VAT Reform in China: Can New Zealand's Goods and services tax Provide helpful Guidance?

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Abstract: Value Added Taxes (VATs or Goods and Services Taxes - GSTs) are being increasingly adopted globally, with VAT/GST revenues similarly increasing through higher contributions from indirect taxation to total tax revenues. Unsurprisingly, increased focus is being placed on the design of such taxes, encompassing policy choices and legislative drafting styles. New Zealand's (NZ's) GST, introduced in 1986, is held up as the 'model' VAT in a post-European VAT environment, especially when measured against the key tax principles of efficiency and simplicity. Importantly, the trade-off has been less equity within the tax itself, which necessitates forms of compensation elsewhere in the tax system. The vast majority of GSTs developed since 1986 have used the NZ GST model as a starting point, although no subsequent GST/VAT has been as 'pure' as the NZ model. A number of factors have been influential in resulting VAT/GSTs. This includes: the actual design, prevailing tax policy process; general economic environment; and jurisdictional political philosophies (at the time the VAT/GST is promulgated and implemented). Of particular importance in NZ is the Generic Tax Policy Process (GTPP) which encourages both early and widespread consultation over tax policy design and draft legislation.

This paper seeks to provide an overview of NZ's GST (including the core concepts within the GTPP) as a case study for evaluation as a possible 'initial model' for adaptation in China as it seeks to reform its VAT. Through building on prior work reviewing the Hong Kong Special Administrative Region's (the HKSAR's) GST experience and policy development framework, this paper offers insights into why the author believes the NZ GST experience should be of both interest and relevance to the People's Republic of China (the PRC). This is premised on the basis that NZ's GST has been endorsed in subsequent tax system reviews, and survived notwithstanding major changes in the NZ political environment and prevailing economic conditions.

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1. Introduction

It is important to emphasise at the outset that this paper provides a high level policy perspective of the New Zealand (NZ) Goods and Services Tax (GST) – the first of the value added taxes (VAT) to move away from the VAT nomenclature to that of GST. This is much more than just a change in name – it represents a significant move away from the relatively complex VATs that members of the European Union have developed as part of their membership. New Zealand's GST represents the benchmark for an efficient and effective GST, from which other jurisdictions have based their GSTs (such as Australia, Canada and Singapore, to name but three examples).

To set the scene, NZ's GST commenced in 1986, some 12 months after the legislation was enacted. The NZ Government's intention was to improve the fiscal environment through a broad based tax, changing the tax mix, and 'compensating' low income taxpayers affected by this change in the tax mix. Consultation with individuals and organisations was included prior to its introduction and with subsequent changes of significance.

In contrast to earlier European VATs, a very limited number of concessions were made to allow zero rating or exemption from GST – most were on grounds of efficiency or practical measurement issues (indeed, NZ's GST base has expanded over time, such as to include business to business financial services). As a consequence, NZ's GST is arguably the 'purist' form of a VAT/GST in operation anywhere in the world.[13] However, subsequent amendments have added additional legislative complexity to the GST but have also clarified some areas of uncertainty. A significant recent development is the increase in the rate to 15 percent in 2010 which accompanied a reduction in the top marginal tax rate on income for individuals.

In the mid-1990s, NZ took a new and innovative route with the adoption of the Generic Tax Policy Process (GTPP), a bi-product of a review of the Inland Revenue Department (IRD) conducted through a committee (the Organisational Review of Inland Revenue) chaired by Rt Hon Sir Ivor Richardson, a former President of the NZ Court of Appeal.[14] Sir Ivor identified a number of problems with the previous tax policy development process, noting that[15]:

> "… the subject matter is complex, and tax legislation is very complex and difficult to understand. The *tax policy process was not clear*, neither were the accountabilities for each stage of the process. There was *insufficient external consultation in the process*."

Essentially, the GTPP provides a more rigorous process necessitating public scrutiny within its various phases, including submissions on both underlying policy and draft legislation. This is particularly important given NZ only has one house of Parliament, the House of Representatives. The GTPP has been reviewed by policymakers and academics in several overseas jurisdictions, with Dirkis and Bondfield viewing it favourably for Australia.[16]

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[13] David White, 'Comment: Twenty Years of GST: The Best Path Forward' (2007) 13(4) *New Zealand Journal of Taxation Law and Policy* 357. See also Gabriel Makhlouf (Secretary to the Treasury), 'The New Zealand Economy and Tax Policy' (Speech delivered at the 2012 International Fiscal Association, Queenstown, 17 March 2012); <http://www.treasury.govt.nz/publications/media-speeches/speeches/nzeconomytaxpolicy/sp-nzeconomytaxpolicy-17mar12.pdf> (emphasis added).

[14] Rt. Hon Sir I. Richardson, *Organisational Review of the Inland Revenue Department, Report to the Minister of Revenue and the Minister of Finance* (April 1994).

[15] Ibid 5 (emphasis added).

[16] Michael Dirkis and Brett Bondfield, 'At the Extremes of a "Good Tax Policy Process": A Case Study Contrasting the Role Accorded to Consultation in Tax Policy Development in Australia and New Zealand' (2005) 11(2) *New Zealand Journal of*

The motivation behind this paper is two-fold; first, it is to share the experiences of NZ's successful GST (the international benchmark for efficiency and simplicity), as well as the innovative and very successful tax policy process, the GTPP. Second, it is to offer practical insights for consideration by the Peoples' Republic of China (the PRC) as it seeks to review and rationalise its consumption taxes into a more comprehensive VAT. This paper draws upon contributions by the author in two recent articles that undertake a comparative GST analysis. Both articles offered the Hong Kong Special Administrative Region (HKSAR) guidance, the first reflecting upon the New Zealand GST experience, and the second on NZ's tax policy development framework (the GTPP).[17]

This paper adopts both positivist and normative philosophies. The analysis of NZ's GST and GTPP takes a positivist perspective, combining a review of perspectives of key players and the author's observations with respect to policy. It also offers a normative perspective in regard to how the PRC could consider the NZ policy experience with regard to its VAT development.

The remainder of this paper is organised as follows. In the next section, NZ's experience with GST is examined, followed by a review of the tax policy framework for NZ (the GTPP) in section 3. Section 4 provides some insights from the NZ experience with GST that could be of value to the PRC, with section 5 setting out the concluding observations.

2. New Zealand's Experience with GST

This section will focus on the background as to how the NZ GST came about, reflect upon why the GST was able to be successfully introduced and continue to remain sustainable, and how it became a critical component of the NZ tax system. It will also in part reflect upon why the NZ GST is held up as an aspirational model for other jurisdictions contemplating introducing a GST, and forms the basis for the vast majority of modern VATs/GSTs introduced since the mid-1980s.

2.1 The arguments supporting a GST in NZ

The NZ story has been well rehearsed by many commentators as reaching a critical point in 1984 when the then incoming Labour Government faced an economy in crisis and in need of a radical overhaul.[18] Much of what occurred over the following three years (1984-1987) can be seen as a radical economic liberalisation experiment that was facilitated by 'perfect conditions', namely an economy in desperate need of a radical overhaul, a new government with an electoral mandate to implement change, and a Minister of Finance with a clear plan to overhaul the economic environment. Importantly, tax reform was an integral part of the reform process.[19]

Taxation Law and Policy 250. Little, Nightingale and Fenwick also reviewed the GTPP and the role of independent tax reform; see Struan Little, Geof D Nightingale and Ainslie Fenwick, 'Development of Tax Policy in New Zealand: The Generic Tax Policy Process' (2013) 61(4) *Canadian Tax Journal – Revue Fiscale Canadienne* 1043. See also C.J. Wales and C.P. Wales, 'Structures, processes and governance in tax policy-making: an initial report' (Speech delivered at the Structures, Processes and Governance in Tax Policy-making Conference, Saïd Business School, Oxford, March 8–9, 2012), where the authors express enthusiasm for the rigour of tax policy-making in NZ.

[17] For further details, see Adrian Sawyer, 'New Zealand's Successful Experience with Introducing GST: Informative Guidance for Hong Kong?' (2013) 43(1) *Hong Kong Law Journal* 161; and Adrian Sawyer, 'Establishing a Rigorous Framework for Tax Policy Development: Can New Zealand Offer Instructional Guidance for Hong Kong?; (2013) 43(2) *Hong Kong Law Journal* 579.

[18] For an overview of the political and economic issues facing NZ in the lead up to the 1984 General Election, see for example, Jon Johansen, *Two Titans: Muldoon, Lange and Leadership* (Dunmore Publishing, 2005); and Barry Gustafson, *His Way – A Biography of Robert Muldoon* (Auckland University Press, 2000). Sir Roger Douglas published his own work in 1996; see Roger Douglas, *Completing the Circle* (Seascape Press, 1996).

[19] For further discussion and analysis, see John Singleton, 'An Economic History of New Zealand in the Nineteenth and Twentieth Centuries', *Economic History* (February 2010); available at: https://eh.net/encyclopedia/an-economic-history-of-

A major component of the tax reform platform was the GST, combined with a reduction in the top marginal tax rate on income tax of 66 per cent to 33 per cent. This high rate applied to many taxpayers as a result of bracket creep due to wage increases, reflecting in part rising inflation. The GST was a major component of a partial, but significant, move away from direct to indirect taxation, along with a broadening of the tax base. Of note is that GST was a component of major tax reform intended to minimise the net impact on individuals but position NZ for economic revival.

An early analysis of the GST is provided by Teixeira, Scott and Devlin in 1986.[20] The authors trace the evolution of the NZ GST from the first announcement of its introduction in 1984, to the stage of final legislation in 1986. Teixeira et al included brief reviews of the work of the Advisory Panel on the Goods and Services Tax and the Select Committee process that reviewed the draft legislation and recommended a delay in the implementation date. The authors also considered various administrative aspects of the tax through a discussion of provisions from the NZ Government's *White Paper*[21] to the amended legislation. Some comparisons are made between the NZ GST and other VAT taxes, particularly the UK VAT.[22] Teixeira et al also considered various features that would be important in shaping the associated administrative and compliance costs of the GST.

Quiggin[23] observed that the Minister of Finance in NZ at the time of the GST proposal, Roger Douglas, was firmly committed to the concept of a GST, and had the firm backing of the Government that commanded a majority in the unicameral Parliament.[24] Writing in 1992 by Bollard[25] (a former NZ Reserve Bank Governor) endorsed these comments, and observed that the idea of a broad-based consumption tax (a GST) was outlined in principle in the Labour Government's first 1984 Budget. A private sector advisory panel was constituted, received a large number of submissions and drafted amendments. Subsequently an announcement was made in 1985 that the GST would take effect from October 1986. All of these key steps followed a major advertising campaign and a series of business seminars. Largely as a consequence of the preparation and publicity, the actual implementation went relatively smoothly. However, Bollard noted that there was some measurable disruption to the pattern of retail sales in the period around the implementation date of the GST.

Bollard observed that the introduction of GST was reasonably well received.[26] While small scale retailers were opposed to compliance requirements, large scale business interests generally supported the GST. This was in contrast to a proposed capital gains tax (CGT) which

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[20] Alan Teixeira, Claudia Scott, and Martin Devlin, *Inside GST: The Development of the Goods and Services Tax* (Institute for Policy Studies, 1986). For an earlier analysis of the major issues surrounding the introduction of the NZ GST, see the work by Claudia Scott and Howard Davis, *The Gist of GST* (Institute for Policy Studies, 1985).

[21] *White Paper on Goods and Services Tax: Proposals for the Administration of the Goods and Services Tax* (New Zealand Government, 1985).

[22] For a comparison of the UK VAT and NZ GST, see Simon James and Adrian Sawyer, 'Comparing the United Kingdom's VAT with New Zealand's GST: Fairness versus Policy Benchmarks?', under review with the *World VAT Journal*.

[23] John Quiggin, 'Social Democracy and Market Reform in Australia and New Zealand' (1998) 14(1*) Oxford Review of Economic Policy* 76, 84 (emphasis added).

[24] In fact Roger Douglas was a very right-of-centre free market leaning politician, such that after leaving the Labour Party, he came back into Parliament as a member of the right-of-centre ACT Party under the new (and current) Mixed Member Proportional (MMP) political system. See further the discussion in footnote 35 on MMP.

[25] Alan Bollard, 'New Zealand's Experience with Consumption Tax' (1992) 9(4) *Australian Tax Forum* 473.

[26] Ibid.

received a broadly hostile response from the business sector.[27] Bollard commented that estimates of the GST impact on consumer prices varied from 5.7 per cent to 7 per cent, indicating there was an inflationary effect. Bollard also reviewed the price effects, distributional effects and macroeconomic effects brought about by the tax reform package incorporating the GST.

The Labour Government at the time was especially reluctant to grant any exemptions but permitted a small number, including financial services, life insurance, non-profit organisations and existing house sales (some of these were due to an inability at that time to measure the value added without undue complexity). Thus, the GST substantially broadened the tax base that was previously heavily reliant upon income tax, and piecemeal wholesale and retail sales taxes on certain goods. GST's introduction also extracted tax payments from many who had paid less in the way of taxation previously (that is, it altered the incidence of taxation). However, the introduction of the GST was part of a package of reforms, and needs to be viewed as part of a tax reform process. The package included a reduction of personal income tax to a lower flatter structure, making the overall tax structure less progressive.

Thus to summarise, the GST was part of an overall package to rebalance the tax mix, with minimal disruption to the business sector, and a well thought out process of conceptualisation, planning and implementation. But this is not the entire story.

2.2 The arguments against a GST in NZ

There has been little in the way of argument put forward against having a GST in NZ conceptually,[28] although there has not been universal acceptance that the focus on efficiency, at the expense of fairness, was the best approach. Indeed, recent calls for introducing exemptions or lower rates for goods, such as fresh fruit and vegetables, are aimed at introducing more fairness into the GST, and reducing its regressionary impact. While initially gaining some traction through support from a number of opposition political parties, these calls have not been developed as far as any firm policy proposals for change.[29]

The theme of radical tax reform through a significant redistribution of the tax burden is reflected in the seminal work of Stephens.[30] Commenting on the introduction of GST, Stephens observed that much of the reform was aimed at a redistribution of the tax burden. While some targeted tax preferences were removed, much of the reform led to a redistribution that may be termed "pro-rich". Stephens also commented that since the relative purity of the 1984 initiated reform, much of this has been lost through added complexity and major forms of income assistance to low income earners and families. Stephens' analysis supports that of Bollard in relation to the impact of GST on prices.

Since its introduction, criticism of the GST has remained, but there has been no reduction in its base, reflecting a general acceptance by subsequent governments that the trade-off for greater efficiency and revenues outweighed the negative impact on equity (which could be

[27] Subsequent attempts to propose a CGT have been unsuccessful with no government willing to make a CGT part of its tax reform agenda, although several opposition parties (including the Labour party) included a CGT as part of their manifesto for the 2011 and 2014 General Elections, along with the Green Party in its manifesto for the 2014 General Election.

[28] In the 1990s, the Alliance Party proposed to replace the GST with a Financial Transactions Tax; this proposal never advanced any further. The Mana Party proposed abolishing GST and replacing it with a levy on financial transactions as part of its 2014 election policy; the party is no longer represented in the NZ Parliament.

[29] As part of the 2014 General Election, the NZ First Party's manifesto included removing GST from food and property rates, along with the Maori Party for food. Neither party's proposals will advance any further in the next three years.

[30] Robert Stephens, 'Radical Tax Reform in New Zealand' (1993) 14(3) *Fiscal Studies* 45.

addressed through various forms of financial assistance provided through income support and welfare).

2.3 Analysing NZ's Policy Experience with GST

In reflecting upon the first twenty years of operation of the NZ GST, White observed that "[i]n many respects, the design and implementation of this tax is still regarded as international best practice. Its basic design features remain unchanged."[31] As part of the twenty year celebrations, a symposium was held in late 2006 in which a number of leading commentators prepared papers addressing aspects of the NZ GST. The opening paper was the address by Sir Roger Douglas (the architect of the NZ GST), who commented on the political issues associated with the introduction of the GST. Douglas remained firmly of the view that the introduction of the GST was successful, a position that he based on five "facts":[32]

- it was supported by two out of every three New Zealanders within days of its introduction;
- it ceased to be a political issue within six months of introduction;
- it was an accepted part of the economic frameworks of NZ within months;
- its introduction ran smoothly; and
- twenty years later it remains fundamentally unchanged.

'Acceptance' by such a large group of taxpayers in such a short time is in part a result of the educational and information campaign conducted prior to implementation, backed by various surveys undertaken by research organisations. Much of this success is attributed to a strong commitment to the GST by the Labour Party Cabinet (led by Douglas), notwithstanding resistance from trade unions and their members. Also vital to its success was the quality of the officials that worked on the design and implementation, the 'packaging' of GST – it was not a new tax introduced in isolation but part of a realignment and broadening of the tax base, with lower tax rates on income.

Furthermore, the process of consultation was extensive, including the establishment of a consultative committee to review over one thousand substantive submissions and make technical changes.[33] This consultation process did not aim to seek a consensus between various interest groups. There was a preparedness by the government at the time to take the pain at the beginning (such as through unpopularity) and be judged on the good results later. In a time of First Past the Post (FPP) electoral system, following an endorsement for change in 1984, such a bold approach is understandable. Had a Mixed Member Proportional (MMP) electoral system operated at the time, where minority governments are the norm, such a bold approach is unlikely to have been taken.

[31] See White, above n 1, 363–364.
[32] Roger Douglas, 'The New Zealand GST Policy Choice and its Political Implications' in Richard Krever and David White (eds), *GST in Retrospect and Prospect* (Thomson Reuters, 2007) 3.
[33] It is important to observe that at the time of the GST, NZ's consultation on tax policy was very limited, and the internationally renowned Generic Tax Policy Process (GTPP) did not come into operation until 1994. For further discussion, see Adrian Sawyer, 'Reviewing Tax Policy Development in New Zealand: Lessons from a Delicate Balancing of Law and Policy"' (2013) 28(3) *Australian Tax Forum* 401.

Green, a member of the Advisory Panel on the Goods and Services Tax, commented that GST was a critical component of the tax reforms in train during the 1980s.[34] Green observes that the Minister of Finance was taking a "hands-on approach" and that the timeframe for change was incredibly tight. Green reflects upon the way in which the Advisory Panel set about analysing the submissions, preparing its reports and making recommendations (including deferring the introduction date to allow the supporting work to be completed). All of these activities assisted with the smooth implementation.

Todd, as Director of the GST Coordinating Office, focused on the information and educational coordination role that the Coordinating Office undertook.[35] The GST Coordinating Office managed all of the publicity and educational guidance. A key aspect was to ensure that all of the relevant government departments were working together, and that the necessary messages were provided to businesses and the general public. The focus was on demonstrating how the GST would make the tax system fairer and that everyone would be compensated for the imposition of the new tax on goods and services.

Dickson, a member of the NZ Treasury at the time of the development and implementation of the GST, reflected on the matters raised by the other commentators at the symposium.[36] He places particular emphasis on the three-year GST campaign that ran from 1984 to 1986, the little known fact that the Treasury never recommended the GST, the technical aspects of the GST, and the importance of the consultation process. Dickson also singled out for attention the high level of commitment to the GST which was given at considerable political risk to the government at the time.

In an academic commentary on NZ's GST, James and Alley suggested that NZ was able to benefit from the introduction of VATs in other jurisdictions before it introduced its GST.[37] Potentially having a shorter period of consultation than in the UK may have led to the simpler GST in NZ, with less time for those in opposition to mount detailed and concerted campaigns. However, this may have led to a GST in need of considerable remedial amendment. It should also be recognised that NZ was in dire economic circumstances at the time and needed a major overhaul of its tax system, along with additional revenue derived from a broader base. The authors emphasised that the choice of the name 'GST', rather than 'VAT', was intended to distinguish the NZ model from that of the UK.[38] The issue over the regressive nature of consumption taxes was largely offset by adjustments to other taxes and support for families and low income earners.

Vial observed that the NZ GST is not only "… an international benchmark for indirect tax design" but that it has the highest C-efficiency ratio in the OECD (currently standing at 99 per cent) – the next closest is Luxembourg at 92 per cent.[39] Politicians have resisted major changes

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[34] Richard Green, 'Consulting the Public in developing a GST' in Richard Krever and David White (eds), *GST in Retrospect and Prospect* (Thomson Reuters, 2007) 13.

[35] Jeff Todd, 'Implementing GST – Information, Education, Coordination' in Richard Krever and David White (eds), *GST in Retrospect and Prospect* (Thomson Reuters, 2007) 27.

[36] Ian Dickson, 'The New Zealand GST Policy Choice: An Historical and Policy Perspective' in Richard Krever and David White (eds), *GST in Retrospect and Prospect* (Thomson Reuters, 2007) 45.

[37] Simon James and Clinton Alley, 'Successful Tax Reform: The Experience of Value Added Tax in the United Kingdom and Goods and Services Tax in New Zealand' (2008) 8(1) *Journal of Finance and Management in Public Services* 35. The authors make extensive reference to the contributors to the work by Krever and White; Richard Krever and David White (eds), *GST in Retrospect and Prospect* (Thomson Reuters, 2007).

[38] James and Alley, above n 25.

[39] Peter Vial, 'The Sustainability of the New Zealand Tax Base: Are we at the End of the Road for the New Zealand Tax System?' (2009) 15(1) *New Zealand Journal of Taxation Law and Policy* 17, 22; citing Richard Krever and David White (eds), *GST in Retrospect and Prospect* (Thomson Reuters, 2007), viii. The C-efficiency ratio (or VAT Revenue Ratio - VRR) is the ratio of VAT revenue to consumption expenditure, divided by the standard tax rate, expressed as a percentage. With NZ having one rate, a comprehensive base and virtually no exemptions, this high ratio comes as no surprise. Since Vial's work, the latest

to the GST since its introduction, with the exception of increasing the rate twice (the first time to 12.5 per cent in 1989, and later to 15 per cent with the major tax review in 2010),[40] increasing the breadth to include certain excluded areas (for example, certain financial services), and remedial legislative amendments. Significantly, the Tax Review 2001, set up by a left-of-centre government, rejected submissions to narrow the GST base.[41] As noted earlier, several opposition parties have been calling for significant amendments to exempt certain items (such as fresh fruit and vegetables, and other essential healthy food items, plus property rates), although these calls have yet to gain traction.

Barrett undertook comparative analysis of the VATs/GSTs in each of Australia, New Zealand, South Africa and the UK.[42] From his application of various tax philosophers, his conclusion is that the GST does not do well in isolation, but with a wider perspective, taking into account the justice of the tax-transfer system, the position can be defended. To this end he concluded with a quote from the Henry Tax Review in Australia:[43]

> "Income redistribution to make [a country] fairer is primarily the job of the income tax and transfer system … *other taxes and charges can be used in the most efficient way, reducing the overall complexity of the system*. It is very difficult to target GST exemptions on some products to certain groups."

The Secretary to the NZ Treasury is very complimentary of the NZ GST model, stating:[44]

> "It has been said plenty of times before but it still bears repeating: *New Zealand's GST is the best VAT in the world and our strong consistent advice is that it should be protected from exemptions that undermine it*. ….

There have been 17 VAT increases in the EU in the last 2 years. In 2011 an average VAT rate across the OECD was 18.5% – it is 20% in the United Kingdom. One reason these countries have higher value added taxes is because they exempt all sorts of goods and services. *As with income tax, we prefer a broad based low rate to a narrow base with a high rate*".

2.4 Summarising the prior analysis of the NZ GST

Thus, to summarise, the sustainability of the GST strategy for over 25 years is based on a combination of economic, legal, geographical and constitutional factors, supported by an open, patient and politically supported implementation. It is important to remember, as White concluded, that the NZ GST was designed to produce 20–25 per cent of tax revenue, with the

estimates place this at 99 per cent as the base has been slightly extended. This is also the figure used in the Tax Foundation's *International Tax Competitiveness Index* (2014), where NZ's VAT base as a percentage of total consumption is 99 per cent, and Luxembourg's is 92 per cent. See also OECD, *Consumption Tax Trends 2012: VAT/GST and Excise Rates, Trends and Administration Issues* (2012, OECD: Paris).

[40] This review followed a report from the VUW Tax Working Group; Victoria University of Wellington Tax Working Group, *A Tax System for New Zealand's Future* (January 2010); available at: http://www.victoria.ac.nz/sacl/cagtr/pdf/tax-report-website.pdf/ (accessed 3 August 2012). Even with the move to 15 per cent an advisory panel was set up to assist businesses with the transition. For details of this most recent advisory panel, which include tax practitioners and business leaders, see http://www.gstadvisory.govt.nz/panel (accessed 3 August 2012).

[41] Tax Review 2001, *Final Report* (Wellington, October 2011).

[42] Jonathan Barrett, 'Equity and GST Policy' (2010) *Journal of Applied Law and Policy* 15.

[43] Ibid 31; citing Commonwealth of Australia, *Australia's Future Tax System: Report to the Treasurer* (2010) ('Henry Report') vol 1, [D 2–1] (emphasis added).

[44] See Makhlouf, above n 1.

largest contributor continuing to be the income tax (this tax itself went through major reform in the 1980s, and again in the early 2000s and most recently in 2010).[45]

The prior literature suggests a number of critical elements to the success of the NZ GST, both prior to, and following, its implementation. Prior to the implementation, NZ was in an economic crisis, with the economy in need of a radical overhaul, including tax reform with a system excessively reliant upon income tax and inefficient indirect taxes. As a geographically isolated nation, heavily reliant on trade and foreign capital, this presented the incoming Labour Government with greater flexibility in determining its tax mix. This Labour Government comprised several "bold" politicians, no more so than the Minister of Finance, Roger Douglas. The political and electoral system facilitated a one party government (operating with a single house in Parliament, the House of Representatives) with a sizeable majority to implement change following the virtual stagnation of the economy and rising debt levels with the previous government.

Douglas, as Minister of Finance, not only drove the development process, but utilised independent consultative and implementation bodies, drawing upon expertise outside of Government and the bureaucracy. This environment, along with the tenacity of the GST's architect, has been supported over the intervening 20 plus years, with the original GST conceptually remaining intact. Indeed research indicates that the bureaucrats took an activist role in policy-making in NZ at this time (and again in the period 2008-10 during which the Tax Working Group[46] operated), encouraging the move in the direction to low rates, broad bases and neutrality in tax policy.[47]

It is interesting to contemplate whether the same GST would be implemented in 2014 as that of 1986. Major changes since 1986 include the move to a MMP political system, which has led to coalition governments (or minority governments dependent on other parties for support). The 2014 General Election initially looked as if it had resulted in, for the first time under a Mixed Member Proportional (MMP) system, a single party having a narrow majority of the party votes, and thereby able to govern alone.[48] However, following confirmation of the impact of special voting, the National Party ended up with 60 out of 121 seats, meaning it needed to form a coalition government. It commenced signing agreements with several minor parties; as a result has formed a coalition government with 64 out of 121 seats enabling it to govern. It would be much more difficult to implement major policy changes, although the result of the Tax Working Group's (TWG's) recommendations in 2010 led to the largest tax policy reforms

[45] It should not be forgotten that a proposal for a single low rate, broad base income tax in 1987 led to the demise of the working relationship between the Prime Minister and Minister of Finance. This indicates that the approach that worked for the development of the GST will not necessarily work for other taxes. The NZ GST, with the increase to a rate of 15 per cent from 1 October 2010, contributes close to 25 per cent of tax revenues collected for the year ended 30 June 2014; see Treasury data from http://www.treasury.govt.nz/budget/2014/taxpayers/02.htm#_whopaystax (accessed 6 October 2014).

[46] See Tax Working Group, above n 28.

[47] Johan Christensen, 'Bringing the bureaucrats back in: neo-liberal tax reform in New Zealand' (2013) 32(2) *Journal of Public Policy* 141, 164-165.

[48] A feature of the MMP system has been (minority) coalition governments, with the major party needing to work closely with several other smaller parties to develop tax policy. Furthermore, Sawyer comments with respect to the operation of MMP:

"MMP is an 'additional member' voting system used to elect representatives to numerous legislatures around the world, including New Zealand. MMP is a form of proportional representation in that the overall total of party members in the elected body is intended to mirror the overall proportion of votes received. It includes a set of members elected by geographic constituency (currently 60 seats in New Zealand comprising 5 Maori seats and 55 general electorate seats) who are deducted from the party totals to maintain overall proportionality. Thus, the additional party seats are compensatory in that they 'top up' the electorate seat results to maintain overall proportionality. There are minimum thresholds, including the need to gain at least 5 per cent of the party vote to gain seats, unless an electorate seat is secured in which case there is no minimum threshold and party seats are provided to top up."

See Adrian Sawyer, 'Reviewing Tax Policy Development in New Zealand: Lessons from a delicate balancing of 'Law and Politics' (2013) 28(2) *Australian Tax Forum* 401, 406.

in over 25 years.[49] That said, several opposition parties and various lobby groups advocated for the introduction of exemptions into the GST for items such as fresh fruit and vegetables, and the further potential to include other basic food items and even property rates.[50] With the outcome of the 2014 General Election, any changes of this nature are not expected to be on the agenda until after the 2017 General Election at the earliest.

2.5 International perspectives

In the context of other countries that introduced a GST based on the NZ model, most have included exemptions and multiple rates, leading to a less than optimal GST from a tax policy perspective. Tenacity is also crucial, with the experience of Australia in 1990 a poignant reminder. The then Opposition leader (and potentially incoming Prime Minister) lost the "unlosable election" in proposing a GST, which suggests that timing and the accompanying package are crucial factors to success.[51] In 2000, GST was introduced in Australia based on the benefit of an extensive consultation, although the coalition composition of the Australian Government at that time led to a number of last minute concessions to enable the GST to be enacted, with the result being a less than optimal GST from a policy perspective.

The European Union (EU) had looked at the NZ GST model. PricewaterhouseCoopers (PwC) commented:[52]

> "New Zealand's bold policy approach in the 1980s – of a broad base/(low) standard rate model – will be a golden lesson to others; and the *New Zealand GST model will be at the forefront of study for European policymakers, which is a fascinating dimension* … [T]he New Zealand model was seen as best practice for a VAT/GST regime."

The EU has many problems of its own, taxation and otherwise, both within and outside its multiple jurisdiction members. Thus, it would be unlikely for the EU to focus its attention on

[49] For an overview of the key Budget 2010 tax changes, see Adrian J Sawyer, '2010 Budget Brings Biggest Tax Changes in 25 Years' (2010) 58 *Tax Notes International* 790. Major changes included a reduction in the top tax rate to 33 per cent (and other changes to rate thresholds), an increase in the GST rate to 15 per cent, the removal of depreciation for tax purposes on most buildings, changes to the taxation of certain companies and a number of related reforms, such as changes to the Fringe Benefit Tax rates. The Tax Working Group (TWG) had recommended that one option could be to introduce some form of land tax; land taxation had ceased to apply in NZ from 1992. This option was not adopted by the government.

[50] See for example the arguments raised by the Child Poverty Action Group arguing for a GST exemption on fruit and vegetables; http://www.cpag.org.nz/assets/Tax%20Issues/Backgrounder_GSTExemptions%20on%20Food%20final.pdf. This proposal led to extensive debate in the lead up to the 2011 General Election, with the Labour, Greens, Maori and Mana Parties all proposing various exemptions to GST (the latter seeking to replace GST with a financial transactions tax). The NZ First Party proposed reducing the GST rate back to 12.5 per cent. See also the following link with details on the policy proposal to remove GST from food: http://nzfirst.org.nz/policy/finance-and-tax. In the lead up to the 2014 General Election, several parties proposed changes to the GST (NZ First Party and Maori Party exempting GST on food (the former also on property rates); the Mana Party, which had formed an alliance with the Internet Party, continued with its proposal of replacing GST with a financial transactions tax).

[51] For a personal recount of the "failed" GST attempt in Australia in 1993, see John Hewson, 'The Politics of Tax Reform in Australia' (2014) 1(3) *Asia and the Pacific Policy Studies* 590, 593-4. See also Kathryn James, 'We of the 'never ever': the history of the introduction of a goods and services tax in Australia' [2007] 3 *British Tax Review* 320. John Hewson proposed a 15 per cent GST with minimal exemptions, accompanied by a reduction in income tax and a tidying up of indirect taxes. A scare campaign by the waning Labour Government saw them retain the government benches.

[52] Eugen Trombitas (PwC), 'GST: One of our Best Exports' (2012) *PwC Media release* (28 January) <http://www.pwc.co.nz/media-centre/opinion-pieces/gst-one-of-our-best-exports/> (emphasis added). The NZ Retailers Association has also called for the exemption from GST for imports less than $NZ400 (approximately $HK2,600) to be scrapped; see Hamish Rutherford, *Call to scrap GST policy on some imports* (January 2011) Businessday <http://www.stuff.co.nz/business/industries/4514945/Call-to-scrap-GST-policy-on-some-imports>.

major reform to its members' VATs until more pressing issues are resolved. Furthermore, while the NZ GST model is the closest to "perfection" from a tax policy design perspective, it can still be improved. That said, I would suggest that NZ's GST should be the blueprint to be used by jurisdictions when contemplating a GST/VAT or refining their existing GST/VAT. While NZ's GST is 'fit for purpose' for NZ, this does not mean it would be entirely appropriate for other jurisdictions, such as the PRC as it refines its existing VAT and related taxes.

3. New Zealand's Tax Policy Approach – the Generic Tax Policy Process

In this section of the paper, I set out a summary of the experience of the operation of the Generic Tax Policy Process (GTPP) in NZ, along with the approach and impact that the Tax Working Group (TWG) had as the most significant recent contribution to tax reform in NZ in the last five years.

3.1 The GTPP

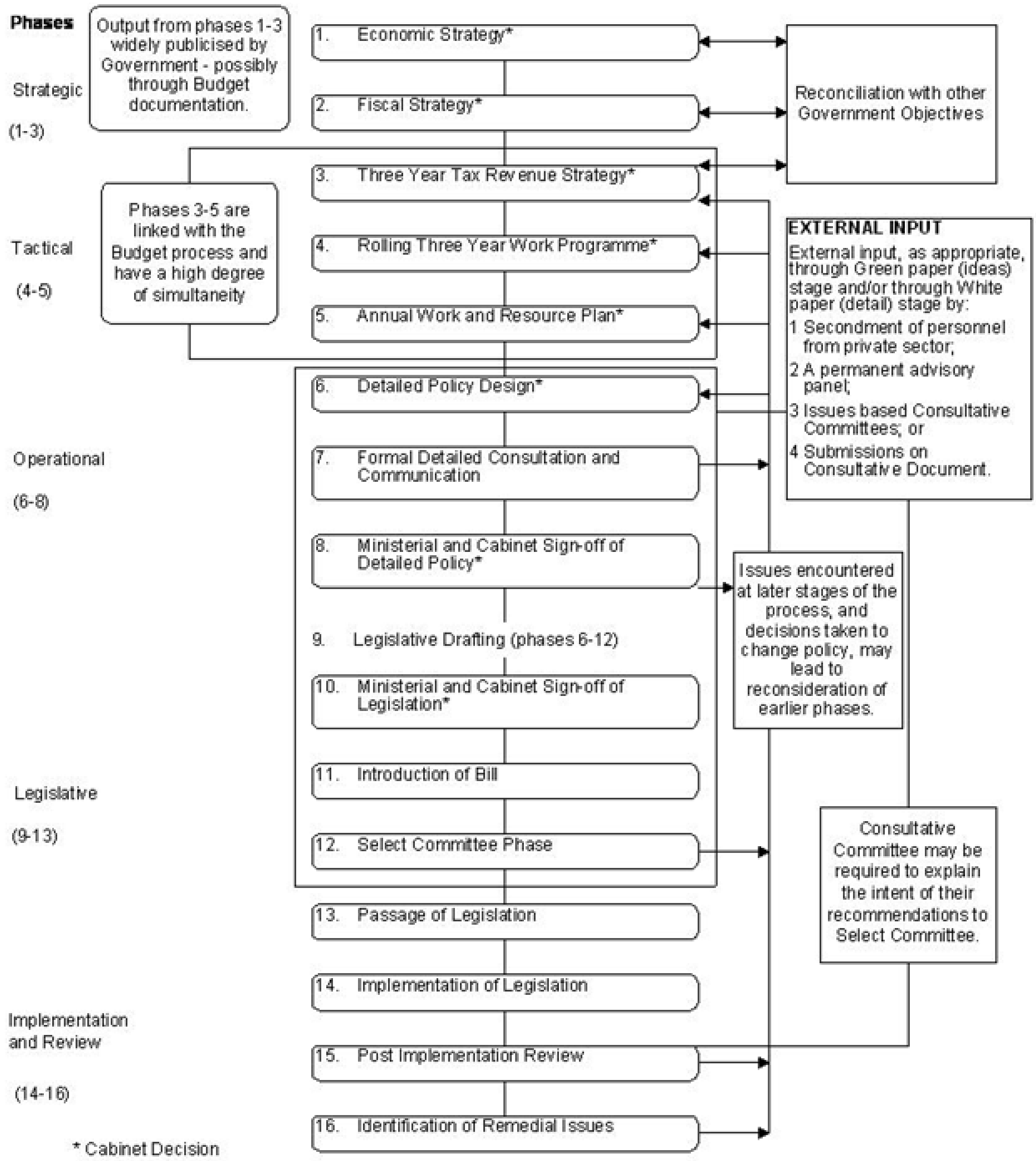
The following discussion is based on a recently published review of the NZ GTPP, reflecting upon its perseverance over the almost twenty years since it was first proposed, and subsequently adopted by the NZ Government. As I have commented elsewhere,[53] NZ chose to take a new and innovative route in the mid-1990s with the adoption of the GTPP, a blueprint for formulating tax policy. As noted in the introduction to this paper, the GTPP emerged as a bi-product of a review of the NZ Inland Revenue Department (NZIRD) conducted through the Organisational Review of Inland Revenue chaired by Rt Hon Sir Ivor Richardson.[54]

A Cabinet directive implemented the GTPP during the review process as a form of administrative or customary practice, rather than formally by way of legislation or regulation. This approach in part, as noted elsewhere, reflects both the strengths and weaknesses of the GTPP.[55] In part, the GTPP arose from consultation undertaken by the Organisational Review Committee with tax experts from both the private and public sectors. Importantly, the GTPP is in stark contrast to the previous policy environment, characterised by an absence of clarity and ascertainable accountabilities during each stage of the process. Furthermore, the perception was that the external consultation was insufficient to the extent of being virtually ineffective.[56]

With the GTPP, the NZ Government and officials are able to draw upon the technical and practical expertise of the business community, and to factor in compliance and administrative effects of potential policy changes. Furthermore, it also provides a mechanism to communicate the rationale for policy changes. The GTPP may appear to be complex and potentially unwieldy, but when examined closely, it provides a comprehensive and robust structure for the development, refinement and enactment of tax policy into legislation.[57] Figure 1 sets out the GTPP in diagrammatical form.

[53] Sawyer, above n 36.
[54] Rt. Hon Sir Ivor Richardson, *Organisational Review of the Inland Revenue Department, Report to the Minister of Revenue and the Minister of Finance* (April 1994). Sir Ivor Richardson was also instrumental in his oversight of the Rewrite Advisory Panel that worked alongside the NZ Government's fourteen year project to rewrite the Income Tax Act; for an analysis *see* Adrian Sawyer, 'RAP(ping) in Taxation: A Review of New Zealand's Rewrite Advisory Panel and its Potential for Adaptation to Other Jurisdictions' (2008) 37(3) *Australian Tax Review* 148.
[55] Sawyer, above n 36, 403.
[56] Ibid 403.
[57] For an in-depth early discussion of the various stages of the GTPP, *see* Adrian Sawyer, 'Broadening the Scope of Consultation and Strategic Focus in Tax Policy Formulation: Some Recent Developments' (1996) 2(1) *New Zealand Journal of Taxation Law and Policy* 17.

Figure 1: The Generic Tax Policy Process (Organisational Review Committee, 1994)



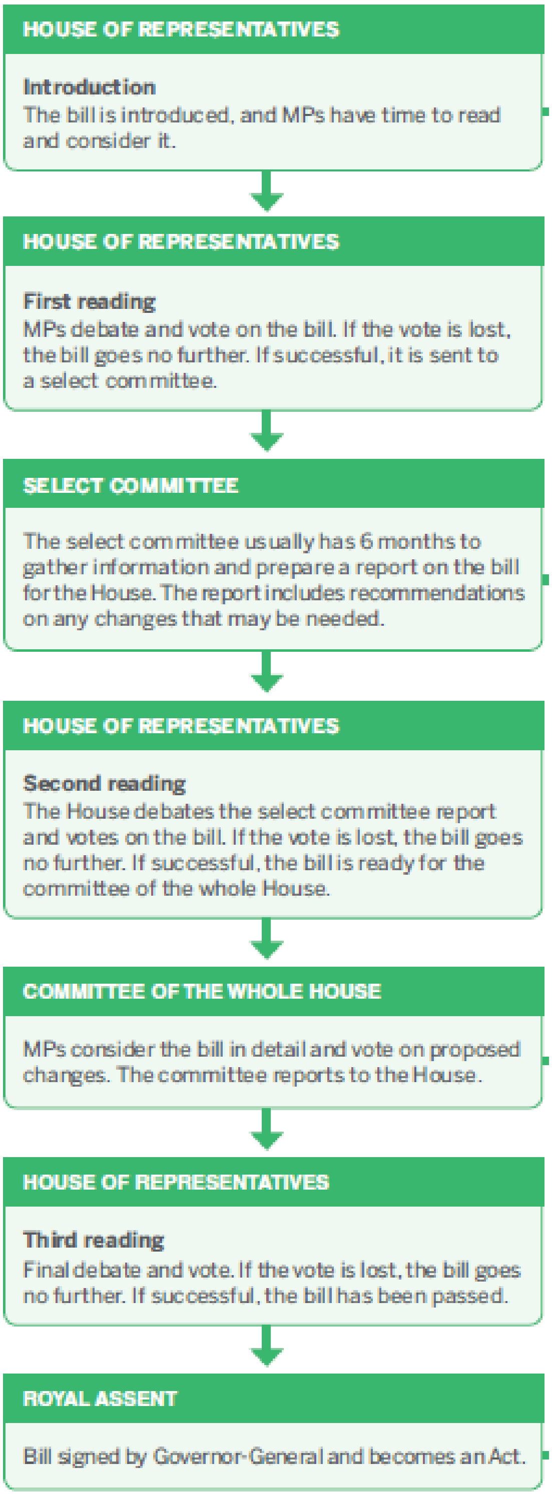
The GTPP has five core stages, each of which has their own phases, totalling 16 phases. The GTPP contains a number of external inputs and feedback loops, including a post implementation of legislation review. Throughout the GTPP, the linkages and feedback loops are intended to reflect a flexible process that recognises that some activities may occur simultaneously or in a slightly modified order, such as the timing of legislative drafting (within Phases 6–12). Essentially the GTPP is designed to improve the technical quality of the tax reform process, whatever the political background of the government at the time. Nevertheless, the subject matter of reform is usually firmly based on the economic, fiscal and revenue strategies of the government at the time (Phases 1–3). A further feature of the GTPP is the requirement for the government to announce annually its Rolling Three Year Work Programme.

Furthermore, the GTPP has three main objectives which stimulated the government's decision to adopt the process.[58] First, the GTPP encourages earlier and explicit consideration of key tax policy elements and trade-offs through linking the first three stages. Secondly, the GTPP provides an opportunity for external input into the process for formulating tax policy to increase both the actual and perceived transparency of the process, and provide for greater contestability and quality of policy advice. Importantly, consultation can occur at the initial stage of policy consideration, the detailed design stage, the legislative drafting phase, the select committee stage and the post-implementation review. Thirdly, the process sets out to clarify the responsibilities and accountabilities of the two major departments actively involved in the process, namely the NZIRD and the NZ Treasury.

Within the Passage of Legislation Phase (Step 13), there are several key steps, as set out in Figure 2, which follows:

[58] Sawyer, above n 36, 404.

Figure 2: Process for enacting government initiated changes to NZ's laws[59]



[59] NZ Parliament, *How a Bill becomes Law* (2014) <http://www.parliament.nz/resource/en-nz/00CLOOCHowPWorksLawsHow1/f072ccbc5a57287160d2511b5504c7de078915fd>.

One minor but yet important weakness in the GTPP is that late policy or legislative developments may be added by way of a Supplementary Order Paper (SOP)[60] during the parliamentary phase (post Select Committee), and as a consequence, such policy is not exposed to public scrutiny via formal consultation. Where the change is remedial and corrective of minor defects in existing legislation, this is not of significant concern.[61] However, with the introduction of significant new developments, this effectively bypasses the GTPP and is a real concern since this late political involvement may fail to maintain the technical quality of the legislation that the GTPP provides.[62] I have previously[63] reviewed the prior literature on the GTPP and examined why it has been successful and managed to survive the highly political policy environment that operates in NZ. One important element has been its adaptability to change to the various manifestations of political policy development in NZ, along with the electoral system, and a general acceptance of its merits from politicians across the spectrum.

A further challenge to the GTPP came about with the commencement of the MMP political system shortly after adoption of the GTPP in 1996. When the GTPP was introduced, NZ had a First Past the Post (FPP)[64] election system for its single house Parliament, the House of Representatives. However, since the 1996 General Election, all general elections utilise a MMP representation system. While MMP was anticipated to lead to less significant and much more protracted tax policy development, it has not prevented major tax reform in NZ. This is where the TWG, most recently, has complemented the contributions of the GTPP to tax policy development in NZ.

3.2 The Victoria University of Wellington Tax Working Group

Sawyer observed[65] that in 2009, following a conference held at Victoria University of Wellington (VUW), that it was decided to establish an independent group (known as the TWG) comprising experts from academia, NZIRD, NZ Treasury and tax practice, to undertake a review of the NZ tax system from a core principles policy focused perspective.[66] The TWG differed from earlier reviews of the tax system in NZ, such as the Tax Review 2001,[67] specifically in that it was not a NZ Government initiative, and that its terms of reference were self-generated. Furthermore, while the TWG received resource support from the NZIRD and the NZ Treasury, it operated separately from and outside the "government appointed

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[60] An SOP is a late legislative amendment introduced by the government at the Second Reading of the Bill stage (during Step 13 in the GTPP) after the Select Committee has reported on the Bill (i.e., after the consultation process has been completed). Step 13 in reality involves several steps, as shown in Figure 2.

[61] Sawyer, above n 36, 404.

[62] See the comments of Peter Vial, 'The Generic Tax Policy Process: A "Jewel in Our Policy Formation Crown"?' (2012) 25(2) *New Zealand Universities Law Review* 318.

[63] Sawyer, above n 36, 404–425.

[64] FFP is a system whereby the person who receives the highest number of votes for their electorate seat will win that seat. The party with the highest number of electorate seats will then be asked to form a government. If that party has more than 50 per cent of the electorate seats then it can become the government without needing to form a collation with one or more additional parties. Usually a government would be formed by a single political party that holds a majority of electoral seats.

[65] Adrian Sawyer, 'Moving on from the Tax Legislation Rewrite Projects: A Comparison of New Zealand Tax Working Group/Generic Tax Policy Process and the United Kingdom Office of Tax Simplification' (2013) 3 *British Tax Review* 321.

[66] Details of independent, Inland Revenue and Treasury members of the TWG can be found at "The Centre for Accounting, Governance and Taxation Research – VUW Tax Working Group" <http://www.victoria.ac.nz/sacl/cagtr/twg>. Details of the number of experts who assisted the TWG are also provided.

[67] The Tax Review 2001 (also known as the McLeod Review) was established by the NZ Government in 2001 to carry out a public review into the tax system. The functions of the Tax Review 2001 were to: examine and inquire into the structure and effects of the tax system in NZ; to formulate proposals for improving that system, either by way of making changes to the system, abolishing any existing form of tax, or introducing new forms of tax; and to report to the NZ Parliament through the Minister of Finance, the Minister of Revenue and the Minister of Economic Development. The terms of reference were set within the constraints of maintaining revenue neutrality with any recommendations for change; available at <http://www.treasury.govt.nz/publications/reviews-consultation/taxreview2001>.

committee" framework of earlier tax reviews.[68] It is arguable that this was a critical factor in its success, in that the TWG complemented the role of the GTPP which seeks to remove, as far as practicable, political influences on the process of tax reform (after the Strategic Phase), with respect to producing high quality legislation. In this regard, the TWG is not a necessity for an effective GTPP, but it facilitated the development of higher quality policy and legislation through its input into the GTPP.[69]

The TWG undertook widespread consultation and extensive reporting to government, which resulted in a series of recommended options for major tax policy reform.[70] The TWG sought to:[71]

(1) identify concerns with the current taxation system;

(2) describe what a good tax system should be like;

(3) consider options for reform; and

(4) evaluate the pros and cons of these options.

In its 2010 Report, the TWG concluded that NZ's tax system faced three critical issues:[72]

(1) its structure was inappropriate;

(2) it lacked coherence, integrity and fairness; and

(3) significant risks to the sustainability of the tax revenue base existed.

Consequently, the TWG established six principles for reform,[73] and made a number of significant recommendations for reform, including major changes to tax rates, structures and bases.[74] The TWG referred its recommendations, which included a series of options or combinations of structural tax reforms, to the NZ Government for its consideration.[75] Several months later, in its Budget delivered on 20 May 2010, the NZ Government announced a major overhaul of the NZ tax system, adopting many of the recommendations of the TWG.[76]

3.3 Interaction between the TWG and GTPP

Turning the focus on how the TWG operated within the GTPP, prior analysis[77] reviewed the comments on the contributions of the TWG within the GTPP environment from those involved

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[68] These operate within the External Input phase of the GTPP.
[69] Sawyer, above n 53, 323.
[70] Tax Working Group, *A Tax System for New Zealand's Future Report of the Victoria University of Wellington Tax Working Group*, (Centre for Accounting, Governance and Taxation Research, Victoria University of Wellington, January 2010) (*A Tax System for New Zealand's Future)*.
[71] See *A Tax System for New Zealand's Future*, above n 58, 19. For further details, *see* The TWG Report <http://www.victoria.ac.nz/sacl/cagtr/twg/report>.
[72] Ibid.
[73] The six principles are: the overall coherence of the system; efficiency and growth; equity and fairness; revenue integrity; fiscal cost; and compliance and administration costs.
[74] For a summary, *see* Tax Working Group, above n 58, 10–11.
[75] The recommendations were included in the TWG's January 2010 report that was publicly available; see Tax Working Group, above n 58.
[76] For details of the New Zealand Budget 2010 announcements, see <http://www.treasury.govt.nz/budget/2010>.
[77] Sawyer, above n 53, 322–327.

either as members of the GTPP, advisors, and expert consultants. Collectively, these commentators/academics emphasised the importance of the interdisciplinary backgrounds and expertise of those involved, the attempt to rationalise tax policy debate, and the engagement of the public in the debate. A major constraining factor with most reviews, the TWG being no exception, is the revenue neutral constraint placed on reviews. Focusing on addressing issues of fairness, especially horizontal equity, was also crucial to the TWG's success.

I have observed that the work of the TWG illustrates a recent example of the operation of the GTPP, through an extension of the usual external input into the policy making process, namely an independent temporary advisory body that has made one of the more significant contributions to tax policy development in NZ.[78] The GTPP has continued to operate largely unscathed under both left-of-centre and right-of-centre governments. Thus, it is my contention that the GTPP (even without the TWG), has facilitated a surprisingly high level of tax policy review that in turn has led to significant structural and legislative tax reform. This is all the more remarkable in that NZ operates under a MMP system that usually leads to coalition (minority) governments, although the outcome of the most recent 2014 General Election offered the party with the largest party vote the opportunity to govern alone.

Overall in this paper, I argue that the GTPP (even without the contribution of the TWG) is genuinely world-class, illustrating how politics can be separated from much of the tax reform and review process. Nevertheless, this comment should not be interpreted as indicating that taxation is not inherently political – policy ideas will almost always be put forward by politicians and governments. In that regard, the GTPP offers an alternative approach from which other jurisdictions, such as the PRC, may be inclined to examine further.

4. Insights from the New Zealand GST Experience and Policy Approach

4.1 Why has NZ's GST been so 'successful'?

What can be said about the success of NZ's GST? First, extensive consultation was undertaken prior to implementation – this included key policy framework and later a detailed operative structure emerged.

Secondly, the consultation led to minimal compromise with NZ's GST, where there was arguably greater focus on efficiency, and less so on equity. To support this observation, NZ has a C-efficiency rating of around 99 percent from OECD – no other GST/VAT comes close. However, this is at the expense of taxpayer equity/fairness in relation to lower income earners. Most other jurisdictions have adopted a more equitable, and less efficient and simple GST/VAT.[79] This may suggest that taxpayers (and the government) in those jurisdictions are 'different' than those in NZ. This may be the result of a range of factors such as different patterns of industrialisation and urbanisation, and different perspectives regarding such issues as the expected roles of government in areas such as income redistribution, food pricing, agriculture and 'essential' goods and services.

Establishing itself as the international benchmark, no other jurisdiction has had the same level of political will to recommend and retain a theoretically pure GST from an efficiency perspective. As far as I am aware no non-OECD member country has a GST/VAT that comes close to the NZ GST on the basis of this measure, but whether this is the most appropriate

[78] Ibid 329. See also Vial, above n 50.

[79] For comments on the UK's reasons for implementing their VAT, see Simon James, 'The contribution of behavioural economics to tax reform in the United Kingdom' (2012) 41 *The Journal of Socio-Economics* 468, 472-474.

measure to assess a VAT/GST is a debatable point. Other measures, such as the degree of equity, may be more appropriate for some jurisdictions.

Thirdly, the economic environment of the time of proposing the VAT/GST is an important factor. New Zealand was facing a dire situation economically and fiscally in 1984, whereas few countries that implement a VAT/GST have been in that situation at the time. The PRC is certainly not in a similar situation as that of NZ at that time.

Fourthly, there is evidence of the success of the NZ approach through the sustainability of the consumption tax. Thus, even after nearly 30 years of operation, only minimal changes have been made, largely to increase the rate, expand the base and clarify some key concepts.

This paper does not seek to evaluate the PRC's current VAT and associated taxes. Not only would such an analysis be outside the motivation for this paper, it is not within the author's expertise to do so. Nevertheless, given the PRC is seeking to rationalise and streamline its current consumption taxes, NZ's experience may prove instructive for the PRC. Table 1 which follows summarises the key aspects of the NZ GST experience with some very tentative comparison of the current environment and fiscal situation faced by the PRC:

Table 1: Comparative analysis of NZ GST v PRC VAT

Evaluation characteristics	NZ	PRC
Economic environment	Economy in difficulty, heavy reliance on income tax creating a narrow tax base, a heavily regulated small economy	A rapidly growing economy in need of raising additional revenues to finance ongoing growth and provision of services. Second largest economy in the world
Debt structure	Heavily indebted at Government level, with debt reduction programme in place from 1984 (increased following 2008 Global Financial Crisis and 2010–11 Canterbury earthquakes)	Debt levels relatively low with considerable offshore investment. May need to raise finances overseas to fund domestic demand if growth rates decline significantly
Constitutional environment	Parliamentary system with one House of Representatives based in Wellington	Taxation legislation should be made by NPC and its Standing Committee as part of a centralised Communist Party (State Council) based in Beijing. State Council introduced the VAT and other taxes/duties
Political structure	Domination by two parties, under First Past the Post (FPP) system; proposal developed and implemented within parliamentary term. Now a Mixed Member Proportional (MMP) model with coalition governments	One party system with varying degrees of delegated authority to provinces, municipalities and counties
Role of consultation	White paper released, independent consultative committee, publicity committee and period to refine legislation of over 2 years	Directives issued by Central Committee of the Communist Party. State Council is both legislative and law enforcement agency. Implementation by State Administration of Taxation (SAT) and Ministry of Finance (MoF) – no formal consultation
Publicity campaign	Independent committee to coordinate all aspects of development and implementation; little in way of opposition	Little in the way of publicity other than announcement of policy direction. Use of VAT Pilot Reform
“Purity” of GST	Purist model of GST ever proposed, minimal exemptions	A mix of business tax and VAT, with varied bases and rates - proposals for change do not suggest a “pure” VAT
Reform package	Extensive reduction in income tax rates, compensation packages for households – revenue neutral approach	Issue under discussion – will need to be some changes in distribution of revenues between localities and central PRC. Some tax cuts expected

While Table 1 indicates very different environments and fiscal situations faced by each of NZ and the PRC, one important common feature that should not be overlooked is the political environment whereby one party had the ‘mandate’ to implement change. In NZ, this facilitated the broadening of the tax base via introducing a comprehensive and ‘pure’ GST, while the

Communist Party in the PRC occupies the position of sole arbiter of tax policy. Where the PRC has a 'choice' is in regard to the extent to which consultation is utilised and the process by which changes to the current consumption taxes are implemented. Qiu observed that:[80]

> "[t]he unique feature in the interpretation of tax laws in China is that administrative organs have enjoyed a near monopoly status in interpreting rules. *Problems arise due to the high centralization of powers and the lack of effective checks.* These problems include ultra vires interpretations, inconsistencies among the rules, retroactive application, infringement to taxpayers' rights without available channels for remedies, etc."

In this context, Qiu highlighted an important development, namely the "…general awakening of awareness among Chinese citizens of their 'rights as taxpayers' in recent years."[81] This includes the supervision of administrative bodies from civilians, tax professionals and non-government entities. Qiu concluded with the observation that "… the integration of China into the international tax community requires the government to be *more attentive to international norms and the practice in other countries*."[82]

In this regard NZ's experience, as an example of best practice with regard to GST, offers a potential blueprint for the PRC. However, such consideration will necessarily require adaptation to incorporate significant cultural and constitutional variances between the two jurisdictions. Importantly, in terms of the policy process, there is little similarity between NZ and the PRC. Nevertheless, the NZ experience and approach offers a well-tested and resilient approach to modern tax reform that has operated since 1994.

An important observation is that both the GTPP (and to a lesser extent the TWG) are structures that emerged following recommendations of review groups that were not set up by the NZ Government to reform tax policy. The GTPP was a recommendation from the Organisational Review of the NZIRD,[83] and arguably while it was not the most significant of its recommendations for the NZIRD and the NZ Government, it is one that has had a substantial impact on tax policy development in NZ since its adoption in 1994. That said the GTPP's course has not always been one that is smooth sailing, with a number of obstacles and challenges faced along its journey, especially in 1999–2000 and more recently in 2010.[84] One factor behind its resilience[85] can be attributed to the insights and perceptions of the GTPP's architect, Sir Ivor Richardson.

Furthermore, its strength is attributable to NZ's constitutional framework and unicameral Parliament, along with the conscious decision that each Government have made to using it as the basis for tax policy development. Nevertheless, the relative ease with which a government can bypass or circumvent the GTPP's processes demonstrates its major weakness, and to that extent, demonstrates the GTPP's relative 'fragility'.

Little et al made the following comment in relation to the transportability of the GTPP:[86]

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[80] See Dongmei Qiu, 'Interpretation of Tax Law in China: Moving towards the Rule of Law?' (2014) 44(2) *Hong Kong Law Journal* 589, 620 (emphasis added).
[81] Ibid 616.
[82] Ibid 620 (emphasis added).
[83] See Richardson, above n 2.
[84] For a discussion on the GTPP's most recent "failing", see Vial, above n 50.
[85] See Sawyer, above n 53, 329.
[86] Little et al, above n 4, 1055 (emphasis added).

> "When considering the transportability of the GTPP, it is important to recognize that because New Zealand's relatively small size facilitates interactions between key tax practitioners and officials, *it is easier for the GTPP to work in New Zealand than would likely be the case in a much larger economy*. The GTPP also works well in New Zealand because there is a clear and coherent policy paradigm that is well understood, and the private sector has bought into the process. To that extent, policy settings that are amenable to the GTPP will be less flexible than would otherwise be the case."

While there are substantial differences between the legislative and constitutional frameworks in NZ and the PRC, I do not see these differences as necessarily preventing the development of a tax policy process based upon the GTPP model that could fit within the PRC's constitutional and legislative structure, assuming that transparency and broader consultation are considered to be essential features of tax policy development. Assuming this is the case, it is my humble suggestion that greater transparency and consultation be undertaken by the SAT and the Communist Party with respect to tax policy development. This would include undertaking a rigorous analysis of the PRC's tax system, and releasing papers and consultation documents from which submissions and feedback is sought from those within the wider Communist Party and outside these organisations and structures. Underlying the research that lies behind any policy proposals should be econometric analysis, regulatory impact analysis, and an evaluation of the issues and implications of each option for reform.[87] The literature on the PRC's VAT is growing; a major focus is on reforms to broaden the base.[88] In the context of the VAT, this should include utilising the experience and data gathered from the VAT Pilot Reform.[89] Conclusions on the best options need to be based on the analysis, as well as reflect the fundamental principles adopted for the analysis (principles that should be widely accepted, such as equity, certainty, efficiency, and simplicity).[90]

Turning to the TWG,[91] this is the most recent example of the vehicle for initiating major tax policy reform in NZ that feeds into the GTPP, but one that departs from most of the prior examples in that it was instigated from outside of the NZ Government. The NZ Government

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[87] For prior research on the effectiveness of such measures in tax policy reform, *see* for example, Adrian Sawyer, 'Compliance Cost Impact Statements in New Zealand – How far have we come?: Tribute to Cedric Sandford' (2002) 17(4) *Australian Tax Forum* 441; and Adrian Sawyer, 'Regulatory Impact Statements and Accountability: Recent Australasian Evidence' (2008) 11(1) *Journal of Australian Taxation* 42. Regulatory Impact Analysis (RIA) refers to analysis undertaken prior to enacting a regulation or law. The role of an RIA is to provide a detailed and systematic appraisal of the potential impacts of a new regulation in order to assess whether the regulation/legislation is likely to achieve the desired objectives. Regulation/legislation commonly has numerous impacts and detailed study and consultation with affected parties is important to reveal these issues. From an economic perspective, it is important to identify whether the regulatory costs exceed the benefits. RIA is frequently comparative, with analysis of the different ways in which the desired objective may be achieved.

[88] For further details on VAT reform in the PRC, see for example: Bolivia SW Cheung and Alice PL Cui, 'A Comparison of the International Monetary Fund and the People's Republic of China VAT Policies' (2004) 30 *International Tax Journal* 10; Wei Cui, 'Business Tax: China's Quasi-VAT' (2009) *International VAT Monitor* (July-August) 291; Xu Yan, 'Putting the 'Value Added' in China's VAT' (2010) *Tax Notes International* (May 10) 487; Wei Cui, 'Learning to Keep the Consumption Tax Base Broad: Australian and Chinese VAT Design for the Housing Sector' in Christine Peacock (ed,), *GST in Australia: Looking Forward from the First Decade* (Thomson Reuters, 2011); Bin Yan and Eva Huang, 'Characteristics of the Chinese Tax System and its Cultural Underpinnings: A Comparison with the West' (2011) 1(1) *Journal of Chinese Tax & Policy* 13; Bin Yang, 'Extending the VAT to Services in China: Special Difficulties and Choices' (2012) 2(1) *Journal of Chinese Tax & Policy* 2; Nolan Sharkey, 'Localization of central taxation in China' in Nolan Sharkey (ed) Taxation in ASEAN and China (Routledge, 2012); Kenny Z Lin and Pauline WY Wong, 'Recent Reform in Chinese VAT Policies' (2012) *International Tax Journal* (July-August) 39; Sarah Chin and Polly Wan, 'How is China's VAT Reform Progressing?' (2013) 17(2) *Asia-Pacific Journal of Taxation* 22; and Bert Brys, Stephen Matthews, Richard Herd and Xiao Wang, 'Tax Policy and Tax Reform in the People's Republic of China' (2013) *OECD Taxation Working Papers No 18*.

[89] See for example, Fuqiang Zhang and Menglu Li, 'The Top-Level Institutional Design of the Perfection & Expansion of VAT Reform Pilot' (2014) 8(1) *International Business and Management* 1.

[90] These fundamental principles have their origins in the work of Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* (1776: 1910 reprint).

[91] See Tax Working Group, above n 58.

set up the prior tax review, the Tax Review 2001,[92] and therefore the terms of reference were determined by the government in place at that time. As noted earlier, while the Tax Review 2001 made a number of recommendations, it comprised a mix of left- and right-of-centre members. Given the political views of the left-of-centre government at the time, few recommendations were implemented, and its terms of reference were narrowly constructed.[93]

A major advantage of the TWG, therefore, was that it was set up by a major NZ university (VUW), which was independent of the NZ Government. Of importance too was that VUW had the support of the then Ministers of Finance and Revenue, along with government officials, tax practitioners and academics (throughout NZ and overseas). Throughout the process, the TWG was consultative, making available papers for its various meetings (many of these papers were very technical, with summaries provided), issuing both an interim report and final report, in which options were presented to the Government for its consideration.[94] The NZ Government, therefore, while making information available to the TWG via officials, was in a sense a step removed from the process. The NZ Government was able to reflect upon the recommendations of the TWG without the restrictions placed on it if it had established the terms of reference and controlled the policy analysis process.

Nevertheless, it should be pointed out that the NZ Government at the time was right-of-centre, and had signalled that it would be receptive to a review of the tax system, recognising that there had been no major review or change for the preceding 25 years.[95] With a largely right-of-centre composition of the TWG, the environment at the time was also right for reform. Whether this would be true with a left-of-centre government at some future time remains unclear. This may become critical if a CGT proposal is formally tabled and opened for submissions as part of a consultation process that would inform NZ Government policy that is then fed into the GTPP.

A further critical element is that once a government initiates or endorses a review of the tax system, it needs to be resolute and committed to seeing the process through to the end. This does not mean that it cannot accept valid feedback through consultation and modify its approach and the options. Indeed if it does not do this, then the consultation process is not genuine and the reform process will be undermined.

It should be clear that the preceding discussion does not attempt to review the effectiveness of the PRC's VAT reform to date. Much has been written on this topic which provides valuable insights and issues for consideration, but this is beyond the scope of this paper.

5. Conclusions

Tax reform is a difficult area for any government to engage in, not surprisingly, as taxes are inherently political and reflect to varying degrees what a society expects its government to provide by way of goods and services. However, it would be naive for any government to believe that its tax system can be entirely the product of its own preferences, since almost all jurisdictions interact with one another (as do businesses), and taxpayers frequently hold assets in numerous jurisdictions. It is also unreasonable, and arguably impertinent, for another jurisdiction, individual or researcher, to suggest what another independent jurisdiction should

[92] See Tax Review 2001, above n 55.

[93] See Tax Review 2001, *Issues Paper* (2001), Chapter 1: Frameworks, 5–26.

[94] These reports are available from: "The Centre for Accounting, Governance and Taxation Research – VUW Tax Working Group <http://www.victoria.ac.nz/sacl/cagtr/twg>.

[95] For a comment on the largest tax changes in NZ for 25 years, *see* the commentary on the 2010 NZ Budget by Adrian Sawyer, '2010 Budget Brings Biggest Tax Changes in 25 Years' (2010) 58 (7 June) *Tax Notes International* 790.

do with respect to its tax system or how it should respond to global tax developments. However, this does not mean that one jurisdiction cannot learn from events, processes and developments in another jurisdiction, and evaluate whether this would be suitable/adaptable for their own jurisdiction and its tax system. In many instances, researchers, including academics, lead or promote such comparative research.[96]

Implementing any form of tax reform is a balancing exercise that in part reflects: the political will of the government; the competing pressures facing the economy; and the level of planning and willingness to allow genuine public consultation in refining the policy and subsequent legislation. New Zealand's experience with GST, while positive from the perspective of the purity of the GST and successful implementation, is not entirely without good fortune and trade-offs. New Zealand's GST focuses on efficiency with a trade-off that the tax is less equitable (indeed there is a strong argument that in isolation its effect can be regressive on low income earners; this is addressed through the income support and guaranteed minimum family income measures).

Having the chief proponent as a key member of the Government, in this situation the Minister of Finance, was crucial to advancing the initiative and resisting the pressure to acquiesce to the demands of various protest groups. Radical reforms, such as NZ's GST at the time of implementation, are usually much easier when they are made early on in the election cycle, rather than straddling over a major election when there is a risk of change in government. Politicians are usually more focused on re-election than major policy initiatives when these have the potential to significantly influence voters' decisions. In the case of the PRC, this is not such a critical issue, although the best timing for implementation of a major change in taxation will be important.

A second observation is that the approach to consultation is critical; NZ was a purist in its approach, benefiting from the prior VAT experience such as that with the UK. It took two to three years from the point of initial policy announcement to introduction. In particular, the extent of consultation and publicity facilitated by bodies' independent of the government, but made with the strong backing of the government and associated bureaucracy. Furthermore, the period for consultation did not need to be compromised by the forthcoming intervention of an election that could have led to a change in government. The choice of name for the NZ tax is not an accident; NZ sought to distant itself from the VAT concept in the UK and elsewhere, devising the concept of a goods and services tax (this is what the tax is levied upon, rather than the portion of value which it taxes), and forming the new international benchmark and nomenclature. Thus for the PRC, the consultative process undertaken will be a critical component to the level of 'acceptability' and potentially 'workability'.

Consultation is a critical part of NZ's tax policy process, the GTPP. As discussed earlier in the paper, this consultation is critical to both the policy development and draft legislative phases. It involves submissions and feedback from organisations and persons outside of the bureaucracy, including the potential set up of special bodies with a mandate to develop policy proposals for a government to consider. Thus, outside of GST/VAT, having a transparent and effective tax policy process could be a major catalyst in improving all tax policy development and implementation.

[96] See for example, Cedric Sandford, *Why Tax Systems Differ* (Fiscal Publications, 2000); Carlo Garbarino, 'An Evolutionary Approach to Comparative Taxation: Methods and Agenda for Research' (2009) 57(3) *American Journal of Comparative Law* 415; and Kathryn James, 'An Examination of Convergence and Resistance in Global Tax Reform Trends' (2010) 11(2) *Theoretical Inquires in Law* 475.

A third factor is the economic environment of the time and the associated government indebtedness. In 1984, NZ was facing its worst financial crisis since the substantial oil price increases during the early 1970s. With immense pressure economically and fiscally, this necessitated radial change for the country's survival. With the PRC looking to 'modernise' its taxation system, rationalising various turnover and other taxes in a manner to create a tax closer to a standard VAT, it represents a key step in this process.[97] Furthermore, a VAT/GST is not something that needs to be seen as having only short term objectives, but rather for the PRC, it may serve to prepare the jurisdiction for future demands on its resources, as well as potentially change the tax mix and relative burdens on taxpayers. For NZ, as noted earlier, the economy was facing a severe financial crisis in all major areas, including huge debts, an over-valued currency, negative trade balances and insufficient tax revenues to meet expenditure needs. Major tax reform was a necessity, not one of a series of choices that the then incoming Labour Government could select from.

Evidence that NZ's approach was successful with implementing its GST is also emphasised by the sustainability of the GST over its almost thirty years of existence. Subsequent amendments have largely been remedial to improve the operation of the GST and to further reduce its minimal number of exemptions.[98] A GST/VAT also assists with maintaining the integrity of the tax system through reporting requirements and links with the associated income tax obligations of GST registered taxpayers. Establishing itself as the international benchmark, no other jurisdiction has had the same level of political will to recommend and retain a theoretically pure GST from a policy perspective as NZ. Furthermore, as far as I am aware, no non-OECD member country has a GST/VAT that comes close to the NZ GST on the basis of this measure.

Successful tax reform also requires a package of reform, a characteristic common to both proposals. Since NZ and the PRC are contrasting economies (the former a small open economy and the latter a large planned economy), this suggests that the literature that pertains to tax reform for such economies will differ. Nevertheless, one could argue NZ made good use of the knowledge offered by the literature and international experience concerning VATs, and since the enactment of the GST, much of the tax policy literature now has NZ's GST as a focus.

How might the PRC develop a more comprehensive and cohesive VAT/GST? This paper suggests that in learning from a jurisdiction that has successfully implemented a GST, the PRC government should closely examine the NZ experience as part of the policy development process. A 'simple' and efficient GST would align with the relative simplicity of the PRC's tax system, although this should not be at the expense of addressing equity concerns. Depending on issues such as rate and thresholds, the majority of businesses in the PRC could either be required to register or be able to stay out of the GST/VAT system when it comes to registering and accounting for VAT/GST.

It is important that I acknowledge that I am an 'outsider' with limited knowledge and experience of the operations of the PRC with respect to developing tax policy and

[97] See Genevieve Lee, 'China's Transition from Turnover Taxes to VAT' (2012) 67 *Tax Notes International* (September 10) 1033.

[98] A significant review was conducted in 1999 when the issue of financial services, amongst others, came under the spotlight. Marie Pallot and Hayden Fenwick comment on the review and the changes that came about by way of remedial legislation. The authors, who come from Inland Revenue, observe that "Over the nearly 14 years since its introduction, GST has proven to be an efficient and relatively problem-free tax to administer, as well as a key contributor to Government revenue"; see Marie Pallot and Hayden Fenwick, 'Recent GST Reforms and Proposals in New Zealand' (2000) 10(1) *Revenue Law Journal* 88, 97.

administering taxes. Furthermore, my experience of the PRC's reforms with respect to VAT has its foundations in my review and analysis of the research contributions by a number of experts. In contrast, my experience with NZ's GST is extensive, including that of a NZ consumer affected by the GST, as well as individual and joint comparative researcher that has compared GST/VAT in other countries, such as Australia, the HKSAR and the UK.

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