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New Zealand's GST by way of Comparison to Japan's Consumption Tax

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The aim of this study is to grasp characteristics of New Zealand's economic reforms, tax reform, and the Goods and Services Tax and to get useful information from it. The Goods and Services Tax, GST, of New Zealand is the same type tax as the Consumption Tax of Japan (SHOUHIZEI).

The introduction of GST in 1986 formed a very important part of the tax reform, and the tax reform was a key area of the economic reforms which are known all over the globe today. The policy mechanisms of the tax reform were: a broadening of the entire tax base, in other words, reduction of tax concessions; reduction of tax rates; a switch toward a greater reliance on consumption rather than income taxes. These were done to weaken a negative impact of tax on spending and investment decisions of people and companies.

The GST's tax base is broader than that of Japan's Consumption Tax. The even lower threshold of the size of exempted traders and the more taxable items attract our attention. My current interest lies in whether or not New Zealand will be able to maintain an actual single rate when the rate of GST is increased.

I New Zealand Overview and Characteristics

An overview of New Zealand is shown in Table 1. In particular, as the result of the referendum in 1993, New Zealand introduced a form of proportional representation. After the first election under this system in 1996, the multi-party era in New Zealand started instead of the two-party era (Labour and National). We have to note that these two parties have actually conducted sweeping and radical reforms since 1984.

In New Zealand, the ratio of exported (or imported) goods and services to GDP is fairly high. With respect to this point, I would like to quote the following comment.

> It will already be apparent that the New Zealand economy is vulnerable to changes in the global economy. This is because international trade is very important to New Zealand (Dalziel and Lattimore [1997], p.7).

New Zealand has depended a great deal on international trade. Therefore, New Zealand

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has been greatly influenced by changes in external circumstances . I think.as referred in the latter chapter, it is one of the most important points when we consider New Zealand's reforms.

Table 1 New Zealand Overview

Location	1,900Km east of Australia
Land Surface Area	268,676 sq.Km (70 % of Japan)
Population	3.8 million in 1999, similar to that of Shizuoka Prefecture in Japan
Ethnic Groups	European : 79 %, Maori : 13 %, Pacific Islanders : 5 %, Others (including Asian) : 3 %
Prime Minister	Helen Clark
Government System	A central government and 86 local governments (Japan : a central government and 3,300 local governments)
Political System	Single-chamber system, a form of proportional representation (120 seats in all)
Gross Domestic Product	
GDP(1997)	US $ 65.1 billion (1.6 % of Japan's GDP)
GDP/Capita	US $ 17,324 (about a half that of Japan)
External Trade	
Exports(1997)	Exports of goods and Services were 23.6 % of GDP (Japan : 8.7 %)
Imports	Imports of goods and Services were 24.4 % of GDP (Japan : 7.0 %)
Composition of Exports	Raw and processed pastoral and wood products
Composition of Imports	Machinery,mineral fuels,and vehicles
Capital flow balance (1996)	US $ 4,321 million,which means capital inflow exceeds outflow (Japan : −US $ 31,390)

II Economic Reforms

New Zealand has conducted sweeping and radical economic reforms since 1984.

As a background to the reforms, we have to focus on New Zealand's serious economoic situations at that time as well as some circumstances such as the political system and

Table 2 Index of Economic Freedom 1997 Ranking

Free		Most Free	
1	Hong Kong	9	Bahamas
2	Singapore	11	Czech Republic, Denmark, Japan, Luxembourg
3	Bahrain		
4	New Zealand	15	Canada,Belgium,UAE
5	Switzeland, US	18	Australia, Austria
7	UK, Taiwan	19	Ireland, Germany

Source : Johon and Stewart [1997] ,p.29.

the initiatives of political leaders of New Zealand. For example,

- low economic growth (in particular, negative growth in 1978)
- high inflation rate (20 % in 1977)
- annual budget deficit (−8.8 % to GDP in 1984)
- rapid increase of overseas debt since 1970's

Prior to England's membership in EEC, England gave an advantageous international trade positon to New Zealand. However, England's EEC membership, together with two oil crises, caused the serious economic problems for New Zealand. To solve these problems, New Zealand has conducted reforms.

The decisive measure of the reforms was the liberalization of markets which made markets thoroughly open and free. It was considered to increase productivity of industries. In addition to that, public sector's efficiency was pursued. Since then, the government of New Zealand has given up strong control and regulation policies to markets and industries and an ideal as a welfare state.

The contents of the reforms were as follows :

- removal of agricultural subsidies
- removal of tariffs
- central bank reform (policy target of central bank became the control of inflation only)
- budget reforms (government expenditure cuts, social welfare cuts, and so forth)
- reform of public sector organizations (corporatizations and privatizations of public organizations)
- deregulation
- tax reform, and so on.

As the result of the reforms, New Zealand has become one of the most free countries economically and now is an ideal welfare state no longer (see Table 2).

Ⅲ Tax Reform and Introduction of GST

New Zealand's tax reform was a key area of the economic reforms.

The philosophy behind the tax reform was that tax should be as neutral as possible in terms of its impact on spending and investment decisions. For instance, consumers usually purchase exempted or lower tax rated goods and services and investors are likely to invest in lower tax rated industries. It means that the decision-making of people and companies is distorted by the tax and a lot of money is used for the industries protected by government instead of industries with actual potential. It is inefficient.

The policy mechanisms to promote neutrality were as follows :

- a broadening of the entire tax base by abolishing some concessions available to particular taxpayers including people and companies
- reduction of high income tax rates which was done to give people and companies the incentive to work harder and to produce more
- a greater reliance on consumption tax rather than income taxes, because income taxes were considered to have a negative incentive to work and to save

Regarding direct taxes, some special treatments, such as the life insurance tax exemption and the tax concessions to the petroleum and mining industries, were abolished. In addition, the high tax rates of personal income tax and company tax were

Table 3 Personal Income Tax

	Tax Rate	Taxable Income Bracket
New Zealand	15 ～ 33 %	3
Japan	10 ～ 37 %	4
US	15 ～ 39.6 %	5
UK	20 ～ 40 %	3
Germany	23.9% ～ 53 %	increase by a formula
France	10.5% ～ 54 %	6

Table 4 Corporate Income Tax Rate (including state and local taxes)

New Zealand	Japan	US	UK	Germany	France
33.00 %	46.36 %	40.75 %	31.00 %	51.67 %	41.2/3 %

reduced. For example,

- the company tax rate : 45 % → 33 %
- the top rate of personal income tax : 66 % → 33 %.

The introduction of GST in 1986 formed a very important part of the tax reform. After the adoption of GST instead of the Wholesale Sales Tax , New Zealand came to depend on GST which has a broader tax base.

Ⅳ Tax Base of GST

Table 5 Ratio of Revenue of GST / Japan's Consumption Tax to Consumption 1996

	Consumption of New Zealand and Japan(A)	Tax Revenues	Revenues in a case of 5% tax rate／(A)
GST of New Zealand	NZ $ 69,180 million	NZ $ 7,270 million (tax rate : 12.5 %)	4.2 %
Japan's Consumption Tax	¥ 350 trillion	¥ 7,560 billion (tax rate : 5 %)	3.6 %

Basically, New Zealand's GST and Japan's Consumption Tax cover almost all goods and services produced in their countries annually as a tax base.

Actually, GST has a broader tax base compared to Japan's Consumption Tax. In other words, Japan's Consumption Tax has more exemptions. We can confirm this fact by Tables 5 and 6.

As shown in Table 5, 4.2 % and 3.6 % indicate that the ratio of revenue of GST to New Zealand's consumption was higher than that of the Consumption Tax of Japan. This means the GST's revenue was based on 4.2 % of the consumption of New Zealand in 1996 . The figure was larger than that of Japan's Consumption Tax.

With respect to Table 6, we particulary have to pay attention to the lower threshold of the size of traders providing relief from taxation and a greater number of taxable items in New Zealand.

For example, the ceiling of exempted traders size under New Zealand's GST is far lower compared to Japan's consumption Tax. It is 1 / 14. Regarding the taxable items of GST, the taxation on sale of land attracts our attention. This is because many countries don't regard the sale of land, in other words, the use of land, as consumption and it is not considered to be a target of consumption taxation. Actually, the "standard exemptions" defined by OECD include the supply of land.

Table 6 Comparisons between the Tax Bases of the Two Taxes

	GST of New Zealand	the Consumption Tax of Japan
Size of trader poviding relief from taxation	up to NZ $ 30,000 (¥ 2.22 million)	up to ¥ 30 million
Standard rate	12.5 %	5 %
Lower rate	7.5 % (services for long term stay in commercial dwelling)	—
Exemption other than "standard exemptions" *	Supply of fine metal (gold, silver, and platinum)	Social welfare services
Taxation of "standard exemptions"	• Postal services • Medical care • Dental care • Charitable work(other than unconditional gifts) • Education • Non-commercial activities of no-profitmaking organisation (other than unconditional gifts) • Cultural services • Insurance and reinsurance (other than life insurance and reinsurance) • Letting of immovable property (other than residential accommodation) • Lotteries and gambling • Supply of land and buildings (other than land and buildings which have been used for provision of residential accommodation for five years or more)	• Letting of commercial buildings • Postal services • Non-commercial activities of no-profit making organisations • Cultural services • Supply of buildings

* "Standard Exemptions" defined by OECD are the following : postal services, medical care, dental care, charitable work, education, non-commercial activities of no-profit making organisations, cultural services, insurance and reinsurance, letting of immovable property, financial services, lotteries and gambling, supply of land and buildings. OECD [1997] , p.19.

V Tax Invoice of GST

Generally speaking, output − input of companies is called value-added.

Figure 1 shows three companies : manufacturer "A" , wholesaler "B" , and retailer "C" . Their output, input, and value-added amounts excluding GST are as follows :

"A"	output : 5,000	input : 0	value-added : 5,000
"B"	output : 7,000	input : 5,000	value-added : 2,000
"C"	output : 10,000	input : 7,000	value-added : 3,000

"A" sells a product at 5,000 to "B" , "B" sells it at 7,000 to "C" ,and "C" sells it at 10,000 to the final consumer.

The GST amount which each trader has to pay at the rate of 10% :

	Onput Tax	−	Input Tax	=	GST amount
A :	5,000×10%	−	0 ×10%	=	500
B :	7,000×10%	−	5,000×10%	=	200
C :	10,000×10%	−	7,000×10%	=	300

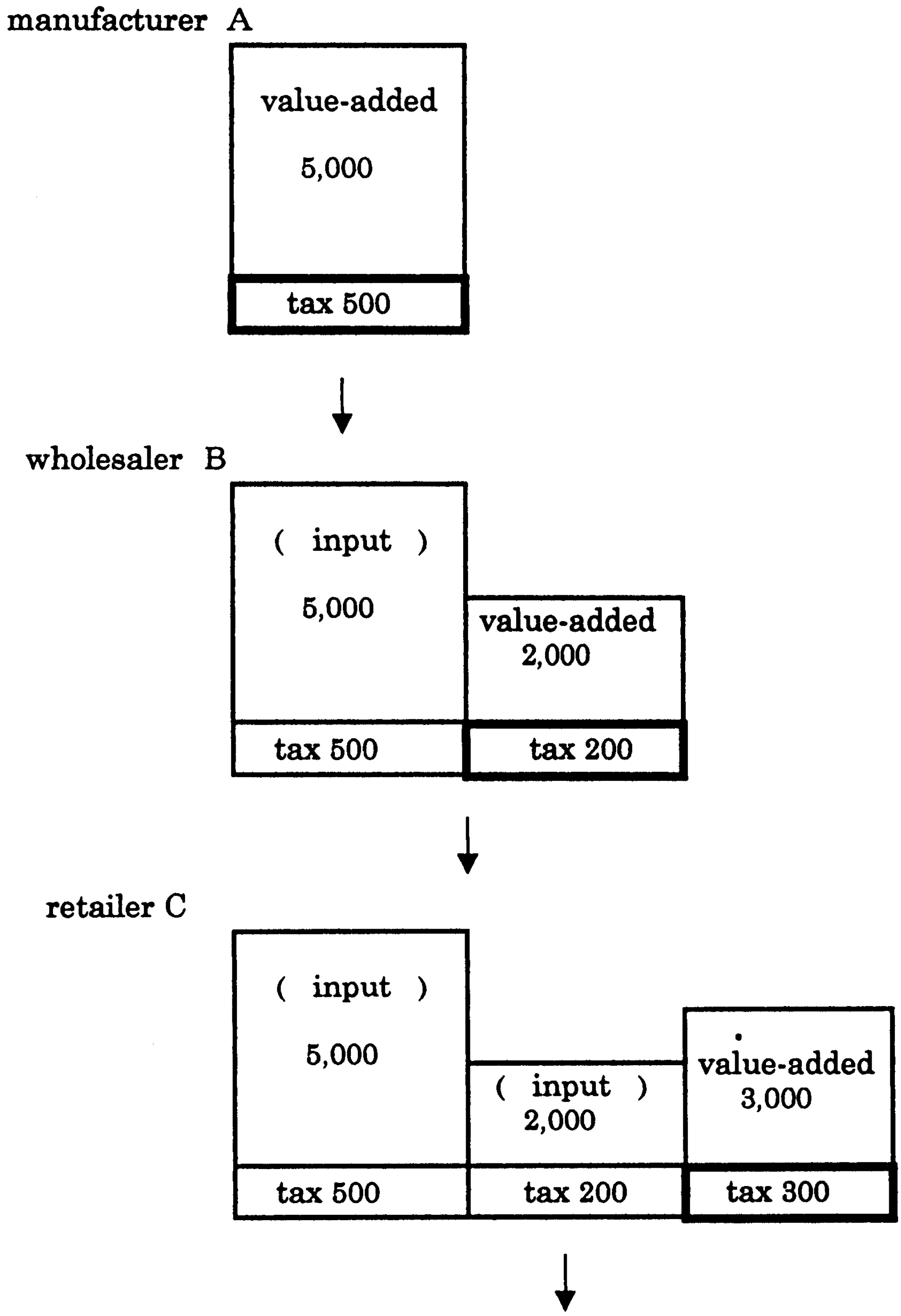
The output and input change of each trader is shown in Figure 1. In this case, "A" sells the product at 5,500 to "B" . It includes GST 500 which "A" has to pay to the tax authority. Because "A" marks up 500 on it's sale of 5,000, "B" actually bears GST 500 as a part of the input. "B" pays GST 200 and sells the product at 7,700 to "C" , and "C" pays GST 300 and sells it at 11,000 to the final consumer. Each trader pays 500, 200 and 300 respectively as GST to the tax authority. In other words, these GST amounts are imposed on the value-added amount of "A" , "B" and "C" . So, a tax of this type is also called Value-Added Tax or VAT.･New Zealand's GST and the Consumtion Tax of Japan are a kind of VAT.

However, the final consumer actually bears GST 1,000 (500+200+300) in this case instead of the traders. This is because the final consumer purchases the product at 11,000 which is higher by 1,000 than the pretaxed price of 10,000. The traders shift their burdens to the final consumer.

Under New Zealand's GST, when each trader deducts input tax from output tax , a tax invoice must be used. The tax invoice is issued by the previous trader. It is "A" to "B" and "B" to "C" . An example of tax invoices is shown in figure 2. The previous case of

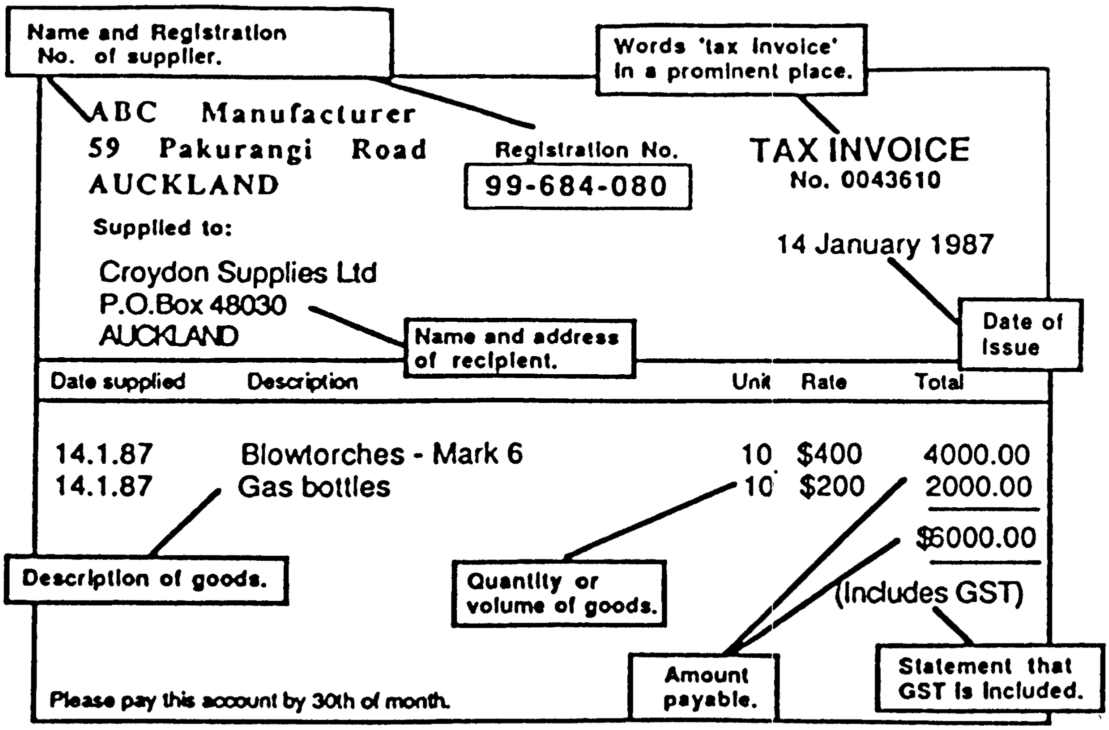
Figure 1 Mechanism of Value-Added Tax (GST or Japan's Consumtion Tax)

(10% tax rate)



final consumer at 11,000(including tax 1,000)

Figure 2 Example of Tax Invoice



Source : Mackenzie [1993], p.123.

"A" and "B" corresponds to "ABC Manufacturer" and "Croydon Supplies Ltd " respectively. The tax invoice system of GST is similar to that of EU's and other countries' VAT. However, in the case of Japan's Consumption Tax, traders can deduct input tax from output tax using privately kept bookkeeping system.

Some people think that the tax invoice system is more fair than the system of using books. I partly agree with them. Because under GST, exempted traders can't issue tax invoices, they can't collect GST amounts from consumers. But under the Consumption Tax of Japan, even exempted traders can collect tax from consumers. It is called "EKIZEI" or the special benefit from the tax system for the exempted traders. To solve this problem, we should reduce the threshold of the size of exempted traders of the Consumption Tax or introduce a tax invoice system. However, I have to say that the tax invoice system is not necessarily perfect, because even under this system, tax evasion can occur ; for instance, by illegal issue of tax invoices.

Indirect taxes, such as New Zealnd's GST and the Consumption Tax of Japan, are taxation on expenditures of people. This is because traders mark up the tax amounts on their output. The difference of expenditures between the rich and the poor is smaller than the difference of their incomes. So, the ratio of indirect tax amounts to their incomes increases as their incomes decrease. Indirect taxes are heavily imposed on lower income families instead of the rich, in other words, it's regressive. If New Zealand adopts additional lower tax rates on some items, for example, food, when the tax rate is increased, it means New Zealand partly gives up its tax philosophy or neutrality of tax to relieve low income classes.

VI Concluding Remarks

- New Zealand is a small country (in terms of land surface area and population) which depends on international trade. When New Zealand faced serious economic situations in the 1970's and 80's , it had to change. The direction was liberalization of markets and making public sectors efficient. It was not a unique policy, but in the case of New Zealand, it was radical and sweeping.
- With the introduction of the policy of market liberalization, taxes were expected to be as neutral as possible.
- The adoption of GST, instead of the wholesale Sales Tax which had a narrow tax base and many tax rates, formed a very important part of the tax reform.
- The GST's tax base is broader than that of Japan's Consumption Tax. The even lower threshold of the size of exempted traders and the more taxable items attract our attention.
- A tax invoice system, such as the GST's tax invoice, is considered to be more fair than the system of record books used by Japan's Consumption Tax. However, it depends on the tax evasion check system by the tax authorities.
- Many EU's countries adopt lower tax rates on some items, for example, food, children's clothing, books, and so on, to relieve low income families. If New Zealand gives up a single rate policy, it means partly giving up the guiding principle of the tax reform or neutrality of tax.

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