Consumption Tax Reform in Accelerating the Establishment of a New Development Paradigm

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Accelerating the establishment of a new development paradigm in which domestic and overseas markets reinforce each other, with the domestic market as the mainstay, has posed new requirements for deepening the consumption tax reform. Therefore, we need to focus on accelerating the establishment of a new development paradigm, combined with the establishment of a modern fiscal and tax system and tax attributes, and make effective institutional arrangements for comprehensively promoting consumption, expanding domestic demand and then forming a strong domestic market. It is meaningful to reduce tax on consumer goods involved in upgrading consumption to meet people's needs for a better life and to raise tax on high energy-consuming, highly polluting and unhealthy consumer goods to enhance the regulatory role of consumption tax and to promote the overall optimization and upgrading of the industrial structure. The revenue of consumption tax on key tax items (categories) should belong to the central government to facilitate the smooth flow of the economic circulation.

Keywords: new development paradigm, consumption tax, expand domestic demand, modern fiscal and tax system

The Fifth Plenary Session of the 19th Communist Party of China (CPC) Central Committee proposed that China should accelerate the establishment of a new development paradigm in which domestic and overseas markets reinforce each other, with the domestic market as the mainstay. Domestic demand is the main driving force of China's economic development. To accelerate the establishment of the new development paradigm, we must firmly adhere to the strategic basic point of expanding domestic demand to accelerate the cultivation of a complete domestic demand system and form a strong domestic market. Consumption is an important component of domestic demand and plays a fundamental role in China's economic development. Therefore, expanding domestic demand should start with comprehensively promoting consumption to stimulate consumption potential, improve consumption quality and expand consumption capacity. As the name implies, consumption tax, as an important tax in China's tax system, closely related to consumption, is one of the effective institutional arrangements to comprehensively promote consumption and expand domestic demand. Under such circumstances, it is necessary to deepen the consumption tax reform and provide

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strong support for accelerating the establishment of a new development paradigm by promoting consumption and expanding domestic demand.

1. Accelerating the Establishment of a New Development Paradigm Gives New Meaning to Deepening the Consumption Tax Reform

Xi Jinping, general secretary of the CPC Central Committee, has stressed that accelerating the establishment of a new development paradigm featuring dual circulation, in which domestic and overseas markets reinforce each other, with the domestic market as the mainstay is a major strategic task related to China's overall development, which needs to be accurately grasped and actively promoted with the overall situation taken into account. In this sense, to deepen the consumption tax reform, we must focus on accelerating the establishment of a new development paradigm and make corresponding adjustments to the tax system to smooth the economic circulation.

In 2020, the national tax revenue was 15431 billion yuan, a year-on-year decrease of 2.3%. Of this total, domestic value-added tax (VAT) revenue was 5679.1 billion yuan, a year-on-year decrease of 8.9%; domestic consumption tax revenue was 1202.8 billion yuan, a year-on-year decrease of 4.3%; corporate income tax revenue was 3642.4 billion yuan, a year-on-year decrease of 2.4%; individual income tax revenue was 1156.8 billion yuan, a year-on-year increase of 11.4%. In the context of effectively responding to the impact of the epidemic and large-scale tax and fee cuts, although the domestic consumption tax revenue ranks third, its decline ranks second. If we consider the decline of the consumption tax on imports, it basically reflects the close correlation between the consumption tax and the economic operation. This also means that the institutional arrangement of consumption tax is an important variable to accelerate the establishment of a new development paradigm and promote sustained and stable economic development.

The key to accelerating the establishment of a new development paradigm lies in the unobstructed economic circulation. Whether it is the domestic market as the mainstay, or the domestic and overseas markets reinforce each other, its essence is being unobstructed. It is necessary to get through the blocking points, fill the breakpoints and solve the difficulties. It is necessary to run through all links of production, distribution, circulation and consumption. Since consumption tax takes the turnover of consumer goods as the taxation object, whether the circulation of consumer goods can be unobstructed will directly affect whether the economy can be circulated and whether the economic circulation can be unobstructed. Although China's consumption tax belongs to a special consumption tax, the collection links involve production, wholesale and retail. Consumption tax affects not only supply, circulation, but also demand. Therefore, deepening the consumption tax reform requires positioning and planning from the strategic height of accelerating the establishment of a new development paradigm.

It was pointed out at the 2020 central economic work conference that the formation of a strong domestic market is an important support for building a new development paradigm. Especially since the reform, after years of economic development, China has the potential to form a strong domestic market. This is highlighted in three aspects. First, with its total economic output ranks second in the world, China is the largest developing country, and also the only country in the world that has all the industrial categories in the United Nations Industrial Classification, which has laid a solid foundation for the formation of a strong domestic market. Second, with the per capita GDP exceeding $10000 threshold, the middle-income group continues to expand, forming the largest middle-income group in the world. Its consumption potential is huge, providing a strong support for the formation of a strong domestic market. Third, China's economic development has maintained sustainability, with strong resilience, potential and room for maneuver. Although the epidemic has brought unprecedented impact, the economy has achieved contrarian growth, and the existing reasonable growth of economic development has been more qualitatively and effectively improved, which has injected sufficient momentum into the formation of a strong domestic market. To turn a strong domestic market from possibility to reality, we need to make efforts in many aspects. As a form of institutional arrangement, deepening the consumption tax reform naturally plays its due role.

Adhering to the strategic basic point of expanding domestic demand is the direct starting point for the formation of a strong domestic market, thus helping to accelerate the establishment of a new development paradigm. Generally speaking, domestic demand consists of consumption and investment. Therefore, expanding domestic demand and attaching importance to demand-side management comprehensively promotes consumption on the one hand, and expands investment space on the other hand. As the final link of economic activities, consumption plays a guiding role for investment and can lead the supply at the production end to provide products that meet consumer demand. Therefore, from the perspective of the relationship between consumption and investment, consumption being the pillar of economic development, investment should, to a certain extent, serve consumption; from the perspective of the relationship between demand and supply, the implementation of the strategy of expanding domestic demand should be organically combined with deepening supply-side structural reform to form a higher-level dynamic balance in which demand leads supply and supply creates demand. Hence, the important support for accelerating the establishment of a new development paradigm is to form a strong domestic market. The direct focus of forming a strong domestic market is to expand domestic demand, and the focus of expanding domestic demand is to comprehensively promote consumption. According to this logic, we should make effective institutional arrangements in reasonably guiding consumption and investment, and deepening the consumption tax reform is an important foothold.

2. Deepening the Consumption Tax Reform Should Start from Three Aspects

On the one hand, starting from accelerating the establishment of a new development paradigm, deepening the consumption tax reform must be reflected in expanding domestic demand to form a strong domestic market. On the other hand, deepening the consumption tax reform is a natural move to further improve the modern tax system, which needs to be comprehensively considered in the establishment of a modern fiscal and tax system. At the same time, as an indirect tax, consumption tax has different attributes and characteristics from other taxes. Therefore, deepening the consumption tax reform also needs to take this into account.

2.1. Promote and Accelerate the Establishment of a New Development Paradigm

To accelerate the establishment of a new development paradigm, the top priority is to expand domestic demand, and the comprehensive promotion of consumption is the focus of expanding domestic demand. Therefore, to deepen the consumption tax reform, we should make efforts in how to stimulate consumption potential and comprehensively promote consumption. In 2020, despite the tremendous impact of the epidemic, China's final consumption expenditure still accounts for 54.3% of GDP, a relatively high level in recent years. However, if we look at the total retail sales of consumer goods alone, the number was 39198.1 billion yuan in 2020, a decrease of 3.9% over 2019. From the perspective of international horizontal comparison, the average contribution rate of China's final consumption expenditure to economic growth from 2013 to 2019 is about 60%, still far below the level of 70% and 80% in developed economies. Consumption undoubtedly plays a fundamental role in China's economic development, but the epidemic has had a serious impact on the consumer market, resulting in a negative growth in consumption in 2020 compared with 2019. There is still large room for growth in the consumer market. It is necessary to explore more consumption growth points and boost household consumption.

To accelerate the establishment of a new development paradigm requires sustained efforts to expand domestic demand and consumption. Consumption tax is an indirect tax, and the tax burden can be transferred to consumers through the price mechanism, thus affecting the consumption cost and guiding consumption. Generally speaking, higher consumption tax means higher consumption cost, and consumption is limited; lower consumption tax means lower consumption cost, and consumption is encouraged. At present, with the epidemic still spreading all over the world, more unstable and uncertain factors in the international situation, and the foundation for China's economic recovery not yet solid, we should take the opportunity of accelerating the establishment of a new development paradigm, take solid steps to ensure stability on six key fronts and security in six key areas, and strive to keep the major economic indicators within the appropriate range. Since consumption is the "ballast stone" for the stable operation of the economy, it is necessary to start with various factors affecting consumption, reduce the constraints on consumption as much as possible, and then expand domestic demand.

Therefore, deepening the consumption tax reform must be closely combined with accelerating the establishment of a new development paradigm, and the reform should be oriented to help promote consumption and expand domestic demand. For a period of time, when talking about the consumption tax reform, some scholars cited the "expansion" of consumption tax as an option, suggesting that high-end consumer goods such as high fashion, private aircraft, high-end furniture, luxury tea, and high-end services such as luxury hotels, private clubs, top beauty and fitness centers should also be included in the collection scope. However, to give full play to the basic role of consumption in economic development, bringing too many high-end goods and services into the collection scope may not be conducive to expanding the scale of consumption, nor to upgrading consumption and creating new consumption, but will exacerbate the outflow of consumption. With the gradual improvement of people's living standards and the increasingly extensive pursuit of a better life, after meeting the basic consumption needs, people are increasingly pursuing quality, personalized and diversified consumption, and are increasingly transforming from physical consumption to both physical consumption and service consumption, indicating that there is a trend of improving both the quality and grade of consumption. Especially, under the impact of the epidemic, efforts should be made to keep the major economic indicators within an appropriate range, and promoting consumption and expanding domestic demand have become important macro policies. Therefore, in view of the current situation, at least in the near future, it is inappropriate to include too many goods and services into the scope of consumption tax collection.

2.2. Conducive to the Establishment of a Modern Fiscal and Tax System

To establish a modern fiscal and tax system, we should not only consolidate the achievements of system construction, but also further deepen and expand on this basis. Deepening the consumption tax reform also faces such a task. Since its establishment in 1994, the consumption tax has undergone several major adjustments, from 11 tax items at the beginning of its establishment to 15 tax items at present, while the adjustment of the increase and decrease of tax items in 2006, the reform of refined oil tax in 2008, and the adjustment of cosmetics consumption tax policy in 2016 to a large extent reflect the process and requirements of fiscal and tax system reform.

In November 2013, the *Decision of the Central Committee of the Communist Party of China Concerning Several Major Issues of Comprehensively Deepening Reform* adopted at the Third Plenary Session of the 18th Central Committee of the Communist Party of China put forward objectives, requirements, main tasks, and implementation paths for the fiscal and tax system reform during the period of comprehensively deepening reform, marking that the fiscal and tax system reform has entered a new period. In June 2014, the *Overall Plan for Deepening the Reform of the Fiscal and Tax System* was issued, which put forward reform ideas and defined reform tasks from the perspective of modernization of the national governance system and governance capacity. In terms of tax reform, the reform focuses on six major taxes, including the consumption tax reform, that is, adjusting the collection scope, links, and tax rates of consumption tax, and including high-energy consumption, high-pollution products and some high-end consumer goods into the collection scope. In addition, the 13th Five-Year Plan clearly puts forward "improving the consumption tax system" in the part of "accelerating the reform of the fiscal and tax system", the report of the 19th CPC National Congress puts forward "deepening the reform of the tax system", the Fifth Plenary Session of the 19th Central Committee puts forward "improving the modern tax system... Optimizing the tax structure", and so on, which are directly or indirectly related to the consumption tax reform. It is worth pointing out that in June 2019, the State Council issued the *Plan for Promoting the Reform of Adjusting the Division of Central and Local Revenue after the Implementation of Larger Scale of Tax and Fee Cuts*, which shifted back the link of consumption tax collection and steadily delegated it to local governments, combining the consumption tax reform with the expansion of local revenue sources, reflecting the synergy and systematization of the tax reform and the reform of the fiscal and tax system.

Deepening the consumption tax reform is a part of the reform of fiscal and tax system. How to reform it must reflect the orientation of fiscal and tax system reform, so as to promote the deepening of fiscal and tax system reform with its own reform. For a period of time after the general plan for deepening the reform of fiscal and tax system was issued in 2014, one of the basic ideas of fiscal and tax system reform is to stabilize the tax burden, that is, the commonly referred to tax system reform is a structural reform in which some taxes are increased and some taxes are reduced. As far as the consumption tax reform is concerned, expanding the collection scope to high energy-consuming, highly polluting, and unhealthy consumer goods has become an important option. Up to now, the background of fiscal and tax system reform has changed significantly. Affected by structural, cyclical and institutional factors, especially the huge impact of the epidemic, China's economy is facing great downward pressure. Large-scale tax and fee cuts have become an important policy orientation of the fiscal and tax system reform. For example, the VAT, the largest tax in China, has been reduced from 17% to 16% in manufacturing and other industries, and from 11% to 10% in transportation, construction, basic telecommunications services and agricultural products since May 1, 2018; for general VAT taxpayers, if the original 16% VAT tax rate was applicable, the rate has been adjusted to 13%, and if the original 10% tax rate was applicable, the rate has been adjusted to 9% since April 1, 2019. It can be seen that in order to keep the economic operation within an appropriate range, tax and fee reduction is one of the policy orientations of the fiscal and tax system reform at present and in the future. Therefore, given the close relationship between this tax and consumption, deepening the consumption tax reform also needs to reflect the policy orientation of fiscal and tax system reform, so as to promote the establishment of a modern fiscal and tax system.

2.3. Highlight the Regulatory Function of Consumption Tax

Theoretically, VAT and consumption tax belong to the same category of consumption tax in a broad sense. The VAT is levied universally, reflecting neutrality; consumption tax is collected selectively, including the choice of taxation objects and the choice of different tax burdens for different objects, reflecting "non-neutrality". In general, consumption tax is mainly levied on three types of consumer goods in China. First, consumer goods that are harmful to health, such as cigarettes and alcohol; second, consumer goods that cause high energy consumption and pollution, such as refined oil, cars, firecrackers, wooden disposable chopsticks, batteries and coatings; third, high-end consumer goods at different stages,[1] such as luxury cosmetics, valuable jewelry and precious stones, luxury watches, yachts, etc. This institutional arrangement of consumption tax reflects the regulatory function of consumption tax — "trying to prohibit a business by taxing it heavily", which reflects the country's macro policy, and its function for financial revenue is in a subordinate position.

OECD member countries generally levy excise duty, which are very similar to China's consumption tax. According to statistics, the share of excise duty in the total tax revenue of OECD member countries decreased from 10.5% in 1975 to 7.2% in 2018 on average.[2] Among them, in 26 member states, the share of excise duty in total tax revenue is between 5% and 10%; there are 8 countries with a share of less than 5%, namely Australia, Canada, Israel, Japan, New Zealand, Sweden, Switzerland and the United States; there are 5 countries, namely Estonia, Latvia, Lithuania, Poland and Turkey, with a share of more than 10%, compared with 12 in 2010.[3] The excise duty of OECD member countries are mainly levied on alcoholic beverages, tobacco products, heating fuels (such as unleaded gasoline, diesel oil and heavy fuel oil). The purpose is not only to obtain tax revenue, but also to affect specific consumption behaviors and reduce the consumption of products harmful to health or the environment. It can be

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[1] The concept of high-end consumer goods is a relative concept. With the improvement of income and living standards, high-end consumer goods in a certain period are likely to become ordinary consumer goods. For example, after 2006, the consumption tax on "skin care and hair care products" was abolished.

[2] OECD. (2020). *Consumption Tax Trends 2020: VAT/GST and Excise Rates, Trends and Policy Issues*. Paris: OECD Publishing, 140.

[3] OECD. (2020). *Consumption Tax Trends 2020: VAT/GST and Excise Rates, Trends and Policy Issues.* Paris: OECD Publishing, 140.

seen that OECD member countries pay more attention to the regulatory function of excise duty. Other countries have similar policy orientations.

In terms of the proportion of domestic VAT, domestic consumption tax, individual income tax and corporate income tax in the total tax revenue, from 2001 to 2020, the proportion of domestic consumption tax in China remained between 7.5% and 8%, as shown in Figure 1. Although consumption tax has certain importance for revenue, the importance is not significant. In terms of key tax source enterprises in China by industry, cigarettes, alcohol, cars, and refined oil constitute the main source of income of consumption tax. Taking the year of 2018 as an example, the consumption tax revenue from these four types of products was 621.552 billion yuan, 4.159 billion yuan, 103.337 billion yuan and 594.185 billion yuan respectively, an increase of 6.4%, 9.6%, −2.1% and 3.2% over 2017. However, the consumption tax revanue contributed by valuable jewelry and precious stones, luxury cosmetics, golf balls and equipment, battery manufacturing, paint manufacturing, etc. are less. This situation is similar to the situation that the excise duty of OECD member countries is highly concentrated on certain types of consumer goods, which also shows that China's consumption tax has mainly a regulatory function. In combination with international practice and the current situation in China, deepening the consumption tax reform and adjusting the tax items and tax rates should still focus on playing its regulatory function, and give consideration to its function of fiscal revenue at the same time.

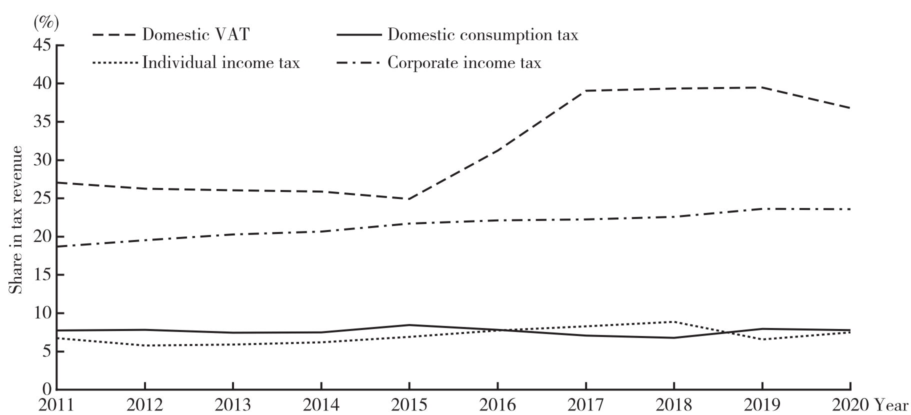

Figure 1. Shares of Four Major Taxes in Total Tax Revenue from 2011 to 2020

Source: Data from 2011 to 2019 are from the website of the National Bureau of Statistics (http://gks.mof.gov.cn/tongjishuju/202101/t20210128_ 3650522.htm), the data of 2020 is from the website of the Ministry of Finance (http://gks.mof.gov.cn/tongjishuju/202101/t20210128_3650522.htm). Compiled and calculated by the author.

3. Policy Suggestions on Deepening the Consumption Tax Reform

Accelerating the establishment of a new development paradigm has posed new requirements for deepening the consumption tax reform. Expanding domestic demand, comprehensively promoting consumption and forming a strong domestic market are the main objectives of deepening the consumption tax reform. At the same time, in combination with the "non-neutrality" attribute of consumption tax, we should make structural adjustments to the collection scope and tax rate, further strengthen its regulatory function on high energy-consuming, highly polluting and unhealthy consumer goods, weaken its regulatory function on high consumption, and do not pursue the goal of one-sidedly enhancing its fiscal revenue function.

3.1. Provide Effective Institutional Arrangements for Comprehensively Promoting Consumption

Accelerating the establishment of a new development paradigm and adhering to the strategic basic point of expanding domestic demand requires the combination of expanding consumption with improving people's quality of life. Therefore, to deepen the consumption tax reform, we need to make corresponding adjustments in tax rates or tax items to help promote consumption in an all-round way. At present, among the 15 categories of products included in the scope of consumption tax collection, luxury cosmetics, valuable jewelry and precious stones, and luxury watches do not involve high energy consumption or high pollution, nor are they unhealthy consumer goods. With the gradual improvement of people's living standards, these consumer goods are closely related to the improvement of people's quality of life. They are the natural choice for people to pursue quality, personalized and diversified consumption, and upgrade consumption after meeting basic consumption. High-end consumer goods will become ordinary consumer goods with the change of economic development level. Moreover, the high tax burden on high-end consumer goods will also crowd out domestic consumption, leading consumers to buy abroad, resulting in an outflow of consumption. Therefore, we should proceed from the reality of the gradual improvement of people's living standards, take the overall promotion of consumption as the goal, and gradually reduce the tax rate of the current so-called high-end consumer goods, or move them out of the scope of collection when the time is ripe.[1] At the same time, nor should too many high-end consumer services be included in the scope of consumption tax collection. Only by constantly making dynamic adjustments and realizing the institutional arrangement of low tax or tax exemption can we comprehensively promote consumption and meet the people's pursuit of a better life.

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[1] In April 2019, the Tariff Commission of the State Council reduced the import tax rate of wine, valuable jewelry and precious stones, golf balls and equipment, luxury watches, luxury cosmetics, etc. by 50%, which provided useful enlightenment for deepening the consumption tax reform.

3.2. Further Strengthen the Regulatory Function of High Energy-Consuming, Highly Polluting and Unhealthy Consumer Goods

In the new development stage, we should implement the new development philosophy, establish a new development paradigm, promote high-quality economic development, comprehensively optimize and upgrade the industrial structure, and form a more efficient and high-quality input-output relationship. All these require constantly highlighting the regulatory function in deepening the consumption tax reform, and raising tax rates in promoting resource conservation and ecological environment protection and curbing unhealthy consumption. For example, consumer goods such as tobacco and alcohol, although closely related to daily consumption, are harmful to health; for another example, refined oil, solid wood flooring, wooden disposable chopsticks, batteries, coatings, etc. are closely related to the protection and improvement of the ecological environment and the reduction of resource consumption. For such consumer goods, the tax rate can be appropriately raised if conditions permit. In addition, non-degradable disposable products (such as plastic packaging, plastic bags, plastic containers, etc.) and other high energy-consuming and highly polluting consumer goods should be included in the collection scope according to the specific circumstances and the process of consumption tax reform. In addition, this part of tax should be earmarked for special purposes and concentrated on promoting green development and improving people's health. It should be noted that whether it is to increase tax on the above-mentioned consumer goods under the existing tax items, or to include more high energy-consuming, highly polluting, and unhealthy consumer goods in the scope of collection, increasing tax revenue is secondary. What is more important is to further enhance the regulation of high-energy, highly polluting and unhealthy consumer goods, drive the optimization and upgrading of industrial structure directly from the supply side or indirectly from the demand side, and improve the "greening" degree of economic and social development.

3.3. The Consumption Tax Revenue of Key Tax Items (Categories) Should Belong to the Central Government to Facilitate the Smooth Economic Circulation

At present, the consumption tax is the central tax, and all revenues are owned by the central government. After the replacement of business tax with VAT, local governments lost their main tax sources due to the withdrawal of business tax from the historical stage. Therefore, some scholars suggested that the consumption tax should be transformed into a local tax to enrich local financial resources.[1] In 2019,

[1] Zhang, X. D.(2018). Discussion on Consumption Tax as the Main Tax of Provincial Government. *Fiscal Science*, 4, 43–46, 51.

the *Plan for Promoting the Reform of Adjusting the Division of Central and Local Revenues after the Implementation of Larger Scale Tax and Fee Cuts* issued by the State Council proposed that, in accordance with the reform requirements of improving the local tax system, under the premise of controllable collection and management, part of the current consumption tax items collected in the production (import) link will be gradually transferred to the wholesale or retail link for collection. This can be seen as an exploration to enrich local financial resources with the help of consumption tax. However, the current tax classification principle in China is to classify the tax with strong regulation, strong liquidity, uneven tax base distribution and large tax base liquidity as central tax, or the central government takes a higher share; the tax with sufficient local information, great impact on local resource allocation and relatively stable tax base are classified as local tax, or the local government takes a higher share. Therefore, from the perspective of the attributes and functions of consumption tax, it is not appropriate to transform it into a local tax by moving the taxation link backward. Otherwise, it will not only obstruct the smooth economic circulation, but also may induce vicious competition among regions, aggravate the imbalance of regional development and distort the regional industrial structure. Therefore, when exploring the link of shifting the consumption tax collection and enriching the local tax sources, it is suggested that the consumption tax revenue of high energy-consuming, highly polluting and unhealthy consumer goods, such as cigarettes, wine, batteries and coatings, should still be attributed to the central government, and the consumption tax of valuable jewelry and precious stones, luxury watches, etc., should be shifted back to the collection link and transferred to the local government, so as to form a new pattern of consumption tax distribution with central tax as the main and local tax as the auxiliary. As for the shortage of local financial resources, we need to increase the transfer payment from the central government to local governments, and further increase the local share of VAT and income tax.

3.4. Effectively Improve the Level of Tax Collection and Management

The success of tax system reform depends on tax collection and management to some extent. Without high-level tax collection and management, it is difficult to achieve the desired purpose of tax reform. To deepen the consumption tax reform, especially to explore the gradual transfer of current consumption tax items to the wholesale or retail sector, we need to effectively improve the level of tax collection and management as a strong support. In this regard, it is suggested to take the legislation of the *Consumption Tax Law of the People's Republic of China* as an opportunity to adhere to the concept of administering taxes according to law, further promote the reform of "delegating power, improving regulation, and upgrading services", accelerate the construction of a new generation of intelligent electronic tax bureaus with the help of high-tech means such as big data, cloud computing and blockchain, continue to promote the construction of tax-related information sharing platforms, and gradually build an integrated and systematic comprehensive tax-related information management system, promote the consumption tax reform with highly intelligent tax collection and management.

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