Improving efficiency and competitiveness for Australian retailers

Submission to the Productivity Commission

National Retail Association

Prepared by the National Retail Association

May, 2014

Contents

Overview

The retail sector is one of the nation's largest employers. More than one in ten workers in Australia is employed in the retail sector.

The success of the retail sector therefore contributes significantly to the strength of the Australian economy, the revenues collected by governments, and the creation of jobs through growth.

The sector is comparatively reliant on labour, compared to capital inputs, and so has a greater capacity than most other industries for creating jobs through growth, which can in turn reduce pressure on government welfare and other social services expenditure.

Notably, retail sector employment typically demonstrates higher than average levels of female employment, youth employment, and other entry level or low-skilled employment. It also typically demonstrates higher than average levels of part-time and casual employment, and higher staff turnover. The sector can play a significant role in creating jobs for the unemployed and other job market entrants, new migrants, youth, the secondary income earner in households, those seeking redeployment from shrinking industries and those seeking new career prospects later in their lives.

However, over the past decade, the retail sector has been undergoing a significant structural upheaval, following advancements in technology, digitalisation and online shopping. These changes have led to new consumer behaviours, new retailing models and increased competition through effective globalisation of retail markets. The structural shifts have brought about significant changes in the retail sector in a short period of time, with both challenges and opportunities for retailers.

Retail trading conditions, particularly for retailers relying on discretionary spending, have been exceptionally difficult over a lengthy period. Australian retail sales have remained depressed since July 2009, and while there has been welcome growth since August 2013, this growth has been fragile at best. Discretionary spending categories continue to struggle.

Retail spending is presently weak by historical standards due to a range of factors. Retailer viability is threatened because of the convergence of weak demand with rapidly escalating costs of operation including labour costs, rents, utilities costs and other increases across the supply chain. At a time when retail is in recession it is being asked to bear annual labour cost increases which are the highest ever experienced.

While dealing with these demand side business pressures, Australian retailers have also been confronted with a range of constraints on the efficiency and productivity of their businesses. These range from administrative issues such as tenancy arrangements to regulatory "red tape" such as packaging laws, trading hours and quarantine rules that often vary from state to state. This submission will outline a number of these issues, and how they are affecting retailers.

About the submitter

The National Retail Association (NRA) is a not-for-profit industry organisation providing professional services and critical information and advice to the retail, fast food and broader service industry throughout Australia. NRA is Australia's largest and most representative retail industry organisation, representing more than 19,000 stores and outlets.

This membership base includes the majority of national retail chains, as well as independent retailers, franchisees and other service sector employers. Members are drawn from all sub-categories of retail including fashion, groceries, department stores, home wares, hardware, fast food, cafes and personal services like hairdressing and beauty. The NRA has represented the interests of retailers and the broader service sector for almost 100 years. Its aim is to help Australian retail businesses grow.

Putting Australian retailers on an even playing field

The NRA believes one of the most critical issues confronting some Australian retailers – and also the most easily resolved – is the "low value" exemption from the Goods and Services tax for overseas purchases valued below $1000. This exemption, along with the accompanying exemption from import duties, excises and customs charges, gives an overseas-based business an advantage of up to 25 per cent in cost competitiveness compared with an Australian-based business. It's important to understand that this is not simply a matter of new types of retail stealing a march on traditional stores – often referred to as the "bricks verses clicks" debate. This unfair tax arrangement disadvantages an Australia-based on-line business as much as is does a traditional bricks and mortar business. Indeed, it serves as an incentive for cyber retailers to establish their operations outside of Australia – exempt from local tax, industrial and product safety laws. Further, it is a significant contributing issue to the recent string of prominent and well-known Australian retail brands announcing store closures, reductions in staff or voluntary administration.

In 2011, the Commonwealth Government established the Low Value Parcel Processing Taskforce (LVPPT) to examine the issue of the current low value import threshold for the GST of $1,000.00. The LVPPT's Final Report was released in September 2012. Both the LVPPT's Final Report and the GST Distribution Review Panel's Final Report conclude that the current low value import threshold for the GST is too high and is out of line with overseas standards.

The GST Distribution Review Panel's Final Report noted that comparable countries such as the United Kingdom and Canada have thresholds of approximately $20.00. The Panel also noted that a much lower threshold is needed to minimise a number of practices currently used to avoid the GST, including the disassembly of products and the adjustment of invoices. In fact, the Panel stated that the current threshold is open to "flagrant abuse".

The NRA supports the recommendations of the GST Distribution Review Final Report relating to protecting the intended GST revenue base and preventing the leakage of GST revenue from online imports. This should involve taking immediate steps to make overseas suppliers to Australian residents liable for remittance of GST on all supplies of goods and services that would be subject to GST if purchased from a domestic supplier, and to reduce the low value import threshold to $20.00.

Taking these steps will yield the following benefits:

1. Local retailers will be able to compete on a level playing field, whereas currently the operation of the GST and customs regime puts our businesses at an immediate price disadvantage compared with foreign competitors. Local retailers are not requesting special treatment or protection – we just want a fair go so we can properly compete on a level playing field. The current regime actively discriminates in favour of foreign companies.

2. Local jobs will be saved. An Ernst & Young report commissioned by NRA estimates that up to 33,400 local retail jobs will be lost if our local businesses continue to face this tax discrimination. Note that these jobs are often likely to be the jobs of the least skilled and most vulnerable workers in our country, as the retail sector employs a high proportion of our nation's least skilled workers, such as our youth, single parents, and senior workers returning to the workforce.

3. The Commonwealth Government will be making good its responsibility for vigilantly protecting the GST revenue base on behalf of the States and Territories, by closing an emerging loophole that has become significant since the original design of the GST;

4. The States and Territories will receive additional GST revenues, allowing them to invest in public services and easing their reliance on Commonwealth financial support. The value of the potential GST revenues is $819 million in 2013-14 and growing to over $1 billion a year within the forward estimates, as forecast in an Ernst & Young Report commissioned by NRA.

5. The Commonwealth Government will also receive additional revenues, by virtue of ensuring that this slice of the domestic economy is retained within Australia, rather than lost overseas, retaining its capacity to receive PAYG, corporate and other taxes received from the resulting domestic economic activity.

Now is the best time for the Commonwealth to take action to solve this problem. The size of the trade in question, both in terms of value and number of physical items imported, is growing exponentially, meaning that delays in resolving these issues will only exacerbate any difficulties in implementing solutions at some future point.

Implementation

There have been issues raised in other places around the implementation of such a measure. This is not the forum for addressing those concerns in depth. However, the NRA believes there are two points which are relevant to the examination of the costs of doing business, and the relative competitiveness of Australian retailers.

Firstly, the overwhelming majority of retail purchases from foreign online retailers are dominated by a number of globally significant online giants. This is partially due to familiarity and momentum following successful marketing and campaigns by those global companies, and is also partially due to the reluctance of local consumers to provide personal and banking details to lesser known overseas websites, given the prominence of security risks that prevail on the internet.

For the most part, these globally dominant online giants, whose sales make up a major portion of the online foreign purchases from Australia, already have in place systems with the capacity to comply with a requirement of Australian law to collect the GST. These companies' capabilities and systems currently exist because so many other comparable jurisdictions around the world have already introduced extra-jurisdictional requirements into their own tax regimes (other countries have already introduced such requirements for exactly the same reasons that Australia should). In other words, these global giants are already collecting similar taxes on behalf of other governments

around the world, and could easily do so for Australia if required by the Commonwealth Government.

And secondly, if the Commonwealth Government is forced to weigh the cost of collection by and through its own agencies against the benefits for local retailers, the NRA believes they should unapologetically favour the potential prosperity of the retail sector and the employment of Australian retail workers over the convenience of the Government's own entities, protected as the government entities are in terms of their future and survival. Lifting employment, living standards and entrepreneurship over time in Australia ultimately depends on growing and strengthening the private sector economy.

Recommendation 1: That the Commonwealth moves to place Australian retailers on a fair and even footing by reducing the low-value threshold for GST on imports from $1000 to $20.

Recommendation 2: That the Commonwealth immediately make amendments to the GST law so as to make overseas suppliers to Australian residents liable for remittance of GST on all supplies of both goods and services that would otherwise be subject to GST if purchased from a local retailer.

A fairer workplace relations regime

Without any doubt the single issue that Australian retailers believe most threatens their competitiveness and productivity is the nation's industrial relations system, particularly the changes that were introduced with the "Fair Work Act" in 2009.

Former Prime Minister Julia Gillard, then in the role of Workplace Relations Minister, made a unambiguous promise to business owners that no-one would be worse off as a result of the award modernisation process set in train by the Labor Government upon its election in 2007. It is indisputable that the changes introduced in July of 2010 have left many thousands of businesses far worse off. This is as evident in retail as it is anywhere else.

As a result of these changes, many small retail businesses have been forced to pay penalty rates at a significantly higher rate than previously, or indeed for the first time ever, with no accompanying productivity gains. The award system has also become far too complex and onerous for businesses to achieve compliance.

Feedback from our members indicates that the current workplace relations regime has prompted a significant proportion of smaller retailers either to remain closed on Sundays, or to limit employment at those locations to proprietors and family members only, thus obviating the need to pay significant penalty rates to staff. Other businesses have reported that they simply no longer open their doors on Sundays. This not only denies their staff the opportunity of work, but it also hinders profitability by forcing the business to recover its fixed costs over a shorter trading period each week.

This rational response by shop owners in the face of higher business costs demonstrates the failure of the modern award process, which runs in direct opposition to the expected role of the Federal

Government to assist with economic growth and job creation. As a direct result of the former government's policy, jobs have been lost in the retail sector.

This reduction in economic activity also exposes the tautological nature of the award "modernisation" process, in that it fails abjectly to recognise the modern nature of retail consumer demand. More than any other time in history, consumers today have greater market knowledge, more purchasing options and 24-hour, seven-day access to the retail marketplace via on-line shopping. While confronting this new world, traditional retailers have been forced also to deal with the strictures of the so-called modern award system.

We believe this system will continue to damage economic growth and cost jobs.

Recommendation 3: We call on the government to revisit the modern award process and reintroduce flexibility and balance into Australia's industrial relations system, with the goal of boosting employment in the retail sector.

Youth wages

At the time of this submission, The National Retail Association is involved in an appeal against the Fair Work Commission's decision to abolish junior wage rates for 20-year-old workers – a decision the association believes would be devastating for both retailers and their staff if allowed to stand unchallenged.

The NRA was shocked by the decision of the then Gillard Government in May of last year to support a union campaign to abolish the retail youth wage scheme. This support was given by the former government without any discussion or consultation with industry. Youth wages are a vital mechanism for creating opportunities for young people in the retail sector. It defied common sense to suggest an employer would be prepared to hire an 18-year-old with no experience for the same rate they would pay for an experienced 25-year-old employee.

Age-based junior wages in the retail industry are currently set independently. When they were last examined the Fair Work tribunal found they were not discriminatory because they provided an entry into the world of work and acted as a proxy for those with lower levels of experience. Indeed, the existence of youth wages was taken into account in the creation of the modern award for the retail industry.

We have been overwhelmed by the response from our members and other concerned retailers urging us to respond quickly to this baffling ruling from the Commission. Many members have also expressed their concern about the chest-beating from unions boasting that this is simply the tip of the iceberg, and that they will now work to spread this precedent across other parts of the retail sector.

We are deeply concerned about the serious contradiction between this decision and a number of the Commission's recent rulings, which have effectively required significant expert evidence or bipartisan agreement in order to bring about any substantial changes to modern awards. This ruling was all the more baffling given the difficult circumstances which have prevailed in retailing over recent years. The simple fact is that retailers have fixed wage budgets. If some of their staff

members suddenly cost more to employ, the only rational choice they have is to cut back on the hours that person works. That's why the NRA has agreed to industry's urging to mount an appeal.

Ensuring greater consistency in FWA outcomes

One of the greatest frustrations the retail industry has with the current system is the wide variance in outcomes and the discrepancies in decision making. There are many examples where the Commission has eschewed a common sense approach to the matters before it, and where agreements have been approved outside the spirit of the legislation. Based on our discussions with other industry bodies, we believe this frustration is not limited to the retail sector.

As an example, we have experienced a situation where a Commissioner refused to certify an agreement, even though he agreed that it passed the Better Off Overall Test. The Commissioner asserted that he did not believe the employees genuinely agreed to the terms. This is despite the employer providing a sworn declaration outlining the steps taken to achieve agreement, as well as offering to provide statutory declarations from the employees as well. The employer did not appeal the decision in this case because of the costs involved in doing so. It is our view that the existence of an expert appeals jurisdiction would not only provide a streamlined option for an employer such as this one to pursue a fair outcome, it would also prompt a Commissioner to think twice before making a ruling that is likely to be overturned on appeal. In this way, a new jurisdiction would not only bring consistency through its own rulings, but is also likely to inject greater rigor into the decision making processes throughout the FWA system.

The NRA believes the creation of a single appeals body for Fair Work Commission would provide some much-needed consistency in the outcomes of matters before the Commission. This is particularly true in matters relating to workplace productivity – bargaining, scope orders, enterprise agreement approvals and so on.

Recommendation 4: The Federal Government should push ahead with the creation of a single appeals body for the Fair Work Commission, in order to improve consistency, efficiency and workplace productivity.

The Carbon Tax and Renewable Energy Target

In the difficult retail trading environment outlined earlier in this submission, the introduction of the Carbon tax and the ongoing operation of the renewable energy target (RET) have added significant pressure to businesses. Some members with small supermarket sites have reported to us additional operating costs of many thousands of dollars per year for each site, as a result of higher refrigeration, lighting and cooling costs flowing from the introduction of the Carbon Tax. This has been exacerbated by the impact of the Carbon tax on refrigerant gas. Restaurants, takeaway food retailers and coffee shops have also experienced a significant increase in business expenses due to the cost of operating electric and gas ovens, cooktops and grills.

This is the microeconomic face of the Treasury modelling which shows that economic growth will be permanently slower as a result of the carbon tax. While the focus has largely been on manufacturing and emissions-intensive industries such as smelting, there has been a very real and significant impact on the retail sector. Given the depressed state of the retail sector and the wide variety of options now available to shoppers, there is little scope for businesses to pass these costs on to consumers. The previous government boasted about the minimal impact its carbon tax had had on inflation. Given the significant increase in business input costs, this can only mean retailers and other businesses are absorbing much of the cost impost due to the inelastic nature of demand for goods and services.

The scheduled imposition of the Carbon Tax on diesel fuel, currently legislated for 1 July 2014, will add further to the pressure on retail businesses, and consumers. There are very few consumer items in Australia that are not carried by diesel-powered vehicles at some point in their production and distribution life. This additional facet to the Carbon Tax will place upward pressure on wholesale costs, further eroding margins for store owners, damaging business confidence and reducing employment opportunities.

Federal regulatory cost pressure on energy prices is compounded by the Renewable Energy Target (RET), which mandates the purchase of green-friendly but highly inefficient power from renewable energy sources. As well as adding to business cost pressures, this cost also impacts on household budgets. The RET impacts on domestic electricity prices, but without the compensation that was paid to householders when the Carbon Tax was introduced. This increases cost of living pressures, and reduces discretionary spending ability.

Recommendation 5: The Opposition and other parties in the Senate must allow the Federal Government to fulfil its commitment to scrap the Carbon Tax.

Recommendation 6: The Government should examine the true impact of the RET on business and employment. And to work with the states to maximise efficiency of the electricity supply chain – reducing real costs for businesses and consumers and providing a long term boost to the retail sector.

Product compliance

The retail sector is littered with examples of packaging and signage requirements which at best can only be described as unnecessary red tape. Many of these examples spread across a range of government agencies – customs and imports, weights and measures, standards, health and consumer agencies, to name just a few. The result is a complex and confusing web of regulations and rules which apply to different businesses depending on their different circumstances.

For example, in the fast food sector some states require energy consumption information to be displayed at the point of sale. The NRA questions the value of this information to the vast majority of consumers, and therefore its efficacy as a public health measure. But putting that to one side,

there is no national consistency on this ruling. Some states go so far as to stipulate the font and size of in-store sign-writing, but these requirements vary, creating significant administrative expense for businesses.

In the area of cosmetics, there are Federal regulations that specify information that must be included on the front of a package. If that product is imported, with the correct information on the rear of the package, it must be repackaged or relabelled in Australia to comply with local laws, which require certain information to be displayed on the front of the package.

Australia is a country which represents only a fraction of the world-wide cosmetics market, but has different restrictions to those of most major economies. Prices are therefore higher than in other countries, due to the additional costs associated with labelling compliance.

The NRA recently achieved some success in changing regulations in the area of packaging and labelling. Previous regulations had specified that a pre-packaged towel or bed linen or other fabric sheet, with dimensions of, say, 80cm x 104cm, must instead be labelled as 80cm x 1.04m - with fines potentially applying to any retailer who labelled their product as "104cm" long. Following representations from the NRA and our members, the National Measurement Institute (NMI), to its credit, has listened and has ordered some changes to its regulations to give retailers the freedom to use centimetres to describe these types of products. The change is expected to take effect from 1 July 2014.

While this has now been changed, it is just one of many hundreds of such onerous and unnecessary regulations impacting on retail trade. In our view, these have led to a regime where many small retailers survive on a system of non-compliance and non-enforcement. This is by no means the universal position of retail businesses, but it is without doubt that some operate outside the strict letter of the law because they simply do not understand their obligations, while others simply cannot comply with their obligations.

A small business owner simply does not have the time or resources to constantly stay abreast of the latest changes. And while industry associations such as the NRA are able to advise our members on these requirements, there is a clear cost impost to businesses that could be reduced through simplification of these rules.

In a similar way to the packaging standards, the laws governing product technical and safety standards are a tangle of bureaucratic red tape. In many cases products that are approved for sale in one state are banned in others (such as the example of honey detailed by Coles Supermarkets in its submission to this inquiry). In the case of the electrical industry, there is no national regime for approving and enforcing product safety standards – nor for responding in the case of a failure.

It would be hard to conceive that a child car capsule or a bicycle safety helmet that is approved for use in Germany, for example, would not be fit for use in Australia. However, having such a product certified as safe or approved for use in Australia can be a costly and time-consuming process. If the most common safety and technical standards applicable in Australia were harmonised with our major trading partners, the compliance costs for wholesalers and retailers would be significantly lower.

Recommendation 7: That the Federal Government establish an industry-led committee to simplify retail labelling laws and bring them under a single jurisdiction.

Recommendation 8: That the Australian Government explore options for streamlining product technical and safety certification and harmonising them with our major trading partners, without surrendering Australia's existing high standards.

Leasing and tenancy

Rent and occupancy costs are a major component of almost all retailers' costs of doing business. Within the regulated shopping centre market, a recurring theme in the concerns expressed by retailers is that the annual compounding escalation of rents has exceeded the growth in sales over many years. The NRA's surveys and benchmarks suggest that occupancy costs in this space currently average around 18% in retail shopping centres, which is higher in most cases than the share of retailers' labour costs and on-costs. In some instances, in the shopping centre space, retailers' occupancy costs are at least partially determined by reference to their turnover or the broader performance of others in their product category.

Retail shop leasing arrangements are highly regulated in Australia, almost to the extent of codification. Separate retail shop leasing legislation exists in each of the States and Territories. The retail leasing regimes in each jurisdiction are similar in many respects, but are certainly not identical. Key differences occur between the different state regimes, in many significant areas of leasing administration and operations.

The retail sector is not necessarily adverse to a high level of regulation in the area of leasing and tenancy operations. There is a broad recognition that much of the regulation is predicated on the assumption that landlords and tenants begin in an uneven bargaining position. That assumption does not hold true in some instances, because there exists both small business landlords and large business tenants such retail chains and franchise banner groups. However, almost every piece of real estate is unique in some respects and that poses policy challenges when considering factors such as bargaining and competition.

Nonetheless, there is significant consensus within the retail sector that there are benefits to be obtained through harmonisation of these laws. There is little doubt that public policy can therefore play a significant role in determining retailers' costs in this area.

In 2008, the Productivity Commission completed an investigation into the operation of the retail tenancy market in Australia. That inquiry examined the operation of the market, including the concept of "negotiating imbalance" between landlords and store owners. It also examined planning.

Inter alia, that report recommended Federal and/or State Government action to:

- Improve transparency and information accessibility in the retail tenancy market;
- Improve national consistency and administration of lease information in order to lower compliance costs;
- Reduce jurisdictional differences in the provisions for unconscionable conduct, as applying to retail tenancies;

- Work with stakeholders towards a voluntary national code of conduct for shopping centre leases, with enforcement by the ACCC;
- Remove restrictions in retail tenancy legislation that provide no improvement in operational efficiency;
- Develop model retail tenancy legislation to help move towards national consistency, and for this to be adopted in each jurisdiction; and
- Relax state controls that limit competition and restrict retail space and its utilisation.

Disappointingly, many of the recommendations in that report have not been actioned by the appropriate governments and/or agencies.

The NRA believes that many of the issues identified by the Commission in 2008 remain relevant and unresolved in the marketplace. In some areas these issues have become more difficult for business owners than was the case six years ago.

The NRA therefore recommends that the Commission's 2008 report be revisited and its recommendations be actioned by government.

Of the list of recommendations above, the NRA considers that all continue to be relevant and should be revisited. Each of the recommendations should be actioned, subject to the following updated comments:

- While the ACCC is not the only potential solution for the enforcement or administration of a national code and conduct for shopping centre leases, there remains a clear need for a national approach to facilitate harmonisation, with the involvement of both industry and government.
- The recommendation to remove restrictions in retail tenancy legislation that provide no improvement in operational efficiency remains relevant as a general principle but many jurisdictions have since concluded a subsequent review of their own regimes. These subsequent reviews have to various degrees focused on the potential for cutting red tape. Future deregulatory gains are most likely to be realised through a national approach to facilitate harmonisation.

Recommendation 9: The recommendations of the Productivity Commission's 2008 report into retail tenancies should be revisited and enacted by the Federal, State and Territory Governments.

Contact information

National Retail Association

Chief Executive Officer Trevor Evans

1800 738 245

nra@nra.net.au

Summary of recommendations

Recommendation 1: That the Commonwealth moves to place Australian retailers on a fair and even footing by reducing the low-value threshold for GST on imports from $1000 to $20.

Recommendation 2: That the Commonwealth immediately make amendments to the GST law so as to make overseas suppliers to Australian residents liable for remittance of GST on all supplies of both goods and services that would otherwise be subject to GST if purchased from a local retailer.

Recommendation 3: We call on the government to revisit the modern award process and reintroduce flexibility and balance into Australia's industrial relations system, with the goal of boosting employment in the retail sector.

Recommendation 4: The Federal Government should push ahead with the creation of a single appeals body for the Fair Work Commission, in order to improve consistency, efficiency and workplace productivity.

Recommendation 5: The Opposition and other parties in the Senate must allow the Federal Government to fulfil its commitment to scrap the Carbon Tax.

Recommendation 6: The Government should examine the true impact of the RET on business and employment. And to work with the states to maximise efficiency of the electricity supply chain – reducing real costs for businesses and consumers and providing a long term boost to the retail sector.

Recommendation 7: That the Federal Government establish an industry-led committee to simplify retail labelling laws and bring them under a single jurisdiction.

Recommendation 8: That the Australian Government explore options for streamlining product technical and safety certification and harmonising them with our major trading partners, without surrendering Australia's existing high standards.

Recommendation 9: The recommendations of the Productivity Commission's 2008 report into retail tenancies should be revisited and enacted by the Federal, State and Territory Governments.