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# SUBMISSION TO PRODUCTIVITY COMMISSION INQUIRY: COLLECTION MODELS FOR GST ON LOW VALUE IMPORTED GOODS

## Sound Policy

The Government's decision to abolish the low value threshold (LVT) for GST importations is a forward thinking, sustainable solution to GST base erosion in Australia. The international consensus on cross-border taxation is moving towards a system which extends GST/VAT liability to overseas suppliers of low value imports. This system recognises the effect globalisation is having on trade, and strengthens Australia's GST base.

## Competing Arguments

In my 2016 analysis of the impact of this policy change in Australia, I determined there were several benefits to abolishing the LVT:

1. Tax neutrality conformity
2. GST base straightening
3. Economic benefit to the Australian retail industry
4. Efficiency of tax collection

The competing arguments against this change were:

1. The case for lowering the LVT was not made out
2. Reducing the LVT would increase barriers to trade
3. Consumers would pay more
4. Foreign suppliers may not comply
5. The law might be unenforceable

My assessment of these competing factors involved an analysis of the relative strength of the arguments and the merit of supporting information. The conclusions that followed are summarised in the below table:

| Reasons in Favour of Decision | Reasons Against Decision |
|---|---|
| Tax neutrality | Consumer price increase |
| Strengthen a weakening GST base | Increased barriers to trade |
| Consistent with global taxation developments | Compliance issues |
| Effect on domestic retail industry | Enforcement issues |

Reasons in green indicate compelling arguments and reasons in blue show unpersuasive arguments.

Issues around compliance and enforcement might better be understood by examining the overseas experience in New Zealand. General compliance data collected by the ATO provides further insight. Arguably, neither compliance nor enforcement issues should be grounds for rejecting this policy decision. Enforcement activities will necessarily be difficult, and the Commission should not, as a starting point, base analysis on a necessity for comprehensive enforcement.

## Effect on the Australian Retail Industry

Of note in my findings, was that the effect of the LVT on the retail industry is wholly equivocal. Contradictory data, findings and reports from competing stakeholders best illustrate this divide. As a starting point, it is probable that the abolishment of the LVT will help reduce a price differential between Australian retail and overseas retail of between 11-23% (see attached paper). However, my research found that it is wholly unclear whether Australian retail would receive an overall benefit from the abolishment of the LVT. It is likely that certain elements within Australian retail would see tangible financial benefit, however this may be partially offset by other losses within the industry. My ultimate assessment of the impact on retail was that it did not matter in terms of a decision on whether to implement this policy.

## My View

Based on my experience researching this policy, my view is that electronic e-commerce platforms are best placed to collect GST on low value goods. Platforms such as eBay and Amazon have access to all the information required for collecting GST, and have appropriate infrastructure and systems in place to most easily adapt to the change. As was found by the OECD in its 2015 paper 'Addressing Tax in the Digital Economy', I do not think it is feasible for financial intermediaries, mail carriers or consumers to be responsible for collecting GST. The arguments against this position are well made out (see my attached paper and bibliography).

The impact of an e-commerce platform collection model on consumers is something to be carefully considered. There is a compelling argument that consumers will suffer as a result of any vendor collection model. On balance, I think the positive impact a vendor collection model will have on the GST base outweighs the loss to the consumer. The nature of tax is such that individuals will always lose when a tax is levied. Based on my research in the area, I am not convinced that the loss to consumers will be so severe as to cause any significant macro economic damage. My research tended to support the proposition that there are other reasons which dictate consumer spending habits, including factors such as convenience. My belief is that the proposed amendments will integrate well into Australian consumer spending culture, not withstanding the highly vocal views of consumer activist groups.

Regardless of the ultimate model of collection, I would suggest to the Commission that strong initial enforcement activities be recommended in the period immediately after the change takes effect (1 July 2018). Periodic compliance and enforcement campaigns would also be advisable. Such activity would likely improve net gains to Australian retail. Wide-scale publication of these enforcement activities will be crucial for educating the public and overseas suppliers. The ATO, Treasury and the Department of Immigration and Border Protection (i.e Australian Border Force) are well placed to develop an inter-departmental team to address enforcement issues.

# GST LOW VALUE THRESHOLD: DID THE GOVERNMENT MAKE THE RIGHT DECISION?

JONATHAN GONSALVES

## INTRODUCTION

The decision of the Australian Government to abolish the low value threshold (LVT) exemption for goods and services tax (GST) is a world first which will enhance Australian tax policy.[1] Extending the GST to low value imports forms the second component of reforms, following the passing of legislation in 2016 to capture GST on intangible, digital products and services (the 'Netflix tax').[2] These initiatives address long standing taxation concerns with the growth of the digital economy and cross-border transactions. Such concerns have been met by opposing arguments that removing the LVT will cause a net economic loss to Australia. Whether or not the Government made the right decision in removing the LVT is the focus of this paper.

This issue will be addressed through an objective analysis of relevant arguments and considerations. In Part I of this paper, Australia's LVT and the problem it presents will be explained. In Part II, the benefits of taxing low value goods using the method chosen by the Government will be described. Part III of this paper will detail the reasons against reduction, including issues of compliance and enforcement. Finally, in Part IV all these factors will be weighed together to determine whether the Government made the right decision.

## PART I: AUSTRALIA'S GST LVT

Australia's LVT on importations exists to exempt low value goods from GST liability, because the cost of collecting revenue would would exceed the revenue itself. The current threshold enables goods below $1,000.01 to be exempt from GST, customs duties and formal entry requirements at the border.[3] This facilitates the passing of goods through the border without labour intensive

[1] The Commonwealth of Australia, 'Budget Measures' (Budget Paper No 2 2016-17, 3 May 2016) 19; Joe Hockey, 'Statement: Council on Federal Financial Relations Tax Reform Workshop' (Media Release, 21 August 2015).

[2] *Tax and Superannuation Laws Amendment (2016 Measures No 1) Act 2016* (Cth) sch 1.

[3] See *Customs Act 1901* (Cth) s 68(1)(e)(ii); note also excludes alcohol and tobacco products: *Customs By-law No 1305011 2013* (Cth) para 4.

arrangements between the Australian Border Force (ABF), express carriers, Australia Post and Australian purchasers.[4]

### A *Legislative Operation of LVT*

In Australia, GST is payable on 'taxable supplies' and 'taxable importations'.[5] 'Non-taxable importations' are not subject to GST.[6] Goods valued below $1,000.01 are classified as 'non-taxable importations' by virtue of a complicated legislative scheme involving multiple sections of the GST Act, the Customs Tariff Act and a Customs Bylaw.[7]

### B *International LVTs*

Australia's LVT on GST is one of the highest in the world. The threshold for other developed countries is listed in Figure 1.

| **Country** | **GST or VAT** | **LVT** | **LVT in AUD[12]** |
|---|---|---|---|
| Australia | GST | AUD$1,000 | $1,000 |
| Canada | GST | CAD$20[8] | $19.90 |
| European Union | VAT | €10-22[9] | $14.59-$32.09 |
| United Kingdom | VAT | £15[10] | $25.42 |
| Singapore | GST | SGD$400[8] | $382.53 |
| New Zealand | GST | NZD$400[8] | $378.85 |
| United States | N/A (De Minimis) | USD$800[11] | $1,040.12 |

**Figure 1**

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[4] Productivity Commission, *Economic Structure and Performance of the Australian Retail Industry,* Inquiry Report No 56 (2011) 199-203; for explanation of these arrangements see Low Value Parcel Processing Taskforce (LVPPT), 'Final Report' (July 2012) 55-86; see also CAPEC, Submission No DR156 to Productivity Commission, *Economic Structure and Performance of the Australian Retail Industry,* 20 May 2011, app 1; purchasers refers to Consumers and businesses who may be entitled to input tax credits.

[5] *A New Tax System (Goods and Services Tax) Act 1999* (Cth) s 7-1.

[6] Ibid s 7-1, 13-5, 13-10.

[7] Ibid s 7-1, 13-10, 42-5; *Customs Tariff Act 1995* (Cth) sch 4, item 26; *Customs By-law No 1305011 2013* (Cth). This scheme tethers the LVT on GST to the 'de minimis'. 'De minimis' refers to the low value threshold below which customs duties are not payable; See *Customs Tariff Act 1995* (Cth) sch 4, item 26; *Customs By-law No 1305011 2013* (Cth). The legislative link between these two LVTs would likely be severed regardless of any changes to the GST LVT: see Commonwealth Government, 'Response to Low Value Parcel Processing Taskforce's Recommendations' (Government Response, 3 December 2012) recommendation 3.3.

The European Union and United Kingdom have both considered lowering or abolishing their thresholds.[13] This position represents a growing global consensus that the LVT on importations should be abolished, to recognise the growth of low value imports as part of the digital economy.[14] In particular, the EU looks likely to abolish the LVT in line with its Digital Single Market Strategy.[15] This view is contested by some in the EU who believe the EU LVT should be raised.[16] The argument put forth is that the current EU LVT costs more than it collects; with quantitative analysis revealing a threshold of €80 to be the most efficient.[17] Such a change is said to be consistent with US policy, where the de minimis threshold was increased in 2016 from $200 to $800.[18] However, whether the Australian LVT should be raised, not lowered, is outside the scope of this paper.

### C *The Problem with the LVT*

There are two main issues with the operation of the LVT in Australia:

1. GST base erosion;
2. The burden on Australian retail.

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[8]; Global Express Association (GEA), *Overview of De Minimis Value Regimes Open to Express Shipments World Wide (*April 2016) Global Express <http://www.global-express.org/assets/files/Customs%20Committee/de-minimis/GEA-overview-on-de-minimis_April-2016.pdf>.

[9] See Council Directive 2009/132/EC (European Union) European Commission, art 23;
Ernst and Young, 'Assessment of the Application and Impact of the VAT Exemption For Importation of Small Consignments' (Final Report, European Commission, May 2015) 7-9; most EU member nations maintain a threshold of €22.

[10] *Value Added Tax (Imported Goods) Relief Order 1984* (UK) c 746, sch 2, pt 8, item 8.

[11] Trade Facilitation and Trade Enforcement Act of 2015, USC 1907 (2016); see also US Customs and Border Protection (CPB), 'De Minimis Value Increases to $800' (Media Release, 11 March 2016).

[12] Using exchange rates on 30 September 2016.

[13]See, eg, Jason Gorringe, *UK Considering Future of LVCR VAT Concession* (09 August 2011) Global Incorporation Guide <http://www.lowtax.net/g/news/UK_Considering_Future_Of_LVCR_VAT_Concession____50809.html>; Commission Expert Group On Taxation of the Digital Economy, 'Report' (Report, European Commission, 28 May 2014) 38-39.

[14] See, eg, OECD/G20 Base Erosion and Profit Shifting Project, 'Addressing the Tax Challenges of the Digital Economy, Action 1- 2015' (Final Report, OECD, 5 October 2015).

[15] European Commission Staff, 'A Digital Single Market Strategy for Europe - Analysis and Evidence' (Working Document, European Commission 6 May 2015) 31-33.

[16] Hintsa J et al, 'The Import VAT and Duty De-Minimis In the European Union - Where Should They Be and What Will Be the Impact?' (Final Report, Cross-border Research Association, 14 October 2014). Note that the LVT in Europe is known as Low Value Consignment Relief (LVCR).

[17] Ibid 44.

[18] CBP above, n 11; note that the US de minimis is the threshold for customs duties, not for a value added tax or GST.

### 1 *GST Base Erosion*

Australia's GST base is subject to erosion as the Government does not collect revenue on an increasingly large number of low value imports.[19] This is occurring because of the growth in international retail and imported goods. Most of these goods are priced below $1,000, and are not subject to GST.[20] The increasing interconnectedness of the world caused by globalisation is likely to result in a growing number of overseas imports, causing levels of GST base erosion to rise.

### 2 *Australian Retail Burden*

The Australian retail industry is burdened by the lack of tax neutrality, caused by the fact that international importers are not required to charge GST. Local suppliers have suffered from negative tax assistance from the LVT, which has converted an indirect tax on consumers (GST) into a direct tax on producers, who must absorb the cost of the GST in order to remain competitive with international retail.[21] This unintended tax equates to the price differential between domestic and international retailers caused by GST, estimated at 11-23%.[22] The result is reduction in turnover, profitability and employment for domestic retail, in addition to lost GDP.[23] These consequences have incentivised domestic suppliers to relocate offshore, whilst simultaneously discouraging investment in Australian retail.[24] Refer to Appendix B for an example of the distortion the LVT can cause on retail.

## D *Abolishing LVT in Australia*

The Australian Government has decided to abolish the LVT so that all imports entering the country from 1 July 2017 will be subject to GST. Legislatively, this will occur by the amendment of s 42-5

[19] See LVPPT, above n 4, ch 2; Explanatory Memorandum, Tax and Superannuation Laws Amendment (2016 Measures No. 1) Bill 2016 (Cth) 3.

[20] LVPPT, above n 4, ch 2.

[21] Productivity Commission, above n 4, 188; Ernst and Young, 'The Threshold Question: Economic Impact of the Low Value Threshold on the Retail Industry' (Report, Ernst and Young, 22 February 2012) 38; see also Appendix B.

[22] Ernst and Young, *The Threshold Question* above n 21, 22.

[23] See Productivity Commission, above n 4, 191-193; National Retail Association (NRA), Submission No 18 to Productivity Commission, *Cost of Doing Business: Retail Trade Industry*, May 2014, 4-6; Ernst and Young, *The Threshold Question* above n 21, 18, 30-31; OECD, *Addressing the Tax Challenges of the Digital Economy*, above n 14, 120-122; Australian National Retailers Association (ANRA), Submission No 16 to Productivity Commission, *Cost of Doing Business: Retail Trade Industry*, May 2014, 17-18.

[24] OECD, *Addressing the Tax Challenges of the Digital Economy,* above n 14, 182; Ernst and Young, *The Threshold Question*, above n 21, 18.

of the GST Act;[25] to remove reference to item 26 of Schedule 4 of the Customs Tariff Act.[26] This will result in low value goods no longer being 'non taxable importations', and thus subject to GST. Further to this change, the Government appears to be modifying the GST Act such that imports to Australian consumers valued under $1,000.01 will become 'taxable supplies'. Liability for collection of GST will accrue to overseas suppliers with a turnover in excess of $75,000.[27] Overseas suppliers importing goods into Australia will be liable to collect and remit GST to the ATO on all importations under $1,000.01. Operators of electronic e-commerce platforms are also likely to be substituted for suppliers for the collection and remittance of GST, in congruence with the 'Netflix tax' changes.[28]

## PART II BENEFITS OF ABOLISHING LVT

There are four key benefits of the Government's plan to abolish the LVT and require overseas suppliers or e-commerce platforms to collect and remit GST:

1. Tax neutrality conformity;
2. GST base strengthening;
3. Economic benefit to Retail industry;
4. Efficiency of tax collection.

### A *Tax Neutrality Conformity*

The abolition of the LVT will result in uniform taxation treatment for all goods acquired by Australian consumers. A consistent policy increases the simplicity of Australia's taxation system, reduces the administrative burden of businesses and prevents competitive distortions in markets. This result is consistent with the taxation principles of fairness, equity and neutrality.

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[25] *A New Tax System (Goods and Services Tax) Act 1999* (Cth).

[26] This will also have the effect of separating the customs duty threshold (de minimis) from the GST LVT, unwinding the path dependency problem preventing efficient changes to both thresholds.

[27] See CIE, 'The Economic Impacts of Changing Arrangements for the Importation of Low Value Products' (Final Report, Centre of International Economics, February 2016) 4-6; The Commonwealth of Australia, above n 1, 19; Joe Hockey, *Statement: Council on Federal Financial Relations Tax Reform Workshop*, above n 1.

[28] Under the Netflix tax changes, operators of e-commerce platforms will be liable instead of suppliers for GST on intangibles where certain conditions are met. Shifting liability to operators for low value goods is implied by the words of the treasurer, and treasury officials who have indicated the changes to LVT will be structured similarly to the 'Netflix tax'; see Joe Hockey, *Statement: Council on Federal Financial Relations Tax Reform Workshop*, above n 1; *Tax and Superannuation Laws Amendment (2016 Measures No 1) Act 2016* (Cth) sch 1; CIE, *The Economic Impacts of Changing Arrangements for the Importation of Low Value Products* above, n 27, 4-5; Interview with Christopher Lyon, Manager of Indirect Taxes at Commonwealth Department of Treasury (Phone interview, 29 August 2016).

## B *GST Base Strengthening*

Applying GST to low value imports recognises the growth of the digital economy as a source of consumer goods.[29] The revenue to be collected by taxing low value imports, estimated at between \$300m-\$427m over 3 years, will strengthen Australia's taxation base and benefit State Governments who receive such revenue.[30] The historical rationale for permitting GST base erosion was that lowering the LVT would be cost prohibitive because of the expensive labour intensive operations required at the border.[31] The Government's decision to implement a 'non-resident supplier collection' model removes this obstacle. This outcome demonstrates flexibility and growth, which is vital for ensuring the future integrity of the tax system.

## C *Economic Benefit to Retail*

Removing the LVT may result in significant economic benefit to the Australian retail industry. Australian retailers argue it will reverse some of the losses mentioned in Part I, including increasing turnover and employment.[32] The net effect is said to be an increase in GDP by up to \$6.5 billion by 2021.[33] Abolishing this exemption will place domestic retail on an even taxation playing field with international retailers, promoting investment and sustainability in Australian retail.

## D *Efficiency of Tax Collection*

One of the key benefits of the Government's method for lowering the LVT is the efficiency with which tax will be collected. Under the overseas supplier collection model, tax will be collected by overseas suppliers instead of at the border by Customs.[34] This method is efficient because it is less labour intensive, avoids expensive capital investments, requires no changes to current border

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[29] CIE, *The Economic Impacts of Changing Arrangements for the Importation of Low Value Products,* above n 27, 18-19.

[30] GST Distribution Review, 'Final Report' (Final Report, The Australian Government, October 2012) 158-161; Estimates of the revenue collected prior to 2015 are unreliable as most are based on the assumption that revenue would be collected at the border. The range of estimates given above are provided by the Commonwealth Treasury (\$300m) and CIE (\$427m); The Commonwealth of Australia, above n 1, 19; CIE, *The Economic Impacts of Changing Arrangements for the Importation of Low Value Products,* above n 27, 38; note that The Treasury estimates revenue foregone in 2015-16 alone of \$430m, see The Treasury, 'Tax Expenditure Statement 2015' (Statement, Department of the Treasury, January 2016) 110.

[31] See Productivity commission, above n 4, 210-214; 'Simply changing the threshold while leaving all else the same creates substantial difficulties in terms of cost effectiveness and efficiency:' LVPPT, above n 4, 2-3.

[32] ANRA, above n 23, 4-6; Ernst and Young, *The Threshold Question* above n 22, 24, 30-34.

[33] Ernst and Young, *The Threshold Question* above n 21, 3.

[34] The Commonwealth of Australia, above n 1, 19; Joe Hockey, *Statement: Council on Federal Financial Relations Tax Reform Workshop*, above n 1. Customs refers to the Australian Border Force under the Department of Immigration and Border Protection, formerly the Australian Customs and Border Protection Service.

processes[35] and enables consumers to incorporate GST into purchase decisions.[36] Moreover, it is ideal to require vendors to collect GST because they possess information about the goods being imported, jurisdictions and postal codes.[37] The substitution of liability to e-commerce operators will further increase efficiency by reducing the number of entities needing to comply.

On a macro view of tax policy, the increase in indirect taxation revenue caused by reducing the LVT will be preferable for economic growth, as indirect taxes favour savings and investment, whilst having less impact on businesses.[38] Expanding GST liability will bring Government revenue from indirect tax closer to the OECD average of 12% from the current 7%.[39] Requiring non-resident suppliers to remit GST embraces globalisation, following the global trend of connecting economies by increasing taxation cooperation between States. This trend is evidenced by the EU's expansion of the Mini One Stop Shop, whereby non-EU importers register and remit for VAT in only one member state, instead of having to comply with the law of every member state.[40] Requiring overseas suppliers to remit and pay tax is evidence of Australian law adapting to international taxation developments.

## PART III REASONS NOT TO ABOLISH LVT

The Government's decision to remove the LVT has been heavily criticised on the basis of five main arguments:

1. The case for lowering the LVT is not made out;
2. Abolishing the LVT increases barriers to trade;
3. Consumers will pay more;
4. Foreign suppliers may not comply;
5. The law may not be enforceable.

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[35] These are the reform considerations of the LVVPT; LVPPT, above n 4, 165.

[36] LVPPT, above n 4, 216.

[37] OECD, *Addressing the Tax Challenges of the Digital Economy,* above n 14,198; this can be contrasted with a model whereby financial intermediaries collect GST as they lack information about goods being imported.

[38] OECD, 'Economic Survey of Australia 2014' (Report, OECD, 2014) 60.

[39] Ibid 61.

[40] Commission Expert Group On Taxation of the Digital Economy, above n 13, 37-40.

## A *Case Not Made Out*

The process which successive Governments have followed to reach the decision to abolish the LVT has involved several attempts to establish a business case to justify the change. Appendix C illustrates this process.

Based on various reviews undertaken since 2009, a number of concerns have arisen about whether a business case has been made out to lower the LVT. The core of these concerns is that reducing the LVT will not be as beneficial to domestic retail as claimed by Australian retail associations.[41] According to widely corroborated research by the consumer group Choice, consumers buy from overseas retailers for convenience more than price.[42] If accepted as fact, this would suggest reducing or abolishing the LVT will not result in an increase in domestic retail market share, and all the corresponding benefits to turnover, employment and GDP. Rather, GDP might decrease instead.[43] Furthermore, some research suggests employment isn't decreasing as a result of international retail; that the internet in general is a net job creator.[44] Contrary to analysis conducted in 2011 for the Productivity Commission, the domestic market share of online retail has increased, boosting retail employment.[45] These factors indicate that lowering the LVT might be less beneficial to Australian retail then initially thought.

## B *Increased Barriers to Trade*

One of the unavoidable consequences of requiring foreign retailers to collect GST is the additional administrative and compliance burden that will be placed on overseas suppliers. In addition to having to implement systems to collect GST from consumers,[46] non-resident suppliers will need to know to collect GST on some goods, but not others. In particular, GST exempt goods and goods

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[41] CIE, 'The GST Threshold For Low Value Products' (Economic Analysis, Centre for International Economics, May 2011); CIE, *The Economic Impacts of Changing Arrangements for the Importation of Low Value Products* above n 27; Kathrin Bain and Dale Boccabella, 'GST and Low-value Imports' (Paper presented at the 28th Annual GST Conference, Brisbane, 28 April 2016) 8.

[42] See Allen Consulting Group on behalf of eBay, Submission No 101 to Productivity Commission, *Economic Structure and Performance of the Australian Retail Industry,* June 2011, 7; Australian Communications and Media Authority, 'Australia in the Digital Economy: Consumer Engagement in E-Commerce' (Research Report, November 2010) 19.

[43] See Allen Consulting Group, above n 42, 42-43.

[44] Ibid 14; Choice, Submission to The Treasury, *Re: Think Tax Discussion Paper,* June 2015, 16.

[45] National Australia Bank, 'NAB Online Retail Sales Index: In-depth Report - June' (Monthly Report, NAB, 3 August 2016); Australian Bureau of Statistics, 'Labour Force, Australia, Detailed, Quarterly, Aug 2016' (ABS, 22 September 2016) table 04.

[46] Overseas suppliers would need to implement business and ICT systems to identify Australian Consumers and whether GST needs to be collected.

above $1,000 would not require collection and remittance, whilst GST would be collected on low value, non-exempt goods.[47] Furthermore, as GST applies only to Australian consumers, there exists the problem of identifying when goods are being consumed by Australian residents. These burdens represent an increased barrier to trade with Australia.

### C *Consumer Price Increases*

One of the most compelling reasons not to remove the LVT is because doing so will increase the cost of goods from overseas retailers. The value of GST remitted by non-resident suppliers will likely be passed on to Australian consumers via increased prices.[48] The extent of this increase in price has been estimated by the Centre for International Economics (CIE) at 9% based on the average rate of GST on goods.[49] If this were to occur, there would be an incentive for Australian consumers to misrepresent their residency in order to avoid a higher price.[50] A 2016 report by the CIE conducted a quantitative analysis of the effects of abolishing the LVT, concluding that the increased price to consumers will result in a net welfare loss of $2m-$28.9m between 2017-2020.[51] Not withstanding some important limitations with this analysis,[52] it indicates that removing the LVT is a poor economic choice which will be detrimental to Australian consumers.

### D *Will Foreign Suppliers Comply?*

Requiring non-resident suppliers of goods to charge and remit GST to the ATO presents a significant compliance risk. This risk is that overseas vendors will disregard the law because they are not physically located within Australia's jurisdiction. Not withstanding this risk, experienced taxation practitioner Michael Evans, writing on behalf of the GST Distribution Review, found that large regular suppliers of goods are likely to comply.[53]

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[47] The list of exemptions for GST is extensive, see *A New Tax System (Goods and Services Tax) Act 1999* (Cth) Ch 3, pt 3-1.

[48] CIE, *The GST Threshold For Low Value Product*s, above n 41, 21; CIE, *The Economic Impacts of Changing Arrangements for the Importation of Low Value Products* above n 27, 28-38.

[49] CIE, *The Economic Impacts of Changing Arrangements for the Importation of Low Value Products* above n 27, 36.

[50] The risk posed by Australian consumers misrepresenting residency is discussed and addressed in Explanatory Memorandum, Tax and Superannuation Laws Amendment (2016 Measures No. 1) Bill 2016 (Cth) 25.

[51] CIE, *The Economic Impacts of Changing Arrangements for the Importation of Low Value Products* above n 27, 40, 42-43.

[52] See Appendix D.

[53] Michael Evans, 'Options for GST Taxation of Imported Goods and Services' (Report, GST Distribution Review, January 2012) 12; CIE, *The Economic Impacts of Changing Arrangements for the Importation of Low Value Products* above n 28, 10.

> 'The clear theme, in my view, is that the offshore suppliers, whilst preferring not to incur the compliance costs of registration and reporting, will respond to gentle persuasion and simple compliance regimes.'

Large organisations such as Amazon will likely be compliant where tax obligations are clear, because it is generally within the interests of such organisations to be seen as good 'corporate citizens.'[54] To support a corporate desire to comply, a simplified registration and compliance regime could be adopted to further decrease administrative burden.[55] This regime would undoubtedly match the simplified requirements implemented in the 2016 Australian 'Netflix tax'.[56]

### E *Can the Law be Enforced?*

Enforcing Australian GST law on overseas retailers is a significant challenge for the ATO. It will be time consuming and costly to identify foreign suppliers who meet the $75,000 threshold but choose not to comply with the law.[57] Even when these importers are identified, it may be difficult to determine if GST has been collected by the supplier but not remitted to the ATO.[58] For half of low value imports, this task will be aided by pre-arrival information collected by express carriers.[59] By contrast, there is a lack of any pre-arrival information for 50% of low value goods in the international mail stream, rendering it economically infeasible to enforce the law. The manual labour processes that would be required to check these goods renders enforcement cost prohibitive, as was initially the issue with lowering the LVT.[60] Although changes to pre-arrival information may be coming to international mail in the near future,[61] as it currently stands, it is not cost effective to enforce abolishing the LVT in the international mail stream.

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[54] CIE, *The Economic Impacts of Changing Arrangements for the Importation of Low Value Products* above n 27, 10.

[55] See OECD, *Addressing the Tax Challenges of the Digital Economy*, above n 14, 199-201

[56] See Explanatory Memorandum, Tax and Superannuation Laws Amendment (2016 Measures No. 1) Bill 2016 (Cth) 46-47.

[57] CIE, *The Economic Impacts of Changing Arrangements for the Importation of Low Value Products* above n 27, 12.

[58] LVPPT, above n 4, 141; refers to air and sea cargo stream imports. See Appendix A.

[59] For an explanation of the different mail streams see Appendix A.

[60] See Productivity Commission, above n 4, 214.

[61] Productivity Commission, above n 4, 207; LVPPT, above n 4, 46-48, OECD, *Addressing the Tax Challenges of the Digital Economy*, above n 14, 114, 119, 213.

Where recalcitrant suppliers are identified, the likely method for enforcing GST law is the use of tax treaties.[62] The problem with these treaties is well articulated by Professor Dale Boccabella and Katherine Bain in their submission to the 28th GST Conference in 2016.[63] This paper explains how the tax treaties purported to be relied on by the Government are complex, expensive and rarely used in practice.[64] The practical realities of international law seem to indicate tax treaties will be an ineffective tool to enforce Australian GST law on non-resident suppliers.

## PART IV DID THE GOVERNMENT MAKE THE RIGHT DECISION?

The decision to abolish the LVT was challenging because there are almost equally weighted reasons for and against change. The weight of the competing arguments are displayed below.

| Reasons in Favour of Decision | Reasons Against Decision |
|---|---|
| Tax neutrality | Consumer price increase |
| Strengthen a weakening GST base | Increased barriers to trade |
| Consistent with global taxation developments | Compliance issues |
| Effect on domestic retail industry | Enforcement issues |

Reasons in green indicate compelling arguments and reasons in blue show unpersuasive arguments.

**Figure 2**

### A *Unpersuasive Reasons Against Decision*

1 *Increased Barriers to Trade*

The increased barrier to trade, caused by requiring overseas suppliers to charge and remit GST, is not a compelling reason against this decision. Although there will be a burden on these suppliers to learn Australian GST law, it does not justify ignoring the long-term loss to Australia's GST base, and tax neutrality caused by the LVT. Implementing new taxes will always increase a taxpayer's burden because of the very nature of taxation. A new tax should not be avoided merely because an

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[62] Christopher Lyon, above n 28; see also Kathrin Bain and Dale Boccabella, *GST and Low-value Imports*, above n 41, 14; see *Convention on Mutual Administrative Assistance in Tax Matters*, open for signature 25 January 1988, [2012] ATS 38 (entered into force 1 December 2012); see, eg, *Convention Between Australia and New Zealand for the Avoidance of Double Taxation With Respect to Taxes on Income and Fringe Benefits and the Prevention of Fiscal Evasion*, signed 26 June 2009, [2010] ATS 10 (entered into force 19 March 2010), art 27; see also Wolters Kluwer, *Table of Australia's Taxation Treaties* (2016) Wolters Kluwer <http://www.iknow.cch.com.au/document/atagUio2009340sl349163133/table-of-australia-s-tax-treaties>.

[63] Kathrin Bain and Dale Boccabella, *GST and Low-value Imports*, above n 41.

[64] See also CIE, *The Economic Impacts of Changing Arrangements for the Importation of Low Value Products* above n 27, 51; see also Kathrin Bain and Dale Boccabella, 'Removal of the GST Low Value Threshold: Analysis of Main Design Options and Enforcement' (2015) 2(9) *Australian Tax Law Bulletin* 172, 175.

obligation will be created.[65] For a taxpayer's burden to justify not implementing a tax, it should be of such considerable weight that it is oppressive or causes a net economic loss.

The burden on overseas suppliers caused by the Government's decision cannot be considered oppressive. There is also no evidence to suggest it will reduce trade to such an extent as to cost the Australian economy. Although there is an added barrier, it is not strong enough to evidence the Government's decision was unsound. Moreover, given the increasing global shift towards taxation of non-residents, it is likely that this barrier will weaken as such taxation becomes more commonplace.

2 *Compliance*

The issue of whether non-residents will comply with GST obligations is a challenge that is not insurmountable. Requiring foreign suppliers to charge and remit GST is becoming a global taxation standard. A vendor registration system already exists in the EU for the payment of VAT;[66] and OECD countries are shifting towards systems that can apply consumption taxes to cross border supplies.[67] Large companies will be further incentivised to be compliant with Australian standards if they are adopted in other jurisdictions where they operate. The real challenge to compliance will be whether smaller importers choose to register and comply.[68] However, even these importers can be encouraged to comply with appropriate incentives. This might include reducing delays at the border through a 'fast track' scheme that expedites packages through Customs.[69] Another incentive might be to reduce fees on high value imports subject to customs fees and duties.[70] The availability of such options indicates that the risk to compliance can be mitigated.

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[65] There must be a balance between the conflicting policy of taxing goods acquired from outside Australia with imposing unnecessary costs on non-residents: Board of Taxation 'Review of the Application of GST to Cross-Border Transactions' (Report, The Board of Taxation, February 2010) 5.

[66]CIE, *The Economic Impacts of Changing Arrangements for the Importation of Low Value Products* above n 27, 14-15; European Commission, *A Digital Single Market Strategy for Europe*, above n 15, 32-33.

[67] See CIE, *The Economic Impacts of Changing Arrangements for the Importation of Low Value Products* above n 27, 14-15; LVPPT, above n 4, 216.

[68] CIE, *The Economic Impacts of Changing Arrangements for the Importation of Low Value Products* above n 27, 10.

[69] LVPPT, above n 4, 141; OECD, *Addressing the Tax Challenges of the Digital Economy*, above n 14, 200-201.

[70] Full Import Declaration (FID) fees could be lowered; see also LVPPT, above n 4, 163.

3 *Enforcement*

*(a) International Mail*

The fact that half of low value imports cannot be reliably evaluated for GST compliance poses a serious problem. Not withstanding this, the body responsible for regulating international mail is developing new processes and systems so that more information is available about goods entering the country.[71] These changes are likely to provide tax authorities with comprehensive information; to better identify non-resident suppliers who are avoiding GST. In the long-term, this will likely facilitate a more effective enforcement regime for international mail.

*(b) Taxation Treaties*

Even though these changes cannot be easily legally enforced through taxation treaties, enforcement options are available to ensure compliance. An alternative approach might be to utilise non-legal enforcement measures. Actions include using the Commonwealth's telecommunication power to block websites of non-complying foreign retailers,[72] reverting to 'backup' collection at the border and modifying the Tax Administration Act[73] so that the ATO can make claims against goods delivered to Australian consumers.[74] Of these options, it seems highly unlikely that the Government will exercise its power to block websites, as it is rife with controversy.[75] Utilising 'backup' taxation at the border might be effective where specific retailers are identified, although would potentially be cost prohibitive.[76] Enabling the ATO to secure GST liability against goods destined to Australians is a more feasible enforcement tool that might incentivise foreign retailers to comply. Arguably, the fact that the law cannot be enforced is not fatal to the Government's decision.

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[71] This body is called the Universal Postal Union. Productivity Commission, above n 4, 207; LVPPT, above n 4, 46-48, OECD, *Addressing the Tax Challenges of the Digital Economy*, above n 14, 114, 119, 213; see also UPU, 'Doha Postal Strategy: The Global Roadmap for Postal Services' (Strategic Plan, Universal Postal Union, 2012).

[72] See Zoya Sheftalovich, *Our Way or the Firewall*, (12 September 2016) Choice <https://www.choice.com.au/shopping/online-shopping/buying-online/articles/gst-overseas-website-block>.

[73] *Tax Administration Act 1953* (Cth).

[74] See Michael Evans, above n 53, 55; note also that the Government can utilise criminal offences to enforce consumers who misrepresent residency: Explanatory Memorandum, Tax and Superannuation Laws Amendment (2016 Measures No. 1) Bill 2016 (Cth) 25.

[75] See, eg, Zoya Sheftalovich, above n 72; Corinne Reichert, *ATO Unlikely to Block Websites That Don't Charge GST: Treasurer* (13 September 2016) ZDNet <http://www.zdnet.com/article/ato-unlikely-to-block-websites-that-dont-charge-gst-treasurer/>.

[76] Collecting tax at the border creates the same cost prohibitive problem as found by the Productivity Commission in 2011; Productivity Commission, above n 4.

### 4 *Equivocality of Retail Argument*

Although the LVT debate originated from the retail industry, it seems apparent that there is conflicting evidence on the effect that abolishing the LVT will have on Australian retail. This discrepancy is best highlighted by the contradiction between: a) Ernst and Young's 2012 prediction that domestic retail's online market share would drop from 65% to 35% by 2021; and b) the NAB online retail sales index showing increases in domestic online market share to 81% in 2016.[77] This is further highlighted by the contradictory arguments seen in Parts II and III of this paper. Not withstanding this inconsistency, it remains likely there would be net benefits to Australian retail caused by enhanced tax neutrality. Universal application of GST serves to level the taxation playing field, and removes an unfair price differential of 11-23%. However, the true weight of this benefit is wholly unclear, and requires further analysis.

## B *Comparative Analysis of Compelling Reasons*

The key question for assessing the Government's decision, is whether the benefit to tax policy, caused by enhanced neutrality, a strengthened GST base and consistency with global change, outweighs the cost to consumers. In economic terms, there is a clear loss to consumers, who will have to pay more for imported goods. This loss is offset against by an increase in revenue for the Government from a strengthened GST base. Assessing which of these stakeholders should prevail is an inherently difficult task because the Government is itself a representative of consumers. Even if the Government were to collect substantially more revenue than consumers would pay in higher prices, the loss to consumers could still be high enough to justify retaining the LVT.

Arguably, the policy value of applying GST liability to non-resident importers of low value goods outweighs the cost to consumers. Although Australians will pay more for low value imported goods, this outcome is not dissimilar to closing a tax loophole that was initially put in place arbitrarily.[78] The LVT was implemented to avoid a net loss on collection of GST from low value goods. Given this issue can be resolved by requiring foreign retailers to charge and remit GST, the justification no longer holds any merit. Consumers have enjoyed a tax break throughout the period the LVT has

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77 National Australia Bank, 'Online Retail Sales Index: In depth report January 2010 - January 2012' (Report, NAB, 31 January 2012).

78 See also Shopping Centre Council of Australia, Submission No 106 to Productivity Commission, *Economic Structure and Performance of the Australian Retail Industry,* 8 June 2011, 8.

operated. Removing this exemption reinstates the full amount of tax that should have initially been payable.

Looking outside the confines of economic terms, there is a clear, long-term benefit to Australian taxation policy caused by enhanced neutrality and international taxation conformity. Maintaining neutrality is an important taxation principle, because it expounds fairness to taxpayers. Even if it cannot be shown that the retail industry will benefit from removing the LVT, it is apparent that competitive distortions are caused by the LVT. Experience in the UK and Denmark illustrates the effect that such an exemption can have on retail markets.[79] Adapting tax policy to stop the potential for such distortions is a forward thinking, sustainable, solution. That the international consensus on cross-border taxation is moving in the same direction demonstrates a fundamental shift in approach. Globalisation is leading to the redundancy of taxation at the border, as digital technology facilitates a network of global taxation. The Australian Government's decision to embrace this change, by making Australia the first country to apply GST/VAT liability to non-resident suppliers of low value goods, will likely pave the way for future international developments.

## PART V CONCLUSION

The Government's decision to abolish the LVT on GST imports, and require overseas suppliers to collect GST, is the right way forward for Australia. There is a clear problem with the current threshold in Australia, resulting in GST base erosion and a lack of neutrality for the domestic retail industry. Although there will be a cost to consumers, these costs are arguably outweighed by the long-term benefit to Australia's taxation policy. Ultimately, making a decision to address the problems caused by the LVT is better then no action at all.

[79] See Appendix B.

# APPENDIX A - METHODS OF ENTRY FOR IMPORTS

Goods can enter the country through three separate streams: international mail, air cargo and sea cargo.[80] The international mail stream comprises 50% of the value of low value goods and is managed by Australia Post, without the assistance of an express carrier.[81] An important limitation on the efficiency of this stream is that information about these goods is only acquired by the ABF when the goods arrive in the country.[82] The air and sea cargo streams (comprising the other 50% of the value of low value goods) are managed by express carrier services such as DHL and TNT. The majority of these consignments are by air cargo.[83] These streams benefit from more detailed pre-arrival information digitally communicated to the ABF.[84]

[80] Productivity Commission above n 4, 182-185.

[81] CIE, *The GST Threshold For Low Value Product*s, above n 41*,* 12, Figure 2.4; see also CAPEC, above n 4, 23.

[82] LVPPT, above n 4, 68-71.

[83] CIE, *The GST Threshold For Low Value Product*s, above n 41, 12.

[84] LVPPT, above n 4, 44, 62-64.

## APPENDIX B - COMPETITIVE DISTORTIONS OVERSEAS

Examples of the competitive distortions caused by the LVT has been seen in the Denmark and the UK.In Denmark, the LVT was exploited by magazine producers who re-routed magazines initially printed in the EU, through non-EU territories to avoid VAT on the sale to EU consumers. This resulted in a 300% increase in non-EU magazine imports compared to the average 5%. To rectify this, Denmark removed the LVT on magazines printed in the EU and subsequently imported through non-EU territories. When magazine companies relocated production to non-EU states, Danish parliament was forced to abolish the LVT on all Danish language magazines.[85]

In the UK, the LVT was abolished for all goods from the Channel Islands.[86] This occurred because of the widespread use of the Channel Islands as a base for importing goods into the UK for the express purpose of benefiting from the LVT. The distortion caused by this exploitation resulted in a 32% contraction in the CD/DVD/Games industry in the UK. To rectify this, the LVT was abolished on imports from the Channel Islands, resulting in £95 million in additional revenue and a 78% reduction in imports from the Channel Islands.[87] Arguably, this will simply cause those companies formerly in the Channel Islands to relocate to other non-UK territories.

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[85] Ernst and Young, *Assessment of the Application and Impact of the VAT Exemption For Importation of Small Consignments* above n 9, 55-56, 60-69.

[86] Ibid; *Finance Act 2012* (UK) s 199.

[87] Ernst and Young, *Assessment of the Application and Impact of the VAT Exemption For Importation of Small Consignments* above n 9, 65.

# APPENDIX C - HISTORY OF LVT ACTION

| Date | Action Undertaken | Result of Action |
|---|---|---|
| **12 May 2009** | Government response to Board of Taxation report: *Review of the legal framework of the administration of the GST* | Requests the Board of Taxation to review, among other things, 'the impact of the current-cross border provisions on the international competitiveness of Australian enterprise.'[88] |
| **February 2010** | Board of Taxation report: *Review of the Application of GST to Cross-Border Transactions* | Concludes it is not administratively feasible to lower LVT because it is cost prohibitive. |
| **November 2011** | Productivity Commission Inquiry Report: *Economic Structure and Performance of the Australian Retail Industry* | Strong in-principle grounds for removing LVT but currently cost prohibitive. |
| **9 December 2011** | Government response to the Productivity Commission Report (above) | Government established Low Value Parcel Processing Taskforce to investigate reform.[89] |
| **January 2012** | GST Distribution Review report: *Options for GST taxation of imported goods and services* | Recommends applying GST liability to overseas suppliers, |
| **July 2012** | Low Value Parcel Processing Taskforce (LVPPT) Final Report | Concluded net economic cost to lower threshold using current border processes. Proposed several reform alternatives including requiring overseas suppliers to collect GST |
| **October 2012** | GST Distribution Review Final Report | Recommends lowering LVT. |
| **3 December 2012** | Government response to the LVPPT Final Report. | Agreed in principle to requiring overseas suppliers to charge GST and requested further work to develop a business case for lowering LVT. |
| **January 2013** | The Low Value Threshold Inter-Departmentsl Committee (IDC) created involving Customs, ATO and Treasury to develop a business case for reducing LVT.[90] | |
| **27 November 2013** | Business case developed by IDC presented to state and Federal treasurer at COAG Standing Council on Federal Financial Relations.[91] | State and Federal treasurers working group announced.[92] |
| **19 September 2014** | Meeting of treasurers during G20.[93] | No agreement on approach to GST. |
| **21 August 2015** | Meeting of treasurers at COAG Council of Federal Financial Relations Reform Workshop.[94] | Agreement in principle to abolish LVT. |
| **3 May 2016** | Federal Budget 2016-17 announced. | Decision to abolish LVT and require overseas suppliers to charge GST. |

# Appendix D - Limitations Of CIE Analysis

It must be noted that there are two key limitations with regard to the CIE's analysis.[95] Firstly, the data used for this was based on data from the Conference on Asia Pacific Express Carriers (CAPEC), who are responsible for 50% of the value of low value imports and only 18% of total low value consignments.[96] Given half of low value imports are excluded from this analysis, it is far from certain that these results are accurate. The second limitation is that data from 2009-10 is used to project the size of low value imports in the period from 2017-2020. The age of this data renders it unreliable because of a change in economic conditions in the intervening period. In 2012, online retail was growing by 29%.[97] Whilst the latest data from July 2016 shows online retail growth at 11.8%.[98] The slow down in online retail is indicative of a a rapidly changing import market. Further research and corroboration is required to verify the CIE's findings.

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88 Chris Bowen, 'Government Response to Board of Taxation Review of GST Administration' (Press Release No 42, 12 May 2009).

89 Australian Government, 'Government Response to the Productivity Commission Inquiry Into the Economic Structure and Performance of the Australian Retail Industry' (Government Response, 9 December 2011).

90 Evidence of this inter-departmental committee is available at: The Treasury *Question Time Brief GST On Online Overseas Purchasers* (2013) Department of the Treasury <http://www.treasury.gov.au/~/media/Treasury/Access%20to%20Information/Disclosure%20Log/2014/GST%20Threshold%20for%20Low%20Value%20Imported%20Goods/Downloads/PDF/Document_2_qtb.ashx>; Australian Taxation Office (ATO), 'Indirect Tax Significant Issues' (Freedom of Information Request Documents, 17 April 2014) <http://foi.iorder.com.au/downloadfile.aspx?filename=1-59XVE6X.pdf&fromPage=FOIPublicationIentification.aspx&Prodid=1-59XVE6X>.

91 Ibid.

92 Mike Baird, 'NSW Welcomes Commonwealth Agreement For Action on Infrastructure and Online GST' (Media Release, 27 November 2013).

93 Joe Hockey, 'Government Focus on Growth and Infrastructure' (Media Release, 19 September 2014).

94 Joe Hockey, *Statement: Council on Federal Financial Relations Tax Reform Workshop*, above n 1.

95 Additionally, it must be noted that the CIE was commissioned by CAPEC to conduct research. CAPEC organisations such as TNT and DHL stand to lose money on any changes to the LVT, as they will have to help facilitate changes to Customs ICT systems.

96 CIE, *The GST Threshold For Low Value Products*, above n 41, 7-12.

97 National Australia Bank, *Online Retail Sales Index: In depth report January 2010 - January 2012*, above n 77.

98 National Australia Bank, 'NAB Online Retail Sales Index' (Monthly Report, NAB, July 2016).

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