

The Rise in Foreign Retailing and New Zealand's GST Exemption: Time for a Change?

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New Zealand's de minimis threshold

- New Zealand operates a *minimum duty/GST payable* de minimis threshold
- Imports into NZ are tax-free if the duty/GST payable is less than \$60
- This has resulted in a roving customs value threshold depending on whether or not a good attracts a tariff



Application of NZ's de minimis – an example

Table 1 – Good subject to a 10% import tariff

	Shirts imported from Vietnam	Value in NZ\$	Duty Payable (NZ\$)
A	Customs Value (i.e. Value in NZ\$)	\$240	
B	Import duty (10% on Customs Value)	\$24	\$24
C	International Freight and Insurance	\$15	
	Value for GST purposes (sum of A to C)	\$279	
D	GST at 15%	\$41.85	\$41.85
Total GST and duty payable			\$65.85 (Collected)

Table 2 – Good with no import duty payable

	A box of books imported from the USA	Value in NZ\$	Duty Payable (NZ\$)
A	Customs Value (i.e. Value in NZ\$)	\$240	
B	Import duty (Not applicable)		\$0
C	International Freight and Insurance	\$15	
	Value for GST purposes (sum of A to C)	\$255	
D	GST at 15%	\$38.25	\$38.25
Total GST and duty payable			\$38.25 (Not Collected)



Overview

- The research was done in two steps:
 1. Literature review:
 - Three key areas of discussion:
 1. What was driving the growth in e-commerce?
 2. Which segments of the economy benefit from e-commerce?
 3. What effects has the government's current tax policy had on the New Zealand e-commerce market?
 2. A review of New Zealand's de minimis threshold in light of the literature reviews conclusions



Literature review – What underlined the growth in e-commerce?

- In 2012, New Zealanders spent \$3.19bn online, this is predicted to grow at 14.3% p.a. to reach \$5.37bn by 2016 (PWC)
- Literature showed 4 key drivers:
 - Lower prices
 - Increased product range available online
 - Increased product availability
 - Other drivers: Debit cards, tablet computers etc.



Lower prices

- Internet allows consumers to compare retailers offers quickly and effectively e.g. webjet.co.nz or pricespy.co.nz
- Internet prices are on average lower than traditional retailers, but a majority of consumers do not select the cheapest offer shown on ‘shopbot’ websites
- However, there are “substantial and systematic differences in prices across retailers on the internet” (Brynjolfsson, Dick and Smith, 2010)
- Consumers appear to use store branding as a proxy for credibility.
- Even though CD’s and Books are identical, regardless of the store which they were purchased in, there remains a strong predilection for well known branded companies such as Amazon or Barnes and Noble (Smith and Brynjolfsson, 2001)
- **Thus prices are important – but are not necessarily the key driver of e-commerce** cf. PWC’s findings whereby 51% of New Zealander’s surveyed regarded lower online prices as being the most important reason for shopping online.

Increased product selection and availability at online retailers

- The increased product range available online provides a greater motivation for the growth in e-commerce than lower prices (Brynjolfsson et al, 2003)
 - The authors estimated that in 2000 alone, the increased product variety available on Amazon led to consumer welfare growth of between US\$731m and US\$1.03bn
 - This gain was approximately 7.3 – 10.0 times larger than the consumer welfare gain from increased prices and competition on the internet.
 - This result was confirmed in 2010
- Increased product variety is especially important in the New Zealand market due to our geographical isolation and small market

Increased product availability:

- Consumers are frustrated if a conventional store doesn't have the desired product in stock, or is unable to find it

Who benefits from the rise in e-commerce?

- Consumers:
 - Markets were traditionally dominated by the Pareto principle: A small proportion of products in the market (e.g. 20%) often generate a large proportion (e.g. 80%) of the industries sales
 - However, internet purchases contain a significantly higher proportion of niche products (the longer tail)
 - Consumer welfare has expanded dramatically – sales of niche books on Amazon created between US\$3.93 – US\$5.04 billion in 2008 (Brynjolfsson, Hu and Smith, 2010)
- Firms:
 - Access to overseas markets, but struggle to compete with foreign online retailers

Online retailing and fiscal policy

Arguments for collecting GST on offshore online sales

- Collecting GST on offshore purchases is simply an application of an existing tax
- A weakened tax revenue base:
 - Unlike the US, failure to tax offshore purchases results in lower company and PAYE taxes as well as lower GST revenues
- Results in undesirable distributional effects:
 - The benefit of the tax exemption is only available to consumers who shop online

Arguments against the collection of GST on offshore online sales

- Taxing online purchases could lead to social under-provision (infant industry argument) through:
 - Reduced network benefits; and
 - Information problems
- Significant company administrative costs
- Customs enforcement costs

How has the government's tax policy affected the decision to purchase online?

Paper	Data Source	Tax elasticity estimate
Goolsbee, <i>In a world without Borders</i> (2000)	Forrester Research Survey of 110,000 US Households – December 1997	-3.5
Goolsbee, <i>Internet Commerce, Tax Sensitivity and the Generation Gap</i> (2000)	Forrester Research Survey of 85,000 US Households – December 1998	-2.4
Alm and Melnik, <i>Sales taxes and the decision to purchase online</i> (2005)	Computer Use and Internet Access Supplement to the Current Population Survey – December 2001	-0.52
Ellison and Ellison, <i>Tax Sensitivity and Home State Preferences in Internet Purchasing</i> (2009b)	Pricewatch.com data from May 2000 to May 2001 for the US Computer Memory Market, plus sales data from two retailers	-5.94
Einav et al, <i>Sales Taxes and Internet Commerce</i> (2012)	Complete eBay browsing and purchasing data from 1 January to 31 December 2010	-1.8

For every 1% increase in state sales tax:

- Result in a 1.8% increase in out-of-state online purchasing; and
- The volume of sales at in-state online retailers falls by 3% – 4%

Applied to NZ, Einav et al's study suggests that if the govt abolished the de minimis threshold there would be a 45-60% fall in purchases from offshore internet retailers, offset by a 27% increase in demand at domestic internet retailers.

The effect of sales on firm location decisions

- Research from the US indicates that sales tax rates affect firm location decisions
- Firms may be discouraged from entering the New Zealand retail market if it entails a loss of their implicit 15% subsidy.



Effect of e-commerce on domestic firms

- With the internet, the location of firms has become less important – NZ firms could sell to consumers in Russia, Hong Kong, Mexico etc.
- However, most of the benefit accrues to large, offshore online firms such as Amazon.
- This has created significant pressure for conventional domestic retailers who are unable to compete on price – especially given the operation of the de minimis threshold
 - For example, Marbeck's recent exit from the CD market

New Zealand's current border processing system

- As noted earlier, New Zealand operates a minimum duties/GST payable limit. Imports are tax-free if the duty/GST payable is less than \$60
- This results in a roving threshold of between \$226 and \$399 depending on whether the good attracts a tariff
- Different procedures operate - depending upon the import channel
 - Mail:
 - All Intl. mail is diverted to the IMC in Auckland, where it is manually screened
 - No customs fees are payable if the parcel is below the threshold
 - If a parcel exceeds the threshold it is withheld from delivery until duties/GST have been paid, and all customs and MPI fees have been paid
 - International Parcel Post/Couriers:
 - All packages entering NZ must be reported to Customs (regardless of their value)
 - All border processing is done by the courier companies, who then pass this cost onto consumers
 - Although the process is costly, it is streamlined and allows for rapid border transit



Customs Processes around the world

Customs Administration	Value Threshold for GST/Sales Tax (except New Zealand)	Threshold in NZ\$ (as at 13/2/2013)
Australia	A\$1000	NZ\$1,229.32
Canada	C\$20	NZ\$23.73
People's Republic of China	CNY500	NZ\$95.32
Republic of Korea	KRW150,000	NZ\$164.28
New Zealand	\$60 in duty/GST payable	Between \$226 and \$399
United Kingdom	£15 (excl. the Channel Islands)	NZ\$27.96
United States	US\$200	NZ\$237.74



Customs Process around the world

- United Kingdom:
 - Operates a split customs value threshold (£15 for VAT (excl. Channel Islands), £135 for duties)
 - All intl. mail manually screened – but collection through Post Office
- Canada:
 - Very similar to the U.K.
 - Courier Low Value shipment programme. Courier companies can clear all goods with a value of less than C\$2,500 remotely (brings Canada in line with the US)
- Australia:
 - Similar to New Zealand – but uses a minimum customs value threshold.
 - Pressure to lower the de minimis threshold from State governments



Suggestions for future change:

Changing the definition to a minimum customs value

Advantages	Costs/Disadvantages
<ul style="list-style-type: none">• Simple legislative amendment• Will make the de minimis easy to comprehend and understand• Increase consumer awareness• Lower Customs costs in Intl. mail environment• Increased border security	<ul style="list-style-type: none">• Changing the definition can have the effect of widening the threshold



Suggestions for future change:

Collection of duty/GST through financial intermediaries

Advantages	Costs/Disadvantages
<ul style="list-style-type: none">• Would remove the threshold entirely• Enable the government to tax 'intangible' transactions	<ul style="list-style-type: none">• Would be impossible to collect duty• Risk that all GST owing would not be collected• Need to isolate a sales tax exclusive price• Identification of offshore transactions not liable for GST• Administrative costs• Ease of avoiding this scheme (e.g. Australian Credit cards)

Conceptually attractive, but currently infeasible



Suggestions for future change:

Multilateral agreement promoting voluntary registration for taxation principles

How would it work?

- Agreement via APEC or through multilateral negotiations
- Designed to promote voluntary registration and collection by firms through incentives such as:
 - Rapid border transit
 - Reduced consumer compliance costs

Advantages	Issues/Solutions
<ul style="list-style-type: none">• Reduced delivery times and costs• Companies will derive the biggest value from large economies – NZ can ‘piggyback’• Increased compliance in intl. mail• More secure border• Model for future action on intangible trade	<ol style="list-style-type: none">1. Countries must ensure that duties/sales taxes are correctly assessed<ul style="list-style-type: none">• Establish a free database2. Duties/GST must actually be remitted to respective countries<ul style="list-style-type: none">• Bonds or instant electronic payment3. Must be able to identify pre-paid packages and check compliance<ul style="list-style-type: none">• Companies given secure identification tools4. Consumers must be able to derive security from their pre-payment



Questions?



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Methodology for future assessment of the de minimis threshold

- Some issues with Customs' cost-benefit analysis to date
- We recommend two alternative methodologies for future assessment of de minimis thresholds:
 - Government focussed approach
 - Societal approach



Methodology for future assessment of the de minimis threshold

	Benefit	Cost
Customs Issues Paper	Tax revenue collected	Administrative costs throughout society
Government orientated	Tax revenue collected	Government expenses less costs recouped from importers
Social welfare maximising	Rise in NZ producer surplus along with the tax revenue collected	Decline in consumer surplus along with increased administrative costs

