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Reflections on the Mirrlees Review: An Australasian Perspective*

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Abstract

This paper compares and contrasts the UK's Mirrlees Review with major tax reviews that have taken place at about the same time in Australia (the Henry Review) and New Zealand (the Tax Working Group Review). It suggests that the three countries share many cultural, social, economic and political traditions and institutions, but that this shared heritage does not necessarily extend to the realms of tax reviews and the possible roads to tax reform that the countries may tread. There are some similarities in aspects of the processes of tax review that have taken place in the three countries (though rather more differences), and all three countries also share a commitment to broadly similar principles underlying the recommendations made by each of the three reviews. But the specific proposals made by each of the reviews do not share much common ground. The differences are more apparent than any similarities that may occur, an outcome (in part at least) predicated upon the very different political, economic and fiscal imperatives prevailing in each of the three countries.

The paper also suggests that it is unlikely that the three reviews will have the same long-term impact or effects upon their respective national tax systems. It may be the case, the paper contends, that there is a form of trade-off between political independence (as in the Mirrlees Review) and the direct policy impact that is more apparent in countries whose reviews had strong

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government backing (as was the case in New Zealand) – at least in the short term. Moreover, independent reviews (such as the Mirrlees Review) may also lead to more radical proposals, which will require a longer time maturing 'on the shelf' before they may be ripe for implementation.

I. Introduction

The United Kingdom is not alone in having been the subject of a recent major tax review and report on possible reform opportunities (the Mirrlees Review[1]). Tax reviews and ensuing reports have also been taking place, almost simultaneously, in other parts of the globe, including Australia (the Henry Review[2]) and New Zealand (the TWG Review[3]). While the three countries share many cultural, social, economic and political traditions and institutions, careful analysis suggests that this shared heritage does not necessarily extend to the realms of tax reviews and the possible roads to tax reform that the countries may tread. This paper considers the recent tax reviews that have occurred in the three countries, and compares and contrasts aspects of both the processes and the recommendations for reform. It identifies certain similarities in approach and outcome but also reveals significant differences.

The publication of major reviews into the tax systems of three broadly comparable OECD tax jurisdictions, effectively in a period of less than one year,[4] affords a rare opportunity for comparative analysis. But that analytical task is undertaken with caution and with humility. Comparative analysis can easily make the mistake of seeking to claim too much. To paraphrase Sandford (2000, p. 193), generalising about tax reform from a sample of three, from one period of tax reform, is a hazardous and unreliable business. Hence this paper is selective in its approach. It does not seek to cover all issues and all aspects. Rather, it restricts itself to the particular, hoping in that selectivity to be able to draw out conclusions of a more universal application.

The paper therefore proceeds as follows. The remainder of this introductory section provides necessary background to each of the three

[1]Mirrlees et al., 2010a and 2010b. Hereafter referred to as the 'Mirrlees Review' – so named after the chair of the review panel, Sir James Mirrlees.

[2]Henry, 2009. Hereafter referred to as the 'Henry Review' – so named after the chair of the review panel, Secretary to the Treasury Dr Ken Henry.

[3]Tax Working Group, 2010. Hereafter referred to as the 'TWG Review'. Note that subsequently a further review with implications for New Zealand's taxation system has been released – Savings Working Group (2011).

[4]The actual period is 11 months. The Henry Review was completed and passed to the Australian government in December 2009, but was not made public until it was released, along with the government's initial response, in May 2010. The TWG Review was released in January 2010 and the Mirrlees Review was launched (in draft form) in November 2010. The three reviews therefore became public between January and November 2010.

reviews – Mirrlees in the UK, Henry in Australia and TWG in New Zealand – in order to provide appropriate context. Section II then discusses issues relating to the process of tax review in the three countries. It considers, on a comparative basis, the provenance and duration of the reviews, how they were constituted and their relationship to their respective governments, what issues came under their purview and how the members of the review panels went about the task. Section III compares the principles that emerged from the reviews and which underpinned the eventual proposals, while Section IV explores the content and key recommendations. Finally, in Section V, observations on the political process whereby some of the recommendations of the various reviews may be translated into practical reality are made, along with concluding comments.

The Mirrlees Review was formally established by the Institute for Fiscal Studies (IFS) in mid-2006 to identify what makes a good tax system for an open economy in the 21st century, and to suggest how the UK tax system could be reformed to move in that direction. It followed in the footsteps of the renowned Meade Report,[5] which had also been undertaken under the aegis of IFS some 30 years earlier. The ambition of the Mirrlees Review was, however, somewhat broader than that of Meade: whereas Meade had focused on the structure and reform of direct taxation in the UK, the Mirrlees Review covered the whole tax system (direct and indirect) and also some aspects of its interaction with the social security and tax credit systems.

The deliberations of the Mirrlees Review took place over a four-year period and involved a number of submissions, consultative conferences and related proceedings. Its first volume[6] was published in 2010 and brought together 13 specially commissioned studies of different dimensions of tax design, plus associated commentaries. A second volume, containing the conclusions of the review's editorial team,[7] is scheduled for publication in September 2011, although a draft of this volume was made available in November 2010. Comments in this paper are based on that draft.[8]

The Henry Review in Australia was set up by means of an announcement in the May 2008 Budget by the Federal Treasurer, Wayne Swan, of a comprehensive 'root and branch' review of Australia's tax system, including its interaction with the transfer payment system and other social support payments, rules and concessions. Almost immediately, the government constrained the comprehensive nature of the review by declaring that the goods and services tax ('GST' – Australia's equivalent of the VAT)

[5]Meade, 1978.

[6]Mirrlees et al., 2010a.

[7]Sir James Mirrlees, Stuart Adam, Timothy Besley, Richard Blundell, Stephen Bond, Robert Chote, Malcolm Gammie, Paul Johnson, Gareth Myles and James Poterba.

[8]They continue to apply to the final version published in September 2011 by Oxford University Press for the Institute for Fiscal Studies. Chapter 20 of that volume, the conclusions and recommendations for reform, is also published in this issue, on pages 331–59.

would not be considered, and that the tax-free status of income received by taxpayers from superannuation schemes would also be off limits. Subsequently, the review itself chose not to consider various aspects of the tax system, such as industry policy, carbon pollution policy and legislative drafting. Otherwise, the aim of the review was to 'create a tax structure that will position Australia to deal with its social, economic and environmental challenges and enhance economic, social and environmental wellbeing' (Henry, 2009, p. v).

The Henry Review team was asked to submit a final report to the Treasurer by the end of 2009, which target it met with a few days to spare. (The government then sat upon the report until May 2010, at which point it publicly released the report together with its own response.) During the course of its deliberations, the review attracted widespread public and media interest. There were over 1,500 written submissions, many stakeholder meetings, public meetings and focus groups conducted by review panel members around the country, a major consultative conference involving Australian and overseas tax academics who provided a series of commissioned papers, and a number of speeches delivered by members of the review panel. The final recommendations (Henry, 2009, pp. 79–106) were underpinned by a series of background documents that were published in the 18 months of the review.[9]

The TWG Review was established by Victoria University of Wellington (VUW) in May 2009, in conjunction with the New Zealand Treasury and Inland Revenue, and produced its report with 13 major recommendations in January 2010. The TWG was chaired by Professor Bob Buckle of the Centre for Accounting, Governance and Taxation Research at VUW and comprised a mixture of academics, tax practitioners, business people and tax officials. The aims of the TWG Review were to: identify concerns with the current taxation system; describe what a good tax system should be like; consider options for reform; and evaluate the pros and cons of these options (Tax Working Group, 2010, p. 9).

The TWG held six meetings between June and December 2009, together with a one-day consultative conference in December 2009. In the course of the deliberations, 19 background papers were also produced.[10]

This background information about the three reviews now permits analysis of key aspects of the processes involved.

[9]*Architecture of Australia's Tax and Transfer System* (6 August 2008); *Australia's Future Tax System – Consultation Paper* (10 December 2008); *Australia's Future Tax System – Retirement Income Consultation Paper* (10 December 2008); *Australia's Future Tax System – The Retirement Income System: Report on Strategic Issues* (12 May 2009).

[10]These are listed on pages 68 and 69 of the TWG report, and are also available at http://www.victoria.ac.nz/sacl/cagtr/twg/.

II. Process issues: why and how did the reviews take place?

Even the most cursory of examinations suggests that there are some similarities but rather more significant differences in the manner in which each of the three tax reviews was conducted, which may therefore have had implications both for what the reviews were likely to conclude and recommend and the potential impact of each of the reviews. The following comparison of the processes involved in the reviews in the three countries, which confirms that initial observation, considers the rationale for the establishment of the reviews and their consequent standing or status, and their terms of reference, scope and time horizons. In so doing, it also comments upon other process issues, including the duration, length and public and professional consultation and engagement involved in the reviews.

1. Rationale and standing of the reviews

All three countries have long traditions of reviews into the whole (or significant aspects) of their tax systems, with reviews taking place at relatively frequent intervals.[11] Indeed, in the context of the Australian taxation system, the Asprey Committee (1975, para. 1.2) noted that 'even if, as is not the case, the Australian system were generally agreed to be as satisfactory as any tax system ever admitted to be, a periodic thorough inspection would be as wise a precaution in this area of affairs as in any other'. Moreover, it often appears to be the case that invoking a review of the tax system can seem an attractive option in times of fiscal or economic uncertainty – though one that is sometimes subsequently regretted by governments. But reviews of the nature considered in this paper are, of course, not all originated from government sources.

Certainly, part of the underlying rationale for the most recent reviews in the UK, Australia and New Zealand does seem to have been widespread concern about the state and nature of the tax system in each of the three countries. In the UK, the Mirrlees Review expounds at some length on the major flaws of the current system.[12] In Australia, the Henry Review refers to 'an unsustainable tax structure' and notes that 'Australia has too many taxes and too many complicated ways of delivering multiple policy objectives through the tax system' (Henry, 2010, p. 11). The TWG Review in New Zealand, in even stronger language, notes that 'the current system is incoherent, unfair, lacks integrity, unduly discourages work participation and biases investment decisions' (Tax Working Group, 2010, p. 9).

[11]See, for example, Evans and Krever (2009) for a detailed exploration of the many tax reviews conducted in Australia since Federation at the beginning of the last century.

[12]See, for example, Mirrlees et al. (this issue, pp. 340–1).

But it is probably reasonable to argue that there will always be disaffection or dissatisfaction with national tax systems, and it is therefore useful to look beyond the statements of concern contained in the reviews and consider other motivations and catalysts that may have brought about the formation of the review panels.

Evans and Krever (2009, p. 340) have argued that the most recent tax review in Australia had an almost accidental, and certainly unexpected, birth. Tax reform was definitely not on the agenda when the newly elected Labor government announced plans in early 2008 for a grand summit on Australia's future with broad community participation. The political leaders were caught slightly off guard when representatives from the business community at the summit almost unanimously nominated tax reform as a priority area.

The provenance of the New Zealand TWG Review may also be accounted for by the interplay of somewhat ad hoc and accidental forces. In that case, the speakers at an international conference on tax policy held in February 2009 at the Victoria University of Wellington 'identified significant concerns with the efficiency, equity and integrity of the current taxation system, concerns that required urgent attention' (Tax Working Group, 2010, p. 5). The support (and presence at the conference) of the New Zealand Inland Revenue and Treasury led to the formation of the review panel a few months later.

By way of contrast to the Australasian experience, the establishment of the Mirrlees Review took place over a much longer period and on a much more considered basis. It owes its existence to the recognition by the Institute for Fiscal Studies that some considerable time had passed since the commissioning of the highly influential Meade Report by that same organisation, and that the time was appropriate for a further review. The project was therefore inspired by the approaching 30th anniversary of the 1978 Meade Report. The longer period of gestation enjoyed by the Mirrlees Review compared with its Australasian counterparts (for example, there were meetings of the Mirrlees core team as early as September 2005) permitted funds to be sought from external bodies.[13] It also paved the way for a far more considered, reflective and comprehensive approach to the review than was the case in the Australasian countries, where decisions were sometimes made 'on the run' and resources marshalled as best as could be managed in the short time frames that had been imposed.

The Mirrlees Review also stands apart from its Australasian counterparts by dint of its formal independence from the governments of the day. It is a creature of an independent economic research centre and is not accountable

[13]The Economic and Social Research Council and the Nuffield Foundation each provided funding to the project.

to the politicians or any government agencies.[14] In contrast, the Australian Henry Review was wholly government organised (if not inspired). After tax reform was raised as a matter of critical importance at the national summit of 2008, 'the government decided to keep the review in-house, appointing the Secretary of the Treasury as chair of a panel that included four external advisers (one of whom formerly worked at the Treasury) to guide a Treasury-based review' (Evans and Krever, 2009, p. 340).[15]

The New Zealand model was not so obviously government led, but 'was formed with the support of the Minister of Finance, Hon Bill English, and the Minister of Revenue, Hon Peter Dunne' (Tax Working Group, 2010, p. 5). To that extent, and despite being coordinated by an academic institution, it cannot claim the same independence as may be claimed for the Mirrlees Review.

Independence from government can, of course, be a double-edged sword. On the one hand, it leaves the review panel free to 'think the unthinkable' and to make proposals that may take the debate outside institutional comfort zones or beyond conventional and mainstream approaches. But this freedom has to be balanced with the potential for impact on immediate policymaking that may not be as evident with an independent review as one sponsored or controlled by the government. The New Zealand government, which supported the TWG Review, has already indicated its support for many of the review proposals and has given effect, partially or wholly, to nine of the 13 recommendations.[16] In Australia, where the Henry Review was government sponsored and controlled, the Rudd and Gillard governments have accepted some of the recommendations and have already moved to implement some of those (albeit the resource rent tax proposals suffered severe emasculation in being translated from proposal to practice – see Section V).

Admittedly, the proposals from the (independent) Mirrlees Review are (at the time of writing) still in draft form. But thus far there has been a relative silence in terms of response from the government. That is, of course, entirely to be expected. The review was never written with immediate impact in mind. Like the Meade Report – and also similar to the Asprey Committee in Australia, where it was noted that 'structural reforms will inevitably take some years to implement' (Asprey, 1975, para. 1.12) – the Mirrlees Review

[14]Vann (2011, p. 5) notes that 'in the UK with typical eccentricity major tax review seems now to be left to the private sector supported by government money'.

[15]Smith (2010, p. 267) suggests that 'most [tax] reform [in Australia] has been pursued in either of two different pathways. Sometimes it has followed the traditional mode of deliberative analysis and persuasion, with proposals developed by reference to "public interest" considerations, by expert bodies, using open consultative processes. Other times, the executive has used its bureaucratic advisers to develop behind-doors, in-house reform packages, akin to the semi-secretive budget formulation process'. Smith considers that the Henry Review is 'an unusual amalgam' of these two approaches (p. 277).

[16]Vial, 2011, p. 1.

is there for the long term, to influence policy and practice over the next decades rather than the next years.

Notwithstanding this longer-term perspective, there is already one indication that the findings of the Mirrlees Review may, as would be expected, be influencing government policy in the UK. During the Budget speech on 23 March 2011, some four months after the recommendations had been issued in draft form, Chancellor George Osborne announced a review/ consultation on the merging of income tax and National Insurance contributions (NICs) – one of the Mirrlees recommendations. Note, however, that this may have simply been a response to a headline recommendation from the Office of Tax Simplification (OTS) rather than a direct response to the Mirrlees Review.[17]

2. Terms of reference, scope and time horizons of the reviews

All three reviews share relatively broad terms of reference, as indicated in Section I above. Commensurate with those terms of reference, all three felt entitled to adopt a system-wide approach to their task, although the Mirrlees and Henry Reviews were able to interpret that more broadly than their New Zealand counterpart. In New Zealand, the focus was more firmly upon the tax system per se, and although the transfer (welfare) system figured in the TWG's deliberations, it was very much as a secondary concern. This is reflected in its 12th recommendation, that 'there should be a comprehensive review of welfare policy and how it interacts with the tax system' (Tax Working Group, 2010, p. 11).

In contrast, the Mirrlees and Henry Reviews considered the interaction of the tax and transfer systems from the start and as a key aspect of their deliberations. Indeed, the Henry Review (p. v) noted that

> [the] relationships [of the tax system with the transfer payment system and other social support payments, rules and concessions] are of such importance that a systemic approach, encompassing the legal, economic and administrative structure of both transfers and taxes at all levels of government, has been adopted in this Review.

This focus is reflected in its recommendations, which range broadly across both tax and transfer payment issues.

The Mirrlees Review terms of reference may have been slightly more constrained than Henry in this connection, but the difference may be more imagined than real. The review noted that 'dauntingly, our canvas ... [covers] *some* areas of interaction with the social security and tax credit systems' (Mirrlees et al., 2010b, draft ch. 1, p. 1, emphasis added). This more limited

[17]On 10 March 2011, David Gauke, the Exchequer Secretary to the Treasury, had issued a Ministerial Written Statement which stated that the government would respond to the OTS interim report on small business taxation (Office of Tax Simplification, 2011) in the Budget speech.

approach may be reflected in the main recommendations, only one of which (the introduction of a single integrated benefit) relates to the interaction of the tax and transfer systems. Nonetheless, the comprehensive treatment of the tax and transfer issues and interactions in the two volumes of the Mirrlees Review indicates that it is far closer in terms of its scope to the Henry Review than to the TWG Review in this regard.

Mirrlees and Henry also share a closer connection so far as the time horizons adopted in their reviews are concerned, compared with New Zealand's review. Both Mirrlees and Henry are able to take a longer-term perspective. The package of recommendations put forward by the Mirrlees Review is 'a prospectus not for the next Budget or the one after that, but for a long-term programme of reform' (Mirrlees et al., this issue, p. 352). The Henry Review (p. v) is even more explicit:

> The perspective in this Report is necessarily long term. Economic, social and environmental change over the next 40 years is expected to have a profound impact on the tax and transfer system, but will evolve gradually. The significant reforms required to respond to these changes will take time to implement and will require further adaptation over time. This Report sets out the main reforms policy-makers should implement as they position the system for the future.

The TWG Review in New Zealand suggests that the 'Group's task was to identify the major issues that Ministers will need to consider in reviewing medium-term tax policy ...' (Tax Working Group, 2010, p. 5) and that 'tax policy changes should be made with reference to a long-term strategy and framework' (p. 9). However, the focus of the body of the report tends to be on more immediate tax reform than these statements might suggest. In particular, there is a concern that New Zealand has a 'tax system [that] was designed in the 1980s for a different set of domestic and international circumstances', and one in which 'piecemeal changes ..., while introduced with good intentions, have undermined the coherence and integrity of the tax system and created a system that is unfair and inequitable' (p. 59). The immediacy of the problem is reflected in recommendations for reform that primarily relate to the relative short term. The fact that the New Zealand government has already implemented (or partially implemented) nine of the 13 recommendations[18] also strongly suggests the more short-term perspective of the New Zealand review.

There are further contrasting features evident in the duration of the reviews. It has already been noted that the Mirrlees Review took place over (at least) a five-year period – beginning even before 2006 and not being completed until 2011. The Henry Review and the TWG were, in contrast,

[18]Vial, 2011, p. 1.

much shorter in duration – respectively one-and-a-half years and nine months from start to finish.[19]

The three reviews also shared a commitment to public engagement and consultation. All were characterised, perhaps more than has been the case in tax reviews before, by an openness and transparency in their proceedings, evidenced inter alia by consultative conferences, commissioned projects, public meetings, focus groups and submissions. There is often a difference between the rhetoric and the reality in terms of the consultative process, but there does seem to have been a genuine attempt in all three countries – despite the short time frames involved in two of them – to engage key stakeholders in the deliberations.

In summary, therefore, the processes of review in each of the three countries share some similarities, including the nature of the problems they sought to address, their broad terms of reference and the open and consultative manner in which they engaged with key stakeholders in discussing reform possibilities. But they were characterised more by the differences that emerged. The independent status of the Mirrlees Review stands in sharp contrast to the government-backed (though not necessarily controlled) inquiries in Australasia. Likewise, its provenance was more considered, less ad hoc, than those that occurred in Australia and New Zealand; and its perspective is certainly far longer than the New Zealand review and probably longer term than the Australian review. These substantive differences in approach have in turn produced some outcomes that distinguish the Mirrlees Review from both the Henry Review and the TWG Review. And – as will be suggested in Section V – the very different procedural approaches are underpinned by a very different economic perspective apparent in Mirrlees when compared with the Australian and New Zealand reviews.

III. The principles underlying the reviews

This section explores the underlying principles that each of the three reviews expressed as being fundamental to their final recommendations.

[19]Notwithstanding the very different time periods spent on reviewing the respective tax systems in each of the three countries, there is a remarkable similarity in the sheer length of the output (measured in numbers of pages) that each review managed. The total number of pages of the two volumes of Mirrlees will easily exceed 1,800 pages (a far cry from the 500-plus pages of the Meade Report). The Henry Review can boast nearly 1,000 pages in the three volumes of its final report published in December 2009, over 600 pages in its two earlier (2008) volumes (‘Architecture’ and ‘Consultation’ – see footnote 9) and more than 100 pages in the two volumes relating to retirement which were published in 2008 and 2009 (see footnote 9). The final report of the TWG Review looks insignificant by direct comparison, at only 74 pages, but its length increases exponentially and to a comparable figure to Mirrlees and Henry when all of its 19 background papers are included in the count.

Based upon its deliberations, the core or baseline principles enunciated by the Mirrlees Review are for a ‘progressive, neutral tax system’. The review emphasises the need to consider the tax system as a whole, to ensure that it is structured to meet overall spending needs but accepting that not all taxes within the system need to address all objectives. Hence, for example, ‘not every tax needs to be “greened” to tackle climate change as long as the system as a whole does so. And not all taxes need to be progressive as long as the overall system is’ (Mirrlees et al., this issue, p. 333). Moreover, the review cautions strongly against earmarking (or hypothecation) of taxes – ‘There is no reason for spending on particular items to be tied to receipts from particular taxes’ (Mirrlees et al., this issue, p. 333). A system-wide view of revenue adequacy is the preferred option.

In seeking neutrality, the review suggests that a tax system that treats similar economic activities in similar ways for tax purposes will tend to be simpler, avoid unjustifiable discrimination between people and economic activities, and help to minimise economic distortions. But it does not consider that there has to be slavish adherence to the neutrality principle. Hence exceptions – such as for taxes on alcohol and tobacco to dissuade harmful practices, or for the encouragement of saving for retirement, or for research and development incentives – may be appropriate and justifiable in particular circumstances. The important conclusion, however, is that the hurdle for departing from neutrality should be set high, requiring a strong and justifiable case. The list of exceptions, it suggests, would be far narrower than is presently the case.

The final guideline adopted by the review is that the tax system should seek to achieve progressivity as efficiently as possible. The review perceives that this should be primarily achieved through the rate schedule for personal taxes and benefits, carefully designed to minimise the efficiency loss associated with achieving progressivity. This means the schedule needs to reflect

> knowledge of the shape of the income distribution and the responsiveness of people to taxes and benefits at different income levels. It also implies taking decisions over both whether to work (including when to retire) and how much to work into account in addition to other responses such as tax avoidance and migration.
>
> Mirrlees et al., this issue, p. 334

The ‘vision’ identified by the Henry Review is one of a 21st century tax and transfer system able to

> meet its purposes efficiently, equitably, transparently and effectively. Critically, it would support per capita income growth rates at the upper end of developed country experience by encouraging high workforce participation, a more efficient pattern of saving, and stronger investment in education and physical capital. It would be robust, capable of supporting large structural change, dealing with unforeseeable external

> shocks and encouraging patterns of economic activity that prove fiscally and environmentally sustainable.
>
> Henry, 2009, p. xvii

The TWG Review considered options for reform in terms of six principles of a good tax system: the overall coherence of the system; efficiency and growth; equity and fairness; revenue integrity; fiscal cost; and compliance and administration costs. The review concluded that the current system required significant change, including changes to tax bases, tax mix, tax rates and supporting tax rules.

This summary suggests, rather unsurprisingly, that the principles underpinning the three reviews are not substantially different. All three have a strong system-wide focus (with an emphasis on revenue adequacy), and efficiency/neutrality as well as equity/progressivity are also strongly expressed and endorsed in all three. Henry may have a more explicit concern with robustness, flexibility, transparency and sustainability, but these concepts are implicit in Mirrlees and the TWG nonetheless.

The paper now considers how these underlying principles were translated into the major recommendations of each of the reviews.

IV. The outcomes of the reviews

Notwithstanding this shared appreciation of the more important principles upon which to base their proposals, it is very difficult to find any significant level of convergence in the actual recommendations made by the three reviews. This section initially outlines the principal recommendations of each of the three reviews, and then seeks to establish what common ground there is (which is relatively little) before considering why their major proposals may have diverged to such an extent.

The three underpinning guidelines or principles that were considered critical to the Mirrlees Review (consider the system as a whole; seek neutrality with minimal exceptions; seek progressivity as efficiently as possible) are translated, in that review, into 18 main recommendations broken down into five major groupings: taxes on earnings; indirect taxes; environmental taxes; taxation of savings and wealth; and business taxes (Mirrlees et al., this issue, p. 353).

So far as taxes on earnings are concerned, the review sees great merit in: merging the personal income tax with NICs; removing the opaque practice of tapered personal allowances and moving to a transparent coherent rate schedule (two or three rates of tax) which should be applied to income after allowing deductions for the costs incurred in generating that income; simplifying the benefits system with a single integrated benefit; and providing greater work incentives for parents whose youngest child is of school age and for those who are around retirement age (two groups who are particularly responsive to work incentives).

The indirect and environmental tax recommendations include: the removal of nearly all zero and reduced rates and exemptions from VAT (with a suitable compensation package for the less well-off); the introduction of a VAT-equivalent tax for the financial services sector; the replacement of the council tax and stamp duty land tax on housing with a tax proportional to the current value of domestic property; a shift towards consistent pricing of greenhouse gas emissions; and the replacement of the current taxes on petrol and diesel with a national system of congestion charging.

It is in the area of the taxation of savings and wealth that many of the more radical recommendations of the review are to be found. The recommendations include the complete exemption of bank or similar interest from taxation, and the partial exemption for capital income from the holdings of risky assets (by means of a rate-of-return allowance for substantial holdings of most equities, unincorporated business assets and rental properties). Hence only ‘excess’ returns would be taxed (at the same rate as earned income), and where these were derived in the form of capital gains or dividends they would be taxed at a reduced rate to reflect corporation tax already paid (as is currently the case in Norway). The review also recommends some fine-tuning of the current system of pension taxation, with an end to the overgenerous tax treatment of employer contributions and the replacement of the tax-free lump sum with an incentive better targeted to encourage responsible retirement saving. Finally in this area, the review suggests that the more egregious avoidance aspects of the current (and ‘not fit for purpose’) inheritance tax should be tackled through short-term amendment, but that longer term the possibility of a comprehensive lifetime wealth transfer tax should be considered.

The review’s recommendations for business tax reform also contain somewhat radical suggestions, including the introduction of an allowance for corporate equity (‘ACE’, as currently operating in, for example, Belgium) into the corporation tax (which would otherwise maintain the same rate) to align treatment of debt and equity and to ensure only ‘excess’ returns to investment are taxed. This also reflects the proposed treatment of capital income for personal investors. Further recommendations include aligning the tax treatment of income from employment, self-employment and corporate sources, and replacing business rates and stamp duty land tax on business property with a land value tax for business and agricultural land (matching the recommendation to remove the council tax and stamp duty land tax on housing for the non-business sector and replace them with a tax on domestic property, already noted above).

The reform proposals suggested by the Henry Review to achieve its vision of a 21st century tax and transfer system able to meet its purposes efficiently, equitably, transparently and effectively were presented in nine broad themes:

- concentrating revenue-raising on four robust and efficient tax bases (personal income assessed on a more comprehensive basis; business income; private consumption; and economic rents from natural resources and land); other taxes required to address social or economic costs, such as taxes on alcohol, tobacco, gambling and environmental costs, should be maintained where efficiently imposed; otherwise, a large number of inefficient taxes should be abolished;[20]
- configuring taxes and transfers to support productivity, participation and growth, through, for example: setting company tax rates towards the lower end of the small-to-medium OECD country average (25 per cent over the medium term); improving support for quality childcare; building clear work incentives into the levels of income support payments; improved treatment of business losses; and a discounted tax rate for personal capital income (interest, rents, capital gains);
- creating an equitable, transparent and simplified personal income tax, with much higher personal tax-free thresholds, removal of the existing complex array of thresholds and offsets, a simple two-step tax scale, rationalised work deductions (with a standard deduction linked to the level of income) and enhanced progressivity;
- developing a fair, adequate and work-supportive transfer system, with means-testing for all methods of primary support;
- integrating consumption tax compliance with business systems, by replacing inefficient State taxes (such as the current payroll tax) with a low-rate destination cash-flow tax and replacing the current inefficient input taxation of financial services under the GST with a more efficient financial services tax;
- adopting efficient resource and land taxation, entailing the replacement of existing resource royalties on all except low-value commodities with a uniform resource rent tax set at 40 per cent and the replacement of existing land tax arrangements (including stamp duty on land transfers) with a more comprehensive land tax based upon the value per square metre of land;
- completing retirement income reform and securing aged care;
- providing an environment geared toward more affordable housing;
- developing a more open, understandable and responsive tax system by means of a more citizen-centric tax system, including the capacity for personal taxpayers with simple tax affairs to have less interaction with

[20]The Henry Review notes that around 90 per cent of Australian tax revenue is raised through only 10 out of some 125 different taxes that are currently levied on businesses and individuals (Henry, 2009, p. 11).

the tax system and for business taxpayers to use normal business processes to engage with their tax affairs.

In turn, these nine themes were developed into the 138 detailed recommendations contained in the Henry Review.

The recommendations of the TWG Review in New Zealand principally focused upon aspects of the direct and indirect tax rates and tax base, with some broader suggestions relating to the corporate tax system, the welfare system and institutional arrangements relating to the process of tax reform itself. More particularly, the Tax Working Group (2010, pp. 10–11) proposed that there needs to be alignment, wherever possible, of the company tax rates and top personal and trust rates. Notwithstanding this, New Zealand's company tax rate also needs to be competitive (particularly vis-à-vis Australia) and this factor needs to be balanced against the integrity gains of full alignment. The top personal income tax rates of 38 per cent and 33 per cent should be reduced as part of the alignment strategy, and all personal income tax rates should be reduced where possible.

Most members of the TWG also favoured an increase in the rate of GST from 12.5 per cent to 15 per cent, with appropriate compensation to those on lower incomes.

The review also recommended broadening the income tax base. Whilst a capital gains tax (CGT) represents the most comprehensive option for broadening the base[21] and was favoured by some members of the TWG, most of the TWG had significant concerns over the practical challenges arising from a comprehensive CGT and the potential distortions and other efficiency implications that may arise from a partial CGT. Hence the majority favoured a more targeted approach and supported detailed consideration of taxing returns from capital invested in residential rental properties on the basis of a deemed notional return using a risk-free rate. Other options for base-broadening favoured by the TWG included: the introduction of a low-rate land tax; removing the 20 per cent depreciation loading on new plant and equipment; removing tax depreciation on certain buildings; and changing the thin capitalisation rules.

In terms of the indirect tax base, the review accepted that the GST should continue to apply broadly, with no exemptions.

The review also proposed that:

- the imputation system should be retained, but kept under review (particularly if Australia were to move away from imputation);

[21]New Zealand does not currently have a CGT regime although certain gains from property are charged to income tax.

- there should be a comprehensive review of welfare policy and how it interacts with the tax system, with an objective to reduce high effective marginal tax rates;
- the government should introduce institutional arrangements to ensure there is a stronger focus on achieving and sustaining efficiency, fairness, coherence and integrity of the tax system when tax changes are proposed.

It is evident that there is little common ground between the recommendations of the three reviews. For example, even though changes to aspects of the tax base and tax rates figure in various recommendations of all three countries, it is obvious that the focus in New Zealand's TWG Review is far more immediate and limited than that in either the UK Mirrlees Review or the Australian Henry Review. In New Zealand, the emphasis is upon income tax rate reduction and alignment (both between personal and corporate rates and between the rates appropriate to different business vehicles). In contrast, in the UK and Australia, there is less emphasis upon the nomination of actual rates and correspondingly greater concern with more structural issues such as the coherence of the rate schedules. And whereas the focus in the TWG Review is upon broadening existing tax bases, both Mirrlees and Henry seek to explore potentially new tax bases – Mirrlees with recommendations relating, for example, to wealth and capital taxation as well as land value taxes and congestion charges; and Henry in relation to a shift to greater reliance upon a resources and land tax base, including through the ill-fated Resources Super Profits Tax (on which, more in Section V).

There are also major differences between the UK and Australian reviews. Most noticeably, their proposals for business tax reform diverge very significantly. Australia, like New Zealand, adopts a 'watching brief', content to maintain its imputation system but prepared to consider alternatives should the need arise. In contrast, the Mirrlees Review, with a more radical approach, suggests that the ACE should be introduced to provide a more efficient and neutral corporate tax system.

The different approaches to tax reform in the three countries, manifest in the very different sets of recommendations in the three reviews, may be accounted for by the different economic and fiscal circumstances prevailing in each of the three countries. They are also, in all probability, the consequences of the somewhat different review processes that took place in each of the three countries, an aspect already explored in Section II. And it is also possible that the different outcomes reflect different political realities, an aspect explored in Section V.

V. Reform potential: the political dimension

To varying extents, and as would be expected, each of the three reviews is solidly underpinned by economic theory and an economic approach to tax design. This is most evident in the Mirrlees Review, where the analysis is strongly grounded in the modern economics literature on taxation, and in particular on optimal tax and social welfare theory. It is least evident in the TWG Review, while the Henry Review contains an interesting mix of the old and the new: some elements of its analysis and recommendations very clearly reflect the 'old' (later 20th century) comprehensive income tax consensus built on low tax rates and a broad base – for example, its proposal that 'all forms of wages and salary for Australian resident taxpayers should be taxable on an equivalent basis and without exemptions';[22] other elements and recommendations, such as its suggestion for a 40 per cent discount on the taxation of income from savings,[23] reflect the 'new' thinking about tax design.[24]

Notwithstanding this economic focus, there still remains the very difficult task of convincing 'the population, or at least a majority, of the rightness of tax reform proposals so that good economics ... become[s] good politics' (Sandford, 2000, p. 196).

The former Australian Prime Minister, Kevin Rudd, needs little reminding of the strong correlation between taxation reform and the political dimension. Only weeks after his government accepted, and attempted to implement, just one of the 138 recommendations of the Henry Review, a political coup took place and Rudd was replaced by his Deputy, Julia Gillard, in late June 2010. The measure that brought about his downfall was Recommendation 45, which suggested that 'the current resource charging arrangements imposed on non-renewable resources by the Australian and State governments should be replaced by a uniform resource rent tax ...' charged at a rate of 40 per cent (Henry, 2009, p. 89). The so-called Resources Super Profits Tax was killed at birth by a mixture of expensive, well-targeted and aggressive campaigning by the mining industry[25] and (arguably) political ineptitude and cowardice on the part of the government. (Ironically, this was the only recommendation that the Rudd government had initially accepted in full when the Henry Review was made public in May 2010. The vast majority of the other 137 recommendations were left 'on the table', while a handful were rejected outright and a few others were partially accepted then and later.)

[22]Recommendation 8 (Henry, 2009, p. 82).

[23]Recommendation 14 (Henry, 2009, p. 83).

[24]Cooper (2011) explores this amalgam of the old and the new in more detail.

[25]It is speculated that the advertising campaign alone amounted to spending of somewhere between AU$20 million and AU$29 million in a six-week period in the middle of 2010 (*Sydney Morning Herald*, 2 February 2011; *Sydney Morning Herald*, 7 February 2011).

That recent Australian lesson serves to underline the importance of the political dimension in any process of tax reform. Tax economists may freely engage in deliberations that seek to design the optimal tax system for a particular country at a particular time, and the results of their deliberations may well provide the best possible blueprint for tax reform in a particular country at a particular time. But no matter how well the tax reform package is crafted and justified in economic terms, it will still face enormous difficulties when attempts are made to translate the theoretically pure and appropriate into the practically possible.

Arguably, New Zealand has already been able to implement most of the reform proposals made by the TWG Review because its recommendations were not as deeply embedded in economic theory, and were far more limited, immediate and practical in focus, when compared with the longer-term blueprints identified for the UK and Australia by Mirrlees and Henry respectively. Strong government backing for the New Zealand review (in contrast to the political independence of the Mirrlees Review) may also account for the earlier implementation of review recommendations in the New Zealand case.

Ultimately, the feasibility of implementation of the Mirrlees tax reform proposals, as with those in Australia, will depend upon the extent to which other – exogenous – factors coalesce to secure a favourable outcome. At the very least, and as Sandford (2000, p. 194) has cautioned, it will require a finance or treasury minister with clear objectives and the energy, conviction and toughness to take on the lobbies and other vested interests and to push through the reforms. Such a visionary is not immediately apparent, at least to this observer, in either the UK or Australia. But it would be pleasant to be proved wrong, and there is ample time, in both countries, for the critical reform messages to filter through into the political processes and influence the future directions of the tax systems in those countries.

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