

The Administrative Foundations of the Chinese Fiscal State



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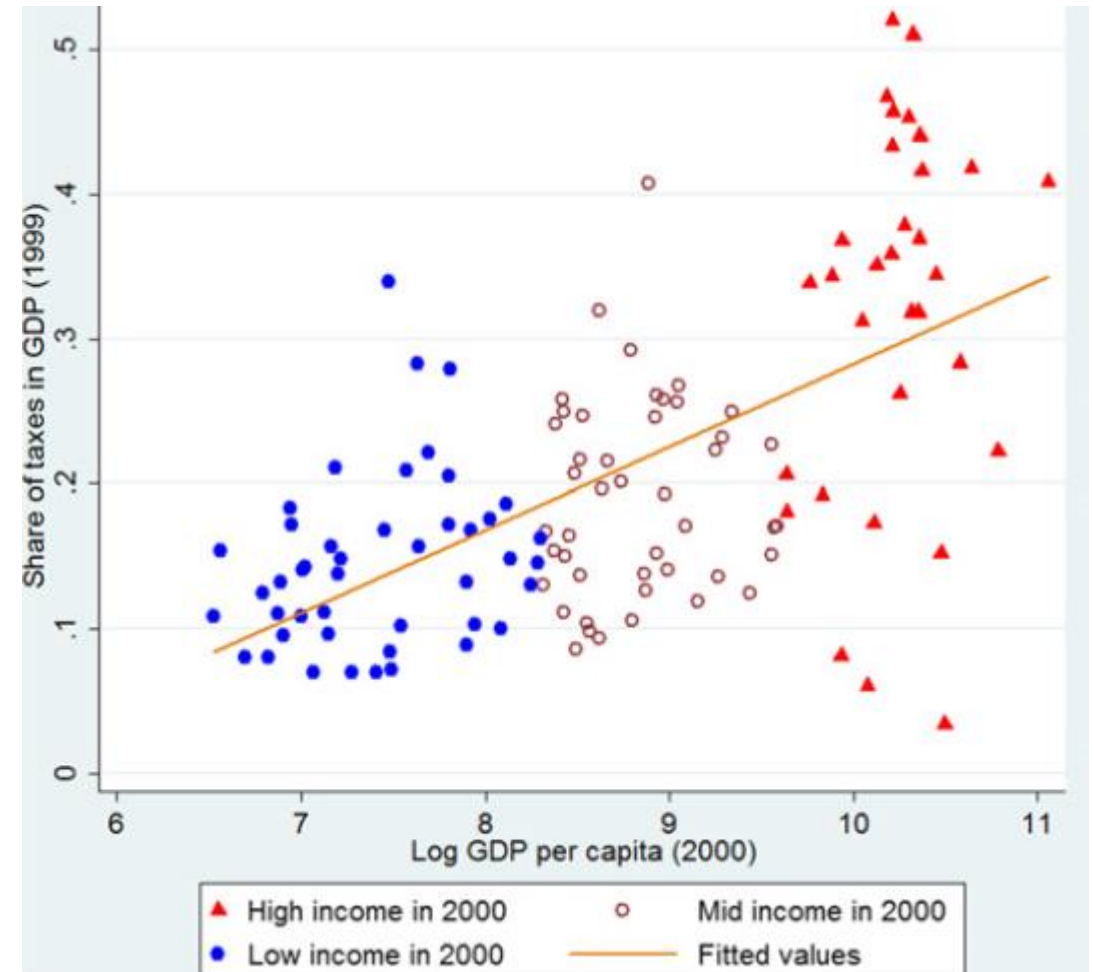
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1. The book's main story
2. Its main conceptual arguments
3. Why the story/arguments matter

How do the world's advanced economies collect tax?

- Self-assessment is central.
- Self-assessment is mainly carried out by businesses
- The government enforces the norm of truthful reporting through audits: but audit rates and penalties generally are not high.



How to introduce the practice of self-assessment when a country doesn't have it?

- China had no self-assessment system before the mid-1990s.
- 1993 tax reform introduced modern taxes that assumed self-assessment: VAT, broad-based excises, enterprise income tax, etc. Rules to be uniform across the country.
- Tax administration reform launched in 1997 to support this national transformation.

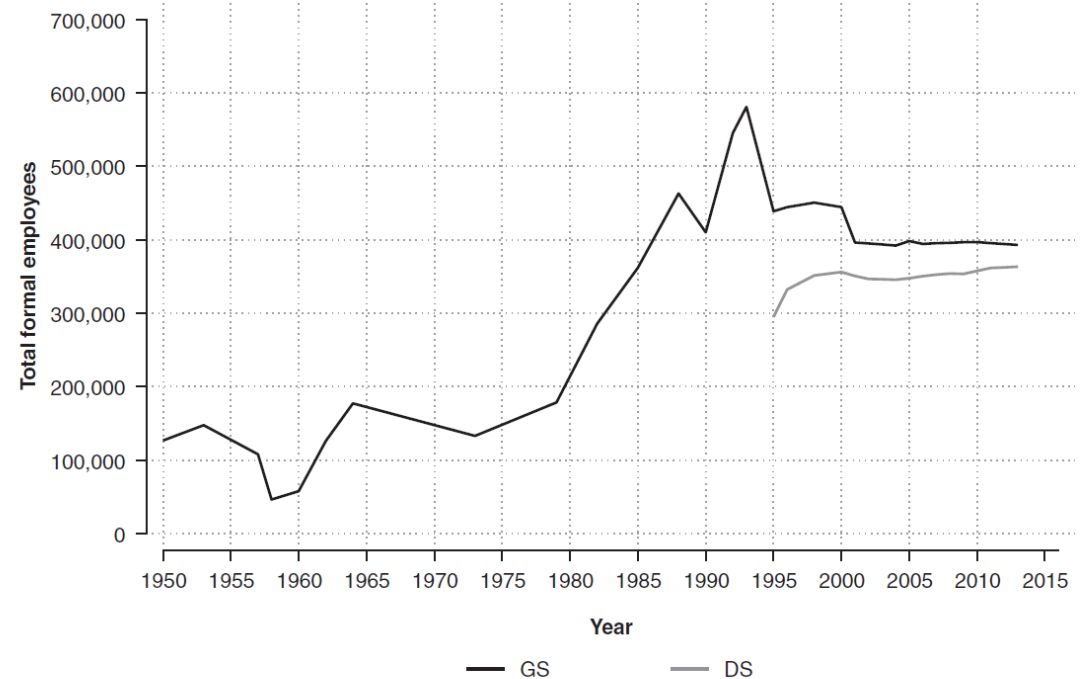


Figure 1.1 The evolution of China's tax administration workforce

- By 2005, the effort to promote self-assessment has largely stalled. Tax agencies began to revert to 1980s-style tax collection.

- **How come?**



Conceptually, what is at stake in this story?

- Self-assessment exemplifies social ordering through legal norms. Economic and sociological theories of tax compliance have neglected law's importance for positive theory.
- What is law? (Hart, Fuller, etc.)
 - A clearly announced set of rules;
 - The rules represent *norms*—non-compliance with which draws disapprobation from others;
 - Subjects find it rational to follow and enforce the norms aside from penalties from officials.

- The reliance on private enforcement explains the most prominent features of the concept of law.
 - If rules are to be exclusively enforced by public agents, they would not have to be common knowledge, display generality, public promulgation, non-contradiction, etc. (the Fullerian features of law)
 - When one substitutes public enforcement for private enforcement, one erodes the rule of law's micro-foundations.
- Self-assessment in taxation is exemplary of private enforcement, and therefore the rule of law's micro-foundation.
 - What happens when public enforcement substitutes for self-assessment?

- This is what happened in China when the promotion of self-assessment stalled.
 - Atomistic coercion: routine government intervention in basic compliance (Chapter 3)
 - No real audit, no fostering of the norms of truthful reporting, no penalties (Chapters 2 and 4)
 - Tax liability determined extensively by government interventions: mechanical determinations such as encrypted invoices (chapter 8); in-person negotiations (chapters 2-4)
- Interestingly, most economic theories about tax compliance likewise privilege public enforcement over self-assessment (Chapter 8):
 - Both Chinese tax administrators and Western economists are more interested in substitutes for the rule of law than in law. Western theories better describe Chinese than Western practice!

Why did China do it this way?

- It raised revenue (as predicted by Western economists!)
- Focus on ex ante interventions made political sense (Chapter 5) because:
 - It generated feasible performance metrics for low-level civil servants;
 - It generated revenue elasticity for low-level politicians;
 - The drive to create cohesion within the state apparatus shaped the strategy to revenue collection.
- Finally, it is complementary to technology.

Why should we care that China collects tax this way?

- Tax systems in advanced economies are consistent with the micro-foundations of rule of law. To know that a major system can function without such foundations is social scientifically informative.
- This is how things are done in other major spheres of Chinese governance, too.
- Implications for studying Chinese law:
 - The super-structures of law (legislatures, courts, etc.) will not work well when law lacks micro-foundations.
 - There is a well-resourced legal system. It is simply little used in Chinese taxation (Chapter 7). Law is important mainly in political rhetoric.
 - When substitutes have been found for “rule by law” (“thin” conception of rule of law), there is no basis to discuss thicker conceptions of rule of law.

Why Chinese taxation (even without law) is important

“Little else is required to carry a state to the highest degree of opulence from the lowest barbarism, but peace, easy taxes, and a tolerable administration of justice; all the rest being brought about by the natural course of things.”

Adam Smith 1755.

- Regime legitimacy may not depend on the rule of law. (Most Chinese taxpayers seem OK without it!)
- Regime legitimacy likely will depend on the strength of the social safety net, redistribution, and government spending to sustain economic prosperity. On these matters, China and Western democracies still share a common language.

Thank you, and please read [the book!](#)

