course, we can also speculate on why Wei might buy from an overseas supplier using an electronic distribution platform.

If Australian retailers are to be believed Wei shops online to avoid paying the GST. This invites us to imagine that the only difference between Australian retailers and international retailers online is the 10% price differential. For example (Low and Mather 2015):

> Retailer Gerry Harvey has seized on the proposal, welcoming it as a way of finally levelling the playing field for local shops, which have to charge GST on all items.

Similarly, Treasurer Scott Morrison made the following comment in his second reading speech:

> These changes are about ensuring that Australian businesses, particularly small retailers, do not continue to be unfairly disadvantaged by the current GST exemption that applies to imports of low-value goods.

Yet what Morrison and Harvey, and many other Australian retailers, refuse to acknowledge is that Australian retail prices are high compared to their international competitors. Novak (2015) provides a broad ranging price comparison between identical Australian sourced goods and internationally sourced goods. The price differentials ranged from a low of 14% to 70% for the *identical* products. Novak suggests that rather taxing foreign goods the government should focus its attention on why

Australian prices are so high. Of course, the government earns higher GST tax revenue from higher prices and has no incentive to lower consumer prices for Australians.

We argue that the extension of the GST is a revenue grab by government being passed off as a protectionist measure. It is simply populism. It is in fact a tariff. There are significant deviations from the structure of the GST to suggest that this new tax is not a GST.

We have already canvassed the fact that sellers with incomes less than $75,000 will be drawn into the tax net. We have touched on the changed legal incidence of the GST. We now explore that issue in some detail. It is worthwhile quoting the Explanatory Memorandum in some detail:

> Broadly, the electronic distribution platform rules apply to shift GST liability for supplies made through electronic distributions platforms from individual suppliers to the operators of the platform.
> …
> The operators of electronic distribution platforms are better placed to comply with GST obligations because they are generally larger and better resourced entities than individual suppliers.

In the operation of the current GST the legal incidence is placed on the supplier with the assumption being that the tax is passed on in full to the consumer. The refund of the input credit is an important part of the tax design underpinning the assumption of the pass forward. The new tax, however, does not involve the commonwealth government refunding any money to suppliers or even electronic distribution platforms. The assumption that the tax is passed on in full, and so becomes a consumption tax, is now fragile. (Of course, it could well be violated in practice already, but now becomes untenable – see Slemrod (2008) for more discussion). The new tax is a tariff on goods imported into Australia based on online purchases. Another way of looking at it is as tax on Australian inbound internet commerce. It is not clear that the tax falls on Australian consumption, or whether the tax becomes a “trading-with-Australians tax”. Most certainly, however, it exposes electronic distribution platforms to arbitrary and uncertain Australian taxation. Very likely some of these platforms will exit the Australian market or refuse to deal with Australian consumers and retailers. This is very likely to isolate Australian internet start-ups and undermine the government’s own innovation agenda.

The very purpose of the A$1,000 threshold was to promote international trade; the government now seeks to inhibit international trade.

We also need to examine the efficiency of the GST as a tax. The GST is an expensive tax to administer. According to the Australian Tax Office 2014-15 Annual Report the cost to collect A$100, including GST collections, was A$0.84 compared to A$0.77 excluding GST collections. The new tax is not likely to reduce the collection cost of the GST. On the other hand, it is not likely to raise very much revenue. Table 1 shows data from the annual Tax Expenditures Statement prepared by the Australian Treasury on foregone revenue from the A$1000 GST threshold and data from the Explanatory Memorandum as to expected revenue from the new tax. GST revenue data are from the Budget Papers.

Table 1: Estimates of GST revenue from Low Value Goods as % of total GST revenue

	Tax Expenditures Statement					Explanatory Memo	
A$m	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
	400.00	390.00	380.00	390.00	390.00	70.00	100.00
Revenue	48,596.00	51,394.00	54,542.00	57,808.00	60,928.00	64,928.00	67,640.00
%	0.82	0.76	0.70	0.67	0.64	0.11	0.15

Sources: Tax Expenditures Statement, Budget Papers 1, Explanatory Memorandum; own calculations.

According to data from the Tax Expenditures Statement the foregone revenue from the A$1000 threshold is less than 1% of total GST revenue. For this financial year we estimate the foregone income to be 0.64% of total GST revenue. Using data from the government's Explanatory Memorandum the expected revenue from the new tax would constitute 0.15% of total GST revenue.

The GST itself is a complex tax to administer and expensive to collect. This new tax being proposed by the Australian government will not be any less complex to administer – in fact, it is likely to more complex to administer and more expensive to collect, yet it is not clear that it will generate substantial revenue.

IV CONSEQUENCES OF REMOVING LOW VALUE THRESHOLD

The first order consequences of the Bill will be to raise the price of goods to Australian consumers and reduce competitive pressure on Australian firms. We see no reason to believe that the revenue raised from this measure will be used by the Australian government in a socially optimal manner. While the Commonwealth is running a substantial budget deficit this is a reflection of the fact that it has increased its recurrent spending rather than suffered revenue declines (Makin and Pearce 2016).

However, the Bill's specific approach to removing the low value threshold is likely to have some significant consequences for Australia's international trade and consumer safety online that the committee should consider.

Consumer safety

The Bill provides no effective mechanism to enforce its requirement that foreign firms participate in the Australian taxation system. In that context, it is a reasonable assumption that only large firms with substantial engagement in Australia – and which intend to extend that engagement over time – will participate. The decision of the government to specifically treat electronic distribution platforms and redeliverers as suppliers, rather than the retailers of the goods themselves, is likely to create substantial problems.

To give context, it is important to recognise how the current ecosystem of online retail has evolved. An early concern with internet commerce was the reliability of service and the enforceability of contracts. Evidence to a 1998 parliamentary inquiry into internet commerce found reasonably high degrees of concern with the response time, access cost, and security of financial transactions online (Joint Committee of Public Accounts and Audit 1998). An influential paper by the economist George Akerlof (1970) identified the apparently high risks of market transactions, finding that information asymmetries between buyers and sellers could leave buyers unsure of the quality of goods and consequently unwilling to make beneficial trades. In the digital space this problem was potentially more pronounced, as buyers and sellers operated at a distance from each other – often in different countries with different legal systems and remedies for fraudulent or unfair trading. The result of these concerns in the late 1990s was the development of principles of electronic commerce that relied heavily on regulatory supervision of online markets (National Advisory Council on Consumer Affairs 1998).

These regulatory perspectives failed to recognise the key role that reputation plays in the establishment and sustainability of market transactions (Klein 1997). As Adam Smith (1997: 17) wrote,

> A dealer is afraid of losing his character, and is scrupulous in observing every engagement. When a person makes perhaps 20 contracts in a day, he cannot gain so much by endeavouring to impose on his neighbours, as the very appearance of a cheat would make him lose. Where people seldom deal with one another, we find that they are somewhat disposed to cheat, because they can gain more by a smart trick than they can lose by the injury which it does their character.

A large part of the success of internet commerce has been the development of these reputation mechanisms. Tadelis (2016) notes the central role that reputation management plays in marketplaces like Amazon Marketplaces, Airbnb, eBay, Uber, Taskrabbit, the Chinese eBay competitor Taobao, and the Indian Flipkart. There are a wide range of niche online marketplaces that use similar mechanisms, such as the Lego trading service BrickLink. These platforms trade on both the reputation of the platform itself – and consumer protection mechanisms within – as well as providing buyers and sellers the ability to monitor the reputation of their counterparties.

As Adam Smith noted, the effectiveness of reputation mechanisms are stronger when there are a large volume of transactions. Large established firms like eBay and Amazon Marketplaces harness vast volumes of reputation data and long established protection processes. The Australian government cannot hope to bring all online sellers onto the GST system – a point made explicit by the Bill's treatment of electronic platforms as suppliers rather than the retailers that utilise them. It is inevitable that some marketplaces and retailers will remain outside the net. These are more likely to be the smaller firms whose generic characteristics raise the riskiness of Australian transactions: smaller firms are likely to have less well-developed protection and reputation mechanisms, and less established relationships with Australian purchasers. The level of foreign compliance with Australia's taxation system is likely highly correlated with compliance with other parts of Australian consumer protection law.

Foreign firms which do not sign up to the GST will, all else being equal, operate at a competitive advantage against those who do. The OECD (2015: 125) has identified that one of the risks of encouraging foreign intermediaries – such as online marketplaces - to collect consumption taxes is that doing so "may come at an additional cost that may be passed on to the purchaser". Australians purchasing online – particularly those purchasing goods online that are available at domestic Australian retailers – are likely to be highly price sensitive. The way the Bill has been structured provides an incentive for consumers to shift from large, compliant, and highly refined firms to more unprotected and riskier suppliers.

Fraud

When the GST was introduced in 2000, the then Howard government authorised extensive price surveillance powers for the ACCC to ensure that Australians were not defrauded by unscrupulous sellers hiding price increases under the guise of the new tax. The A New Tax System (Trade Practices

Amendment) Bill 1999 granted the ACCC special transitional powers to monitor prices to ensure that tax reductions and the GST had been fairly applied. As Joe Hockey, then Minister for Financial Services and Regulation, told the parliament:

> This bill is necessary to deal with those instances where price exploitation could occur. The substantial penalties that can be imposed demonstrate this government's determination to ensure that consumers receive the full benefits of the changes to the tax system. (Hockey 1998)

This was a key part of the Howard government's defence of the GST – that consumers would be well protected from fraud. Members of the government repeatedly referred to the ACCC's special responsibilities when defending the GST's introduction in parliament. For example, the Treasurer Peter Costello exhorted the public in parliament that:

> … if anybody believes that a price has been moved in a way which it should not, that matter can be reported to the ACCC, which has strong enforcement powers and which can investigate those particular matters to ensure that there is no price taking under the misleading or deceptive cover of a tax change (Costello 2000).

Between July 1999 and July 2001 the ACCC investigated 5,000 "GST-related matters" which resulted in "9 Federal Court actions, 40 court enforceable undertakings … more than 600 administrative undertakings, such as apologies refunds, corrective advertising and written undertakings refunds totalling almost $9.5 million for about 528,000 consumers" (Australian Competition and Consumer Commission 2001). The ACCC had a similar role at both the introduction of the carbon tax and again after its repeal. ACCC monitoring of major tax changes has become a standard procedure in Australian politics. However, it is not clear how the government will monitor international sellers and marketplaces in the case of the imposition of extraterritorial taxation. It is also not clear how the Australian government will monitor domestic prices that may change as a result of the lessening of domestic competition as a result of this policy change. The government should clarify whether it still considers that fraudulent activity under the cover of taxation changes is of concern, and how the legislation will deal with this risk.

Exiting the Australian market

A likely consequence of this new tax is that some electronic distribution platforms may exit the Australian market. The very large one's may well remain; but smaller second tier electronic distribution platforms – especially those that are just above or below the A$75,000 threshold – may exit the Australian market and so reduce competition among electronic distribution platforms operating in Australia.

Electronic distribution platforms are likely to have a business model that either collects a flat fee per transaction or a percentage of the purchase price of each transaction. (There may be additional features such as bulk discounts and sliding scales and the like.) This constitutes their revenue and they in turn have business costs that must be covered. Electronic distribution platforms will in turn pay the normal company tax rate on their taxable income in those jurisdictions where they are liable for company tax.

The proposed new tax, however, makes them liable for ten per cent of the sales price of their own customers trading with third parties. It is very likely that an additional ten per cent impost on the sales price of good being traded will exceed the profit margin electronic distribution platform's earn from any given transaction. The simplest solution to that situation would be for the electronic distribution platform to exit the Australian market. Alternately they would have to massively increase the prices they charge to their own consumers who deal with Australians in the hope that their own consumers can pass on the additional cost to Australian consumers. Given international competition, that prospect is somewhat unlikely.

Issues with harmonisation and international trade protectionism

The Treasurer has stated that this reform "is a significant world first, but it is consistent with the direction of international tax policy in this area. It is only a matter of time until others jurisdictions follow suit" (Commonwealth Parliamentary Debates, House of Representatives, 16 February 2017, p. 1279). It is true that the possibility of imposing a value-added tax on foreign suppliers and intermediaries, rather than imposing that tax at the border, has been canvassed by the OECD in its work on base erosion and profit shifting (OECD 2015). We do not, however, believe that the government should be so blasé about leading the world on this approach.

It is possible to imagine a situation where internet retailers all register for, comply with, and impose the domestic consumption taxes of their global customers. KPMG identify 121 jurisdictions with their own value added taxes in 2016 (KPMG 2017). Should this come about, the compliance burden on internet retailers, particularly small internet retailers, would be substantial. Tax enforcement under such a system would be near impossible, and the opportunities for arbitrage virtually limitless. The Australian government should not assume that such a global consumption tax system is inevitable, or even probable. In the short term, the OECD (2015) has warned that any implementation of any alternative to tax enforcement at the border "will need to be complemented with appropriate risk assessment and enhanced international administrative co-operation between tax authorities to enforce compliance."

The fact that the government is seeking to lead the world on this approach leaves it vulnerable to accusations – in our view, correct accusations – that the policy is being driven by protectionist sentiment rather than concerns with the viability of the Australian taxation system. The committee will be acutely aware of the political history of the push against the low value threshold. It is significant that this debate seriously begun between 2010 and 2013, when the Australian dollar was at a high against the United States dollar. In that period, the exchange rate meant that foreign retailers where highly competitive against Australian retailers.

If parliament does remove the low value threshold, however, retailers should not feel reassured. Novak (2015: 2) finds that "Putting a GST on low-value imports is unlikely to revive Australian retailing in the face of intense online shopping competition, given the significant price differentials for many popular consumer products." As outlined above, subjecting these goods to the GST does not erase the competitive advantage. Novak attributes Australia's retail disadvantage not to the low value threshold, but to our highly regulated labour market, and regulatory restrictions on retail and land use.

Nevertheless, as discussed in Section III above, a host of retailers have sought to blame their loss of market share on the Australian tax system. For example, the chief executive of Harvey Norman, Gerry Harvey, has claimed that the GST is a "huge, huge problem … If you are in retail selling those sort of goods, you are severely disadvantaged" (AAP 2010). The head of the National Retail Association has argued that the low value threshold "poses the greatest threat to traditional retail jobs and domestic online retail growth" and that if the government does not change it "the Australian retail sector will lose 33,000 jobs" (AAP 2012). A group of local retailers including Myer, David Jones, Angus and Robertson and (the now defunct) Borders argued that imposing GST on low value foreign imports would "create a level playing field where the same rules apply to everyone" (Winterford 2011).

In this context, it is highly likely that the government's policy will be challenged as a violation of Australia's free trade commitments. One of the central positions of Australian foreign policy is its desire to reduce barriers to trade and foster economic integration. This as we have seen is one of the stated purposes of the low value threshold. Eliminating this threshold – particularly in a manner as to try to impose extraterritorial taxation – is likely to bring Australia into conflict with either trading partners or foreign firms wishing to trade with Australia.

The fact is that protectionism (and populist economic policy generally) never achieves it stated aims of promoting domestic prosperity. Ultimately it results in lower living standards and higher prices. This policy will isolate Australians – both consumers and sellers – from the most effective and efficient electronic distribution platforms. In turn it will expose Australians – both consumers and producers – to the less desirable facilitators of international trade. Adding to the costs of international cannot be consistent with the current government's aim of promoting jobs and growth. In the 1970s there was a proposal known as the Tobin tax – the idea that a tax could be implemented to deliberately reduce the efficiency of foreign exchange market, in many respects this appears to be a tax introduced deliberately to reduce the efficiency of internet commerce for Australians.

V CONCLUSION: REGIME UNCERTAINTY IN AUSTRALIAN TAXATION

It is certainly the case that Australia's low value threshold is high by international standards. This should be seen as a feature rather than a bug. In countries with much lower thresholds, there is pressure to raise it. For example, Canada's globally low threshold at C$20 has been under much scrutiny in recent years (Stairs 2016). Australia's threshold might be high relative to other nations but that does not speak to the desirability of lowering it – the goal of any threshold ought to be the minimising of red tape and the facilitation of trade. Efforts to collect tax from trade should not be prioritised over the trade itself.

More fundamentally this policy increases the uncertainty that Australian firms, foreign firms operating in Australia, and firms in foreign jurisdictions trading with Australians will have about Australia's tax regime going forward. That this policy forms part of the OECD's work on base erosion and profit shifting is significant. We have argued that other policies under this umbrella – such as the diverted profits tax which passed parliament in March 2017 – have put Australia's reputation as a good international player in tax administration at risk, have been introduced contrary to the evidence about the erosion of the tax base, and will be implemented in a way that will decrease Australian competitiveness (Berg and Davidson 2017a). We see similar problems with this policy. However, such taxation changes add up to more than the sum of their parts: offering investors a picture of Australia's taxation regime as highly uncertain and confused. We recommend that the government does not proceed with the Treasury Laws Amendment (GST Low Value Goods) Bill 2017.

BIBLIOGRAPHY

AAP. 2010, 'Gerry Harvey calls for GST on online purchases'. The Sydney Morning Herald, 23 November. http://www.smh.com.au/business/gerry-harvey-calls-for-gst-on-online-purchases-20101123-1850x.html

AAP. 2012, 'Retailers call for GST on online sales'. News.com.au, 14 September. http://www.news.com.au/finance/work/retailers-call-for-gst-on-online-sales/news-story/3a84e4dbab88452dcdcdd95db6fc6172

Australian Competition & Consumer Commission. 2001, 'One year on and most businesses comply with ACCC price guidelines.' https://www.accc.gov.au/media-release/one-year-on-and-most-businesses-comply-with-accc-price-guidelines

Akerlof, GA 1970, '"The Market for Lemons": Quality Uncertainty and the Market Mechanism', Quarterly Journal of Economics, vol. 84, no. 3, pp. 488-500.

Alley, C and Bentley, D 2005, 'A Remodeling of Adam Smith's Tax Design Principles', Australian Tax Forum, vol. 20, p. 579.

Australian Taxation Office 1997, Submission to the Joint Committee of Public Accounts Inquiry into Internet Commerce, Commonwealth of Australia.

Berg, C 2015, 'Forcing GST on imports doesn't stack up', ABC The Drum, 24 August.

Berg, C and Davidson, S 2015, Submission to Treasury consultation into exposure draft of Tax Laws Amendment (Tax Integrity Multinational Anti-avoidance Law) Bill 2015, Institute of Public Affairs.

---- 2017a, 'Diverted profits tax will go nowhere'. The Australian Financial Review, 28 March.

---- 2017b, '"Stop This Greed": The Tax-Avoidance Political Campaign in the OECD and Australia', Econ Journal Watch, vol. 14, no. 1, pp. 77-102.

Board of Taxation 2010, Review of the Application of GST to cross-border transactions: A report to the Assistant Treasurer, Commonwealth of Australia, Canberra.

Chung, F 2015, 'Coalition 'selling out' to unions, retail groups in push to lower overseas online GST threshold', News.com.au, 5 January.

Commissioner of Taxation 2014-15, Australian Taxation Office Annual Report.

Costello, P 1998, 'Questions without notice: Goods and Services Tax: Price Increases', Commonwealth Parliamentary Debates, House of Representatives, 16 February 2000.

Davidson, S 2014, Multinational corporations, stateless income and tax havens, Association of Certified Chartered Accountants.

Durkin, P 2016, 'eBay's global CEO Devin Wenig tells Malcolm Turnbull to drop plans for GST on overseas online purchases', The Australian Financial Review, 4 December.

Explanatory Memorandum 2016-2017, 'Treasury Laws Amendment (GST Low Value Goods) Bill 2017', House of Representatives.

Hockey, J 1998, 'Second Reading: A New Tax System (Trade Practices Amendment) Bill 1998', Commonwealth Parliamentary Debates, House of Representatives, 10 December 1998.

Howard, J 2005, 'Letter addressed to Senator the Hon Chris Ellison', Department of Prime Minister and Cabinet, FOI Disclosure foi-2013-021. http://www.dpmc.gov.au/foi/ips/disclosure_logs/dpmc/docs/2012-13/foi-2013-021.pdf

Inspector-General of Taxation, 2015, Review into the ATO's approach to debt collection.

James, K 2015, The rise of the value-added tax, Cambridge University Press, New York, NY.

Joint Committee of Public Accounts and Audit 1998, Internet Commerce: To buy or not to buy?, Parliament of the Commonwealth of Australia.

Klein, DB 1997, Reputation: studies in the voluntary elicitation of good conduct, Economics, cognition, and society, University of Michigan Press, Ann Arbor.

Low, C and Mather, J 2015, ' Gerry Harvey urges GST on $20 imports', The Australian Financial Review, 22 July.

Makin, AJ and Pearce, J 2016, 'Fiscal Consolidation and Australia's Public Debt', Australian Journal of Public Administration, vol. 75, no. 4, pp. 424-40.

Morrison, S 2017, Second Reading: Treasury Laws Amendment (GST Low Value Goods) Bill 2017, Commonwealth Parliamentary Debates, House of Representatives, 16 February 2017.

National Advisory Council on Consumer Affairs 1998, Consumer protection in electronic commerce: principles and key issues, Department of Industry, Science and Tourism, Canberra.

Novak, M 2015, No to the GST tax attack: Why the exemption for online purchases should stay, Institute of Public Affairs.

Productivity Commission 2011, Economic Structure and Performance of the Australian Retail Industry.

Slemrod, J 2008, ‘Does it matter who writes the check to the government? The economics of tax remittance’, *National Tax Journal*, vol. 61, 251-275.

Smith, A [1776] 1976, An inquiry into the nature and causes of the wealth of nations, University of Chicago Press, Chicago.

---- 1997, 'Lecture on the Influence of Commerce on Manners', in DB Klein (ed.), Reputation: studies in the voluntary elicitation of good conduct, University of Michigan Press, Ann Arbor, pp. 17-20.

Stairs, A 2016, 'Canada’s customs threshold: out of step and out of pocket', The Globe and Mail, 23 June.

Tadelis, S 2016, 'Reputation and feedback systems in online platform markets', Annual Review of Economics, vol. 8, pp. 321-40.

Tait, A, Ebel, R and Le, T 2005, 'Value-added tax, national', In J Cordes, R Ebel and J Gravelle (eds) The Encyclopedia of Taxation and Tax Policy, The Urban Institute Press.

Webley, P, Adams, C, and Elffers, H 2006, 'Value added tax compliance', In E. McCaffery and J Slemrod (eds) Behavioral Public Finance, Russell Sage Foundation.

Winterford 2011, ‘Retailers call for GST review as online sales boom’, CRN, 4 January.

Zhang, D, Li, L, Burns, K and Davidson, S 2017, 'A test of the Kleinbard stateless income hypothesis'.

About the Authors

Chris Berg is a Postdoctoral Fellow in the School of Economics, Finance and Marketing at RMIT University. He is also a Senior Fellow at the Institute of Public Affairs and an Academic Fellow at the Australian Taxpayers' Alliance. He has written several books on economics, politics, and civil liberties and appears regularly in the media as a commentator on public affairs.

Sinclair Davidson is Professor of Institutional Economics in the School of Economics, Finance and Marketing at RMIT University, a Senior Research Fellow at the Institute of Public Affairs, and an Academic Fellow at the Australian Taxpayers' Alliance. He is a member of the Centre for Independent Studies Council of Academic Advisers. Sinclair has published in academic journals such as the European Journal of Political Economy, Journal of Economic Behavior and Organization, Economic Affairs, and The Cato Journal. He is a regular contributor to public debate.