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Interlinking between Income Tax, Citizenship and Democracy? A Case Study of Canada and China

[DRAFT]

Written for the Workshop on "The Interlinking between Taxation, Citizenship, and Democracy" on May 8, 2023, Oslo, Norway

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[The author thanks the research assistance of Luke Chao and David Zhang, JD candidates. She recognizes the support of Social Sciences and Humanities Research Council of Canada for a project that this research is part of.]

1. INTRODUCTION

The interlink between taxation, citizenship and democracy appears to be obvious in Western democracies: citizens are voters, taxpayers and beneficiaries of public spending funded by tax revenues.[1] The literature on the politics of taxation suggests that democratic institutions affect taxation at every stage of the policy-making process,[2] the type of elections and governance model influence the level of redistribution and complexity of the tax system,[3] democracies generally choose policies that are more favorable to the poor than non-democracies,[4] the tax mix varies with the nature of the political regime,[5] and more repressive governments rely less on personal income taxation.[6] Political citizenship is not identical to tax citizenship as most countries rely on residence as the basis of tax jurisdiction and some citizens living abroad are not tax residents.[7] However, citizenship can be viewed as a proxy for domicile[8] and, in effect, correspond to residence in most cases. The principle of "no taxation without representation" captures the quintessential link between taxation and democracy.

Canada is a liberal democracy. China is not. Both are tax states in that public spending is funded primarily by tax revenues: in 2022, tax revenues account for about 92% of total revenues of the government of Canada

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[1] Neil Brooks, "Taxation and Citizenship", Labour / Le Travail , Fall, 2001, Vol. 48 (Fall, 2001), pp. 353-358 "Tax law is shot through politics"); Wolfgang Schön, "Taxation and Democracy" (2018) 72 Issue 1 Tax L Rev. available at SSRN: https://ssrn.com/abstract=3267279 (there is a notion of congruence" – individuals vote on the tax to pay, pay the tax, and benefit from the tax); Nancy C. Saudt, "Taxation without representation" (2002) 55 Tax L. rev. 555, at 556 (taxation and democracy is mutually reinforcing; "taxation is central to how the members of a democratic state experience their participation in the democratic community).

[2] See Andrew Gould and Peter J. Baker, "Democracy and Taxation", (2002) 5 Annu. Rev. Polit. Sci., 87-110. See also Edgar Kiser and Steven M. Karceski, "Political Economy of Taxation", (2017) 20 Annu. Rev. Polit. Sci. 75-92.

[3] E.g., Sven Steinmo, "Taxation and Democracy: Swedish, British and American Approaches to Financing the Modern State" (Yale University Press, 1996); V. Birchfield and M.M.L. Crepaz, "The Impact of Constitutional Structures and Collective and Competitive Veto Points on Income Inequality in Industrialized Democracies" (1998) Eur. J. Polit. Res. 34:175-200; Sven Steinmo and C.J. Tolbert, "Do Institutions Really Matter? Taxation in Industrialized Democracies" (1998) 31(2) Comp. Polit. Stud. 165-87; BjÃ Volkerink and Jacob de Haan, *Political and Institutional Determinants of the Tax Mix: An Empirical Investigation for OECD Countries* (1999) (http://irs.ub.rug.nl/ppn/183019881).

[4] Allan H. Meltzer and Scott F. Richard, "A Rational Theory of the Size of Government" (1981) 89(5) *J. of Polit. Econ. 914-27;* Carles Boix, *Democracy and Redistribution* (Cambridge: Cambridge University Press, 2003).

[5] Lawrence W. Kenny and Stanley L. Winer, "Tax Systems in the World: An Empirical Investigation into the Importance of Tax Bases, Administration Costs, Scale and Political Regime" (2006) 13 *Int Tax Public Finan*, 181–215; Pavlos Balamatsias, "Democracy and Taxation" (2016) MPRA Paper No. 82563 (https://mpra.ub.uni-muenchen.de/82563 (democratic countries rely on progressive income tax to win support from the majority); Meltzer and Richard, supra note 4 (taxation and public spending for redistribution reasons are affected by the political process and by majority rule voting).

[6] Kenny and Winer, ibid.

[7] For a discussion of taxing citizens, see Reuven Avi-Yonah, "Taxing Nomads: Reviving Citizenship-Based Taxation for the 21st Century", *U of Michigan Public Law Research Paper No. 22-035;* Ruth Mason, "Citizenship taxation," (2016) 89 S. *Cal. L. Rev.* 169, 169; Giorgio Beretta, "Citizenship and Tax" (May 2019) World Tax J. 227-259.

[8] Edward A. Zelinsky, "Citizenship and Worldwide Taxation: Citizenship as an Administrable Proxy for Domicile", (2011) Iowa L. Rev. 1292.

and 94% of revenues of the government of China.[9] Income taxation is a major source of revenue in both countries. The level of taxation and tax structure are shown in Table 1.[10]

Table 1: Tax Level and Tax Structure in Canada and China

	Tax-GDP ratio	Corporate Income tax to total tax revenues ratio	Personal income tax to total revenues ratio	Social security contributions to total tax revenues	VAT/GST to total tax revenues
Canada (2020)	34.2%	12%	38%	14%	13%
China (2020)	20.1%	21%	6%	24%	30%

To what extent can these similarities and differences be explained by political differences? In other words, is there any interlink between income tax, citizenship and democracy, and if so, in what ways?

This paper seeks to examine these questions through a comparative case study. Part 2 presents the two income tax systems to set the stage for some comparative analysis. Part 3 shows that citizenship is the linchpin for defining tax citizenship and fiscal citizenship. Part 4 explains the meaning of democracy and its connection to tax policy making. Part 5 infers different level of interlinking between income tax, citizenship and democracy in different dimensions of income tax law. Part 6 concludes the paper.

This paper aims to contribute to literature by presenting a more nuanced analysis of the relationship between political regimes and income tax laws through a comparative study. It hopes to add to literature by showing that the interlink is weak in the technical and economic dimensions and more evident in the social dimension. However, even in the social dimension, there are other factors that may explain the different role progressive income tax plays in the two countries.

2. A TALE OF TWO TAX SYSTEMS

2.1 CANADA

2.1.1 History

Income tax was first introduced in 1917 (the *Income War Tax Act (IWTA).*[11] "The statute was drafted and enacted in haste in response to pressing political rather than fiscal imperative, using materials readily at

[9] See Canada, Annual Financial Report of the Government of Canada Fiscal Year 2021-2022 (https://www.canada.ca/en/department-finance/services/publications/annual-financial-report/2022/report.html); China, Ministry of Finance, "Central Government General Public Budget Revenues 2023" (http://yss.mof.gov.cn/2023zyczys/202303/t20230327_3874779.htm) (total revenues of CNY 9488498 millions, of which CNY 8997512 millions were tax revenues in 2022).

[10] Revenue Statistics 2022 – Canada, file:///C:/Users/jinyanli/OneDrive%20-%20York%20University/Desktop/1WORK/1Democracy%20&%20Taxation%20Oslo/literature/revenue%20tax%20structure/2022%20revenue-statistics-canada.pdf; Revenue Statistics in Asia and the Pacific 2022 – China, https://www.oecd.org/tax/tax-policy/revenue-statistics-asia-and-pacific-china.pdf. See also Baoyun Qiao, et al, *Critical Issues for Fiscal Reform in the People's Republic of China, Part 1: Revenue and Expenditure Management* (ADB East Asia Working Paper Series, No.53, Dec.2022).

[11] S.C. 1917, c. 28 [*IWTA 1917*]. For an overview of the importance of the IWTA, see J. Li & S. Wilkie, "Celebrating the Centennial of the Income War Tax Act, 1917: The Future by the Light of 100 Candles" in J. Li, J.S. Wilkie & L. Chapman, eds., *Income Tax at 100 Years*: *Essays and Reflections on the Centennial of the*

hand, and it was a work in progress from the beginning."[12] The conscription of wealth was necessary to enable the passing of the conscription law.

The ITWA imposed tax on the income of individuals at progressive rates and corporations at a flat rate. It adopted residence as the jurisdictional threshold to emphasize social and economic ties with Canada as opposed to political status (citizenship) or parental intention (domicile). "Any person can be a taxpayer in Canada", a visceral response to inclusiveness and pragmatism for a young immigrant country.[13] It adopted the self-assessment system and the necessary rules to ensure its operation, such as the provision of information to the minister, the minister's power to audit, request for information and impose penalties, as well as dispute resolution.

The political context of the IWTA's enactment made it very clear that the incidence of income tax is supposed to be borne by high-income people. The income tax was an "elite tax". This changed in the 1940s when source withholding was introduced to include working-class people in the tax base. By turning working class Canadians into new taxpayers helped making the tax bargain part of the democratic process and most citizens had a new direct effect on tax policy.[14] Fiscal policy makers began to see the need for making a connection between taxes on small income and provision of social goods in the form of social security and tax reliefs. Taxpayers' resistance to the income tax was replaced by negotiated tax concessions.

> "[P]ersonal income tax, along with more obviously, conscription and wage and price controls, made the national state so much more intimately involved in daily life that a responsiveness to popular opinion was newly important as a means of legitimating state power. On an array of tax matters, from those affecting the poor to those affecting taxpayers in "special" circumstances, Finance and Revenue listened to concerns raised by taxpayers and took steps to address those concerns. Most of these steps were related to variations in family obligations and the relationship between saving and taxation. In this respect, it is easy to see how modifications of personal income taxation would come to be connected to child welfare and old age security dimensions of the nascent welfare state.[15]

During the 1950s and 1960s, there were significant changes in the social, economic and political conditions in Canada that exposed the deficiencies of tax policy and administration. There was a cat-and-mouse game of litigation and legislation between big taxpayers and revenue authority. Many "small" or new taxpayers had to comply with tax filing and record keeping requirements. The revenue authority had to learn how to communicate and educate a growing new taxpaying public. Meanwhile, the tax base was narrow by excluding capital gains and eroded by "loopholes". The creation of social security (e.g., Old Age Security) and social insurance programs (such as employment insurance and Canada Pension Plan) added fiscal

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Income War Tax Act (Toronto: Canadian Tax Foundation, 2017] at 1:1. See also William Watson and Jason Clemens, eds., *Zero to 50 in 100 Years: The History and Development of Canada's Personal Income Tax* (Fraser Institute 2017).

[12] Colin Campbell and Robert Raizenne, in J. Li, J.S. Wilkie & L. Chapman, eds., *Income Tax at 100 Years*: *Essays and Reflections on the Centennial of the Income War Tax Act* (Toronto: Canadian Tax Foundation, 2017] at 2:1; Campbell and Raizenne, *A History of Canadian Income Tax, Volume 1 – the Income War Tax Act 1817-1948* (Toronto, Canadian Tax Foundation, 2022).

[13] Li and Wilkie, supra note 11.

[14] Shirley Tillotson, *Give and Take: The Citizen-Taxpayer and the Rise of Canadian Democracy* (UBC Press, 2017), at 202. See also David Tough, *The Terrific Engine: Income Taxation and the Modernization of the Canadian Political Imaginary* (UBC Press, 2018).

[15] Tillotson, ibid.

pressure and citizen's sense of participation in the tax and fiscal policy-making. A new phase of Canadian democracy, one in which the promise of all people would be heard and well served by the state, seemed to be on the verge of fulfilment.[16] A royal commission on taxation chaired by K. Carter was established in 1962 to "examine anomalies in the existing laws, consider inequitable tax burdens, close loopholes that now existed and ease hardships now caused by some laws."[17]

The Carter Commission assembled a large team of researchers and experts, resorted to economic science, embraced the principles of ability to pay and neutrality and recommended measures to broaden the tax base (a buck is a buck is a buck) by taxing capital gains, integrate corporate and personal income taxes, close loopholes and raise the exemption threshold to lighten the burden on the poor. The 6-volume report was published in 1966, providing the blueprint for the 1971 reform – the most important reform since 1917.[18] It took five years of consultation, back-and-forth negotiations and balancing the interests of various groups. Upon the release of a white paper to implement the recommendations, Finance Minister and the prime minister engaged Canadians in an exercise in participatory democracy. Citizen engagement was at its highest level. Modern social science and economic science met with populism (the voices of diverse mass electorate), resulting in a new tax system that is informed by first principles, but also offers something for almost everybody. The new Income Tax Act (ITA) came into effect in 1972, 10 years after the creation of the Carter Commission.

The 1987 tax reform followed the transformative US tax reform by the Regan administration in 1986.[19] Federal Finance Minister Wilson released a White Paper on Tax Reform on June 18, 1987. The White Paper package contained over 500 pages of statistics, graphs, analysis and proposals covering the personal and corporate tax systems as well as a new broad-based Goods and Services Tax (GST). The complex materials were summarized in reader's Digest-like pamphlets which the government freely distributed in shopping centers, supermarkets and other public places to generate public debate. The public had two months to submit comments to a Parliamentary committee. Business groups focused on all aspects of the reform, labour, women's and social policy groups focused more on personal income tax and the GST. The overall objectives of the tax reform were fairness, competitiveness, simplicity, consistency and reliability. Broadening the base and lowering the rate were the main themes. Tax base was broadened by reducing tax exemptions and converting some policy-based deductions to credits. The top marginal personal tax rate was reduced from 34 percent to 29 percent and the number of brackets reduced from ten to three. It also included the introduction of the GAAR to counter increasingly aggressive tax planning practices and mandate the courts to consider the object, spirit and purpose of the legislation in tax avoidance cases.

Subsequent changes to the Income Tax Act mainly include specific anti-avoidance rules and spending programs in the form of tax expenditures and income-support payments. For example, a refundable GST credit was introduced in 1990 to provide some relief to low-income Canadians who had to pay a regressive GST. In 1992, a refundable Working Income Supplement was introduced along the lines of the Earned Income Tax Credit in the United States. In 2016, a Canada Child Benefit was introduced to support low-

[16] Ibid., at 276.
[17] Ibid., at 285.
[18] For critique of the Carter Report, see Richard A. Musgrave, (1968) 1:1 The Canadian Journal of Economics, 159-82; Boris I. Bittker, "Income Tax Reform in Canada: The Report of the Royal Commission on Taxation," (1968) 35 The University of Chicago L. Rev. 637-59; Kim Brooks, ed., *The Quest for Tax Reform Continues: The Royal Commission on Taxation Fifty Years Later* (Thomson Reuters, 2013).
[19] For further, see Geoffrey Hale, *The Politics of Taxation in Canada* (Broadview Press, 2002), 181-248.

income families with children.[20] In 2023, a child dental care payment program was introduced as the newest refundable tax credit.

2.1.2 Policy Objectives

Fairness is the most important reason for enacting the 1917 Income War Tax Act.[21] In 1916, the government committed to double the size of the Canadian army, but enlistments were far outpaced by casualties in the ceaseless attrition of trench warfare. Conscription was necessary, but the working classes were opposed to conscription and asked that "if they are to be called upon to give their blood, the wealthy class should, at least, give their wealth."[22] The government was wrestling with some other difficult issues, such as rampant inflation, rising labour unrest and militancy, the controversy over the use of French in Ontario schools. A federal election in 1917 was inevitable when attempts to form an all-party wartime coalition failed. To win support, the government introduced the Income War Tax Act a few days after introducing the Military Service Act. The Minister of Finance spoke during the conscription debate about the fairness of income tax. He attributed much of the public pressure for income taxation to the failure of a few prominently wealthy individuals to make sufficient contributions voluntarily to the Red Cross or the Canadian Patriotic Fund. It is clear that income tax was adopted for political reasons.

Fairness has been invoked to justify subsequent tax reforms. The most recent one is about taxing large multinational enterprises (MNEs) under Pillar One and Pillar Two – making MNEs pay their fair share of taxes and levelling the playing field for Canadian workers.[23] Fairness has also been invoked to support the introduction of the general anti-avoidance rule and other anti-avoidance rules. The proposed amendment to the GAAR provision includes a preamble, stating that the GAAR was necessary to protect the tax base and the fairness of the tax system.[24]

Equity is an important objective identified by the Carter Commission.

> The government can change the distribution of the flow of goods and services among individuals and groups of individuals by imposing higher taxes on some than on others, by making larger transfers of purchasing power to some individuals or groups than to others, and by providing public goods and services that benefit some more than others.[25]

The tax expenditure mechanism (including transfers) is equitable "when it increases the flow of goods and services to those who, because they have little economic power relative to others, or because they have particularly heavy responsibilities or obligations, would otherwise not be able to maintain a decent standard of living."[26] In order to achieve a more equitable distribution of output, the tax burden should be allocated "in proportion to ability to pay."[27]

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[20] For further, see Wayne Simpson, "The Rise of Refundable Tax Credits: Implications for the Canada Disability Benefit" (2023) *Osgoode Hall L. J.* (forthcoming).
[21] Campbell and Raizenne, supra note 14, at 26-29; Richard Krever, "The Origin of Federal Income Taxation in Canada" (1981) 3:4 *Canadian Taxation: A Journal of Tax Policy* 170-88.
[22] Debates, June 18, 1917, at 2398 (Campbell book, 28)
[23] Canada Budget 2022 and Budget 2023.
[24] Canada, Budget 2023, Tax Measures: Supplementary Information, at 67.
[25] Canada, Report of the Royal Commission on Taxation (Ottawa, 1966) (Carter Report), Vol.2, at 10.
[26] Ibid., at 11.
[27] Ibid.

> This means, in effect, that the government must seek to impose progressive marginal tax rates on all additions to personal economic power, without regard to the source of those increments in power. Wages, salaries, business profits, gifts and capital gains all increase the economic power of the recipients and should be treated on exactly the same basis for tax purposes.

The notion of vertical equity and horizontal equity are used in most tax policy debates.

Economic growth has been another major policy objective. As a young country that was dependent on inflow of foreign capital and international trade, ensuring the tax system does not alarm investors was a main policy concern in 1917. Politicians took pains explaining that the use of "conscription of wealth" meant taxation of income, not wealth.[28] "To maximization of the growth of output" was listed as the first objective in the Carter Report. To achieve this goal, the tax system should be neutral:

> The tax system should be neutral in the sense that, with explicitly specified exceptions, it should be designed to bring about a minimum change in the allocation of resources within the private sector of the economy relative to the allocation that would take place in the absence of taxes. …
>
> Where there are imperfections in the market mechanism, as the result of uncertainty, immobility of the factors of production, monopoly power, and so on, the tax system should be used to change the allocation of resources to compensate for these imperfections. However, the use of compensatory non-neutral tax provisions is not justified if other policy instruments could achieve the same result at a smaller total cost than could tax provisions.[29]

Making the tax system work is a major goal of tax reform. The self-assessment system introduced in 1917 has remained largely unchanged. The changing legal and business circumstances, including globalization, digitization, and the rise of artificial intelligence and cryptocurrency, have called for changes to be made to the specific features of the system without undermining its core design. While tax rules need to be designed to work in practice, a collection of rules, by itself, is not enough. "What make those rules come to life is how they are applied – that is, how they are administered by those in the private and public spheres who are responsible for making the bones of the tax skeleton … more smoothly by supplying the necessary cartilage and muscle."[30] The humanity of the tax statute in terms of serving the needs of people and behavioral significance of participants of the tax system "play an indispensable role in the Canadian income tax system."[31]

2.1.3 The Taxing Regime

The taxing regime refers to the most fundamental aspects of the tax system designed to raise revenue. The ITA defines liability to tax by reference to the residence of a person: the worldwide income of any person resident in Canada at any time of the year is subject to tax, while only the Canadian-source income of a non-resident is subject to tax.[32] Personal income tax rates are progressive, ranging from 15% to 33% at the federal level.[33] Taxpayers must file tax returns to report and pay taxes.

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[28] Campbell and Raizenne (book), supra note 12, at 30.
[29] Carter Report, supra note 25, vol.2, at 8.
[30] Li and Wilkie, supra note 11, at 1:14.
[31] Ibid, at 1:15.
[32] Income Tax Act (ITA), RSC, 1985, c.1 (5th Supp.), ss.2 and 3.
[33] ITA, s.117(2).

To backstop the progressive personal income tax, the ITA provides for numerous rules to, in effect, "look through" private corporations to prevent the deferral or shifting of tax through the use of corporations. For example, passive investment income of resident private corporations is taxed at rate parallel to the top personal tax rate and passive income of controlled foreign corporations is imputed to the resident shareholder for tax purposes.

The ITA does not define "residence" in any comprehensive manner and provides for two deeming rules. Subsection 250(1) deems an individual to be resident in Canada throughout a taxation year even if the individual is not physically present in Canada. Examples are Canadian diplomats or members of Canadian armed forces who are based overseas. The sojourner rule is perhaps the more litigated one. Under paragraph 250(1)(a), a person shall be deemed to have been resident in Canada throughout a taxation year "if the person sojourned in Canada in the year for a period of, or periods the total of which is, 183 days or more".[37] In practice, this deeming rule applies primarily to non-citizens.

Subsection 250(3) provides that "a person resident in Canada includes a person who was at the relevant time ordinarily resident in Canada".[31] It is typically relied upon together with the common law test to determine whether a person who has been absent from Canada for a significant period of time retains his or her Canadian residence. It reinforces the proposition that a temporary absence from Canada (even one lasting more than one or two years) does not necessarily involve a loss of Canadian residence. The ITA seeks to determine objective determinants of whether a Canadian's departure from Canada is intrinsically temporarily and anchored in Canadian interests, as would be the case for Canadian diplomats and members of the military (subsection 250(1)). It typically applies to citizens and long-time residents.

Parliament chose to leave the general meaning of residence undefined because it is quite impossible to give it a precise and inclusive definition. There is a plethora of cases defining the meaning of residence. The courts have held "residence" to be "a matter of the degree to which a person in mind and fact settles into or maintains or centralizes his ordinary mode of living with its accessories in social relations, interests and conveniences at or in the place in question".[34] Ultimately, the common law test is based on the facts and circumstances of the case. Key factors considered by the courts include: whether a dwelling is available in Canada for occupation by the taxpayer or the taxpayer's family; whether the taxpayer's spouse and children are residents of Canada; whether the taxpayer retains coverage by public health insurance; social and economic ties.

In general, it is harder to give up residence than not acquiring one. For example, in *Thomson v. M.N.R.* (1946),[35] the taxpayer, a wealthy Canadian citizen who had gone to a lot of trouble to give up his Canadian residence, was held nonetheless to be a resident of Canada. In 1923, he sold his home in New Brunswick, announced that Bermuda was now his residence, and went to Bermuda. In the following years, he spent very little time in Bermuda, mainly living in the United States, where he built a house that was kept permanently ready for occupancy and where he spent most of his time. Starting in 1932, he began to regularly return to New Brunswick for four or five of the warmer months every year, and he eventually

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[37] ITA, supra note 32, s. 259(1)(a). Paragraph 250(1)(b) also deems members of the armed forces and federal and provincial civil servants who are stationed outside Canada to have been resident in Canada. The most important and interesting provision is para. (a), under which a person who "sojourned" in Canada for 183 days in a taxation year is deemed to have been resident for the entire year.

[31] ITA, supra note 32, s. 250(3).

[34] Canada Revenue Agency, Folio S5-F1-C1, "Determining an Individual's Residence Status" at para. 1.5.

[35] *Thomson v. M.N.R.* (1946), [1946] C.T.C. 51, 2 D.T.C. 812 (S.C.C.), at para. 47.

built a house there that was kept available all year long. Every year, however, he kept his stay in New Brunswick to less than 183 days (to avoid the sojourning rule). The taxpayer's wife and child accompanied him in these regular migrations. The Supreme Court of Canada, by a majority, held that the taxpayer was resident in Canada. Rand J., who wrote the principal opinion, said that the taxpayer's time in Canada was not a temporary "stay" or "visit":

> His living in Canada is substantially as deep rooted and settled as in the United States. In terms of time [the United States] may take precedence but at best it is a case of *primus inter pares*. He is [in Canada] as at his "home"; and the mere limitation of time does not qualify that fact . . . That brings him within the most exacting of any reasonable interpretation of "resides" or "ordinarily resident.[36]

In a more recent case, *Hauser v. R.* (2005),[37] an Air Canada pilot was found not have sufficiently "divorced" himself from Canada when moving to the Bahamas. The Tax Court remarked:

> Canada was a magnet that attracted the Hausers. After they set up residence in the Bahamas both of Mr. and Mrs. Hauser, and particularly Mr. Hauser, continued to have a presence in Canada. Mr. Hauser spent over a third of a year in Canada each year. Air Canada required Mr. Hauser to be in Canada to fly airplanes; he reported to work at Pearson Airport and other airports in Canada. Most of his flights left from and returned to Pearson; much of his training was at Pearson. Pearson Airport was part of the routine of life. Mr. Hauser's presence in Canada during the years in appeal was not occasional, casual, deviatory, intermittent or transitory. He was in Canada in great part because he had to be, to earn a living.[38]

In contrast, in *Shih v. R.* (2000)[39] the taxpayer immigrated to Canada with his wife and three sons, purchased a home in Canada and returned to Taiwan to work in the same year. He visited Canada annually to see his family but his stays did not exceed 59 days in any given year. He had several residential ties to Taiwan: other family members; a job that he had held for 25 years; a house that he owned; various memberships; a driver's licence and bank accounts. Based on these facts, the Court held that the taxpayer's connections with Canada (his house and wife and sons) were not strong enough to make him a resident of Canada. The taxpayer's primary reason for having a connection to Canada was to educate his children. The fact that the wife and children were "social citizens" in terms of benefiting from public health care and education was not considered pertinent.

2.1.4 Tax Expenditures and Transfers

The ITA has two types of spending programs: tax expenditures and transfers. They are generally available to resident taxpayers.[40]

Personal tax expenditures generally take the form of non-refundable tax credits. A universal credit is available to every taxpayer for the "basic personal amount." Over 100 credits cover almost every aspect of life: [41]

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[36] *Thomson*, *supra* note 35 at para. 56.
[37] *Hauser v. R.* (2005), [2005] 4 C.T.C. 2260, 2005 D.T.C. 1151 (T.C.C.); affirmed [2006] 4 C.T.C. 193, 2006 D.T.C. 6447 (Fed. C.A.).
[38] *Ibid.* at para. 58.
[39] *Shih v. R.* (2000), [2000] 2 C.T.C. 2921, 2000 D.T.C. 2072 (T.C.C.).
[40] Canada, Report on Federal Tax Expenditures 2022.
[41] Brooks, boutique

- Education: education tax credit; textbook tax credit; tuition tax credit; exemption of scholarship, fellowship and bursary income; student loan interest credit; registered education savings plans
- Family: spouse or common-law partner credit; dependent care credit; Canada caregiver credit; tax treatment of alimony and support payments
- Children: adoption expense tax credit; child care expense deductions; eligible dependent credit
- Old age and retirement: age credit; pension income splitting; pension income credit; registered retirement savings plan; registered pension plans,
- Health and disability: infirm dependent credit; medical expense credit; disability credit; disability support deduction; registered disability savings plan; refundable medical expense supplement; home accessibility tax credit; non-taxation of benefits from private health and dental plans
- Housing: non-taxation of capital gains on principal residence; first time home buyers' tax credit; first-time home savings account
- Savings and investment: partial inclusion of capital gains; tax-free savings account
- Donations: charitable donation tax credit; first-time donor's super credit; non-taxation of capital gains on donations of cultural property and ecologically sensitive land
- Employment and self-employment: non-taxation of strike pay, employee stock option deduction, Northern residents deduction; Canada training credit, deduction of costs incurred by musicians and tradespeople
- Social and religion: deduction for clergy residence; moving expense deduction, deduction of union and professional dues; deduction for contributions by individuals who have taken vows of perpetual poverty;
- Indigenous Canadians: non-taxation of personal property (including income) of status Indians and Indian bands situated on reserve
- Culture: Canadian journalism labour tax credit; film or video production services tax credit; credit for subscriptions to Canadian digital news media; deduction for self-employed artists; tax-free amount for emergency services volunteers.

A Conservative government tends to introduce boutique tax expenditures to benefit relatively narrowly defined groups of potential conservative voters, such as: "parents who enroll their children in fitness and arts programs, people who purchase public transit passes, volunteer firefighters, search and rescue volunteers, adoptive parents, people who care for infirm family members, first-time home buyers, people who renovate their homes, seniors and disabled people who undertake alterations to make their homes more accessible, students purchasing textbooks, and first-time donors to charities."[42] The Liberal government tends to introduce income support programs.

There are several income support programs implemented through the ITA: Canada Child Benefit, Canada Workers' benefit, Refundable GST credit, and refundable medical expense supplement. They

Table 2: Tax Transfers in Canada

Program[43]	Number of recipients (2019)	Estimated cost for 2019	Estimated cost for 2022

[42] Neil Brooks, "Policy Forum: The Case Against Boutique Tax Credits and Similar Tax Expenditures," (2016) 64(1) Canadian T. J. 67-129 ("Brooks Tax Expenditures").
[43] The source for the data is *Report on Federal Tax Expenditures 2022*, supra note 40.

Canada Child Benefit	3.5 million	$24.3 billion	$25.5 billion
Canada Workers Benefit	2.1 million	$2.005 billion	$3.63 billion
GST credit	10.5 million	$4.9 billion	$5.1 billion
Refundable medical expense supplement	545,000	$165 million	$165 million

The current Canada Child Benefit can be traced to the $200 tax exemption introduced in 1918 to reduce the tax payable by taxpayers with children, in recognition of the fact that having children reduced the amount of income available to pay tax.[44] It is also built on the family allowance program introduced in 1944 to help lower-income families.[45] "Tax fairness and social welfare were thus tightly tied together"[46] and tax system is used to provide social assistance. The Canada Child Benefit under section 122.6 of the Income Tax Act[47] currently provides a maximum amount of $6,833 per child under the age of 6 and $5,765 per child aged 6 through 17. The benefit is income-tested based on adjusted family net income with the benefit phase-out rate depending on the number of children.

The GST Credit under section 122.5 of the ITA provides income support to about 10.5 million individuals in the name of GST credit. This benefit is assessed by the CRA based on the information on the tax returns.[48] The Canada Workers Benefit under s.122.7 of the ITA provides income support to low-income workers as employees or self-employed. The rationale was to "reward and strengthen incentive to work" and "help people over the welfare wall … and achieve the dignity and independence that comes with a job".[49] It was promised to help lift "tens of thousands of workers out of poverty".[50] The refundable medical expense is a

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44 For further, see Ken Battle, "Child Benefit Reform: A Case Study in Tax-Transfer Integration" (1999) 47:5 *Canadian Tax Journal 1219-1257,* at 1222; Jinyan Li and Jacklyn Neborak,"Tax, Race and Child Poverty: Improving the Canada Child Benefit Program" (2018) 28:2 *Journal of Law and Social Policy 67-96;* R. Kesselman, "The Child Tax Benefit: Simple, Fair, Responsive?" (1993) 19:2 Canadian Public Policy 109-32.

45 Tillotson, *Give and Take*, supra note 14, at 175: "[I]n the face of tax resistance and protest, changes in the law were meant to build consent to the new level of personal income taxation, mainly among working-class and modestly paid middle-class Canadians. A similar purpose was served by the Family Allowances Act of 1944."

46 Tillotson, *Give and Take*, supra note 14, at 201: There are reasons to distinguish among methods of delivering social assistance, but in 1942-45, when these tax and welfare measures were being designed and first delivered, the tax dimension of the story indicates that personal income tax relief, inflation control, and social spending had common origins – the new ideology of social security. … The Liberals' tax program connected social security and stabilization policy, and their response to lower-income Canadians' tax resistance became an occasion to explain those connections.

47 Overall, the trend in the tax recognition of children is moving away from rewarding parents for their services of raising children or providing them with financial support toward investing in children on economic and social policy grounds.

48 For the 2021-2022 fiscal year, based on net family income reported for the 2020 taxation year, the amount of annual benefit is as follows: a basic adult credit of $299; a basic child credit of $157 for each child; and an additional credit of $157. The amount of benefit is reduced for individuals and families with annual incomes over $38,892.

49 House of Commons Debates, March 20, 2007, regarding the Working Income Tax Benefit (WITB), predecessor of Canada Workers Benefit, per Diane Albonczy (Conservative), John McCallum (Liberal), https://www.ourcommons.ca/DocumentViewer/en/39-1/house/sitting-124/hansard.

50 Remarks by Prime Minister Justin Trudeau in the House of Commons, 42nd Parliament, 1st Session, February 27, 2018 regarding Budget 2018 and proposing to replace the WITB with Canada Workers Benefit, see https://www.ourcommons.ca/DocumentViewer/en/42-1/house/sitting-268/hansard

refundable tax credit that provides low-income working Canadians with assistance for medical and disability-related expenses.

Canadian residence is required to qualify for the benefits. Canadian residence is also the basis for Canada to tax personal income on a global basis (i.e., income earned anywhere in the world to ascertain ability to pay tax in Canada).

2.1.5 Roles of Personal Income Tax

The personal income tax plays an important role in raising revenue and achieving distributive justice in Canada. In the 2019-2020 fiscal year, total federal revenues amounted to $334.1 billion, of which 68% were income taxes, and about 2/3 of income tax revenue came from personal income tax.[51] In the same year, total expenses amounted to $373.5 billion, about two-thirds of which were transfer payments, including funding income support programs administered by provinces and territories.

As a source of revenue, the personal income tax generated less than 10% of total federal revenues between 1917 to 1942, 10% to 30% between 1942 and the mid-1960s, and over 60% in recent years.[52] According to one study,[53] about 87% of the federal income tax is estimated to be paid by those earning $50,000 or more taxable income; individuals earning over $100,000 taxable income account for 8.4% of taxfilers but paid over 50% of total federal income tax; about one-third of all filers paid no federal income tax, many of whom received benefits.

Historically, the creation and growth of social income programs are tied to the expansion of the progressive income tax system.

> In addition to associating the new income taxes with paying for the war and inflation prevention, Ilsley [Minister of Finance] invoked social goods in the form of social security … – an ideal of connectedness in which individuals' self-interested actions were linked by macroeconomic mechanisms to social goods.[54]
>
> The transformation of the income tax during the war accompanied a peaceful revolution in popular thinking about the proper role of the state and became inextricably connected with the somewhat troubled birth of the modern Canadian welfare state.[55]

Since the 1940s, the income tax system has been engaged to raise the necessary revenue to pay for social spending, including the OAS/GIS as well as to directly provide income support through tax reliefs, such as family allowances (now Canada Child Benefit).

The personal income tax has always been progressive, although progressivity has varied over time. The marginal rate on taxable income exceeding $10,000 (but below $15,000) was 13.7% before WWI and 69%

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[51] Canada, Annual Financial Report of the Government of Canada Fiscal Year 2019-20, https://www.canada.ca/en/department-finance/services/publications/annual-financial-report/2020/report.html#revenues

[52] Livio Di Matteo, "Major Changes to the Federal Personal Income Tax: 1917-2017" in William Watson & Jason Clemens, eds, *Zero to 50 in 100 Years: The History and Development of Canada's Personal Income Tax* (Fraser Institute, 2017), at 11-16.

[53] See Jake Fuss and Tegan Hill, "Measuring Progressivity in Canada's Tax System" Fraser Research Bulletin, August 2021.

[54] Tillotson, supra note 14, at 198.

[55] Collins and Raizenne (book), supra note 12, at 235.

by 1942.[56] Since WWI, the tax became more democratic: while only 2.3% of the population filed income taxes in 1938, 24% did in 1955, and over 75% in 2017.[57] By the early 1970s the federal government had put into place a comprehensive framework of expenditure policies built on the robust economic growth after WWII and the belief that such growth would continue. "The role of the state as the provider of core public goods within a liberal market economy had shifted to one of government as a source of redistribution and social investment."[58] Since the 1972 tax reform, the marginal rate for the top bracket began to decline when the tax base became more universal (e.g., taxing capital gains): 60% in 1971 (exceeding $400,000); 47% in 1972 (exceeding $60,000); 34% in 1987 (exceeding $63,347), 29% in 1988 (exceeding $55,000) and bounced back to 33% in 2016 (exceeding $200,000).[59]

Studies show that taxes and government transfers (including those implemented through the income tax system) have helped to reduce income inequality in Canada, but at various degrees at different times.[60] Because the personal income tax is the sole progressive tax, it plays a critical role in reducing the after-tax income of the highest income group. Between the mid-1970s and the mid-1990s, after-tax income inequality did not increase, despite a significant rise in market income inequality and two major recessions. For example, in 1976, the first year for which data are available, the Gini index was 0.38 using market income. When government transfers and the effect of the tax system is included, the Gini index was 0.30 in 1976, 0.299 in 2019 and 0.281 in 2020.[61]

2.1.6 Underlying Values

The fiscal contract embedded in the taxing and spending choices reflects some important values. At a deeper level, one can say that equality, fairness and inclusion underlie the design of the spending programs. As a policy design matter, the requirement of Canadian residence is the linchpin between paying taxes and receiving benefits of tax expenditures or income support payments.

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56 Livio Di Matteo, *A Federal Fiscal History: Canada, 1867-2017* (Fraser Institute, 2017), at 35.
57 Ibid., at 48.
58 Ibid., at 47.
59 William Watson and Jason Clemens, eds., *Zero to 50 in 100 Years: The History and Development of Canada's Personal Income Tax* (Fraser Institute 2017).
60 See David A. Green, W. Craig Riddell and Frances St-Hilaire, "Income Inequality in Canada" Driving Forces, Outcomes and policy", https://irpp.org/research-studies/income-inequality-in-canada/; M. Frenette, D.A. Green and K. Milligan, "The Tale of the Tails: Canadian Income Inequality in the 1980s and 1990s" (2007) Canadian J. of Economics 40(3): 734-64; M. Frenette, D.A. Green and K. Milligan, "Taxes, Transfers and Canadian Income Inequality" (2009) Canadian public Policy 35:4, 389-411; A. Heisz and B. Murphy, The Role of Taxes and Transfers in Reducing Income Inequality", (2014), Ottawa: Income Statistics Division, Statistics Canada; J.R. Kesselman and R. Cheung, "Taxation Impacts on Inequality in Canada: Methodology and Findings," in D. Green and J. Kesselman, eds., Dimensions of Inequality in Canada (Vancouver: University of British Columbia Press, 2006).
61 Statistics Canada, "Canadian Income Survey, 2020". Since the mid-1990s, however, the redistributive impact of taxes and transfers fallen substantially and, therefore, after-tax family income inequality increased even more rapidly than market income inequality for a period of several years. For example, in 2009, the richest group had 24.6 times as much market income as those in the poorest group. After considering taxes and transfers, the richest group had 9.1 times as much income as the poorest group. This means that taxes and transfers are reducing income inequality, but not as much as before. In 1989, the richest group had 7.2 times more income after taxes and transfers than the poorest group. This increased to 9.1 times in 2009.

Fairness is the glue of a democratic society.[62] To achieve substantive fairness or equity, the ability to pay principle guides the design of progressive income tax. The Income Tax Act reflects the ability to pay principles by measuring income as broadly as possible to ascertain the economic capacity to pay tax as well as by applying progressive rates to higher amounts of income.[63] In order to protect the integrity of the progressive income tax, the Income Tax Act contains many rules to prevent individuals from using legal constructs (such as corporations or trusts) or arrangements (such as contracts) to defer or avoid tax. The ability to pay principle influences the design of tax-transfers and tax assistance measures. For example, the Disability Tax Credit and Disability Support Deduction recognize non-discretionary expenses that reduce a taxpayer's ability to pay. Childcare expense deduction and the Canada Child Benefit recognize non-discretionary expenses of raising children and the parent's ability to pay.

Work is the "basis for the economic survival of individuals and society".[64] Workers are the "bulk of Canadian citizens" and taxpayers. Workers bear the main burden of personal income tax. Disincentives for work is a main policy concern in designing the taxing rules as well as tax-transfer rules and the OAS/GIS system. Income from work became the most important base for personal income tax in the early 1940s when waged work became widespread in the industrializing Canadian economy and a pay-as-you-go withholding tax was imposed on wage earners. This tax was accepted as fair and legitimate means to finance the public goods and social transfers that workers sought from government. Income tax on workers remains crucial to financing social spending. In 2022, employment income and income from self-employment accounted for about 70% of total personal income for tax purposes.

Family is recognized as a unit by the Income Tax Act for some purposes, even though everyone is taxed as a unit. The Income Tax Act recognizes that family members support each other in finance and care. Examples are the Canada caregiver credit, caregiver credit, eligible dependant credit, spouse or common-law partner credit; transferrable medical expense tax credit, tuition tax credit, education tax credit, pension income credit and disability tax credit; pension income splitting; tax deduction for contribution to spousal RRSPs; and definition of principal residence by reference to inhabitation by dependent children and spouse or common-law partner.[65] Family income is used to test financial neediness. For example, the Canada Child Benefit is reduced when adjusted family net income reaches $32,028 (2021) and phased out when adjusted family net income exceeds $69,395 (2021).

The rule of law and certainty and predictability of tax rules are important. Taxpayers have the right to avoid tax by exploiting legislative ambiguities. The following statement in the *Duke of Westminster* (1936) case is regarded by the Supreme Court of Canada to be a "bed rock" of Canadian tax law: [66]

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[62] Richard M. Bird and J. Scott Wilkie, "Tax Policy Objectives" in Heather Kerr, Ken McKenzie and Jack Mintz, eds. *Tax Policy in* Canada (Toronto: Canadian Tax Foundation, 2012), ch.2 at 2:3. See also John Ralston Saul, *My Fair Country: Telling Truths about Canada* (Toronto, Viking Canada, 2008), at 303: "When Canadians are asked –as citizens, not as representatives of interest groups or as employees –what lies at the heart of their civilization, they are most likely to reply: fairness and inclusion."

[63] See Jinyan Li, Joanne Magee and Scott Wilkie, *Principles of Canadian Income Tax* Law (10th ed.) (Thomson Reuters, 2022), ch.2.

[64] Harvey J. Krahn, Graham s. Lowe and Karen D. Hughes, *Work, Industry & Canadian* Society (5th ed.) (Thomson & Nelson, 2007), at xxi.

[65] For a summary of each, see Canada, Tax Expenditures Report (2022), supra note 40.

[66] *Canada v. Alta Energy Luxembourg SARL* 2021 SCC 49.

> Every man is entitled if he can to order his affairs so as that the tax attaching under the appropriate Acts is less than it otherwise would be. If he succeeds in ordering them so as to secure this result, then, however unappreciative the Commissioners of Inland Revenue or his fellow taxpayers may be of his ingenuity, he cannot be compelled to pay an increased tax.[67]

This right has been extended to taking advantage of tax subsidies and other benefits available under the Income Tax Act.[68] To ensure fairness for all Canadians, the Income Tax Act has been drafted in specific and air-tight language, which is protected by specific and general anti-avoidance rules.[69]

The rule of law requires an independent judiciary to interpret and apply the law. To achieve fairness and neutrality among taxpayers, the more observable and demonstrable evidence the better. Canadian courts have made it clear that in tax cases, taxpayers' motivations or morality considerations are not relevant; what matters is what Parliament says through legislation. As such, even though many provisions of the Income Tax Act reflect moral values, judges limit their interpretation of the provisions to the extent of the words used by Parliament, albeit interpreted textually, contextually and purposively.

The administrative dimension often dictates policy design choices. "Tax administration *is* tax policy"; "How to do it" is as, if not more, important as "what to do".[70] All underlying values, aspirations and policy objectives must be reduced to legislative text that can be administered fairly and cost-effectively. Tax administration relies on the application of general law (e.g., family law or property law), certification by third parties (e.g., medical practitioners regarding disability and employers regarding employee expenses) and a system of reporting, verification and control. The Income Tax Act seeks to connect everything to an objective accounting number and uses that number to determine the transfer of money to or from the government. Not everything can be connected to an amount of money and many social and economic ills cannot be cured by money. Some democratic values are not reducible to dollars.[71]

2.2 CHINA

2.2.1 History

The Chinese individual income tax (IIT) was first introduced in 1980 at the inception of China's economic reform and open to the world policy.[72] Until then, private ownership of property, free enterprising and freedom of contract were not allowed and individuals earned income from work and the amount of wages was regulated. In a command (or centrally planned) economy, there was no need for using income tax to raise revenue or redistribute income. The new tax was meant to apply mainly to foreigners working in China.

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[67] *IRC v. Duke of Westminster* [1936] 19 TC 490.
[68] See, e.g., *Canada Trustco Mortgage Co. v. Canada*, 2005 SCC 54, and *Canada v. Alta Energy Luxembourg S.A.R.L.*, 2021 SCC 49.
[69] See Li, Magee and Wilkie, supra note 63, at 570-94.
[70] Richard Bird, "Administrative Constraints on Tax Policy" in Cedric Sandford, ed. *Further Key Issues in Tax Reform* (Bath, Fiscal Publications, 1998), 183-99, at 184.
[71] Linda Sugin, "Invisible Taxpayers", (2016) 69 Tax L. Rev. 617, at 651.
[72] Individual Income Tax Law of the People's Republic of China [中华人民共和国个人所得税法] 1980 (amended 1993, 1999, 2005, 2007, 2011, 2018) (hereinafter referred to as "IIT Law"); CN: 中华人民共和国个人所得税法实施条例 [Detailed Rules and Regulations for the Implementation of the Individual Income Tax Law of the People's Republic of China] 1980 (amended 1994, 2005, 2011) (hereinafter referred to as "IIT Regulations").

The monthly tax deduction of CNY 800 was more than 13 times the average wage of Chinese workers.[73] Its primary purposes were to exercise taxing jurisdiction over foreigners, deal with nation-to-nation tax relations and encourage foreigners to work in China.[74] The IIT followed a schedular system and only taxed wages and salaries at progressive rates. Tax was collected through withholding at source and there was no requirement of self-assessment. The IIT legislation was brief. The IIT Law contained 15 articles, written in 1,265 words: The last two articles were authorizing the government to introduce implementation rules and date of the law taking effect.[75]

By the mid-1980s, some Chinese citizens had been granted the freedom to pursuit economic activities for profit and were earning significant incomes from operating private businesses and other entrepreneurial activities. There was an increasing income gap between their income and that of ordinary wage earners. To reduce the gap, the government introduced special taxes applicable only to Chinese citizens – the Individual Income Regulatory Tax (1986)[76] and the Private Investors Individual Income Regulatory Tax (1988).[77] Under those two taxes, a monthly deduction of CNY 400 – about four times the average wage at the time – was allowed, and the excessive amount was taxable at progressive rates ranging from 20% to 60%. In 1986, the government also introduced a special tax on private industrial and commercial households at progressive rates (7% to 60%).[78] A surtax of 10% to 40% was imposed on taxable income exceeding CNY 50,000. In the meantime, the CNY 800 monthly deduction was found vastly inadequate for foreigners and an additional deduction of CNY 3,200 was allowed. As such, the monthly deduction was CNY 4,000 for foreigners and CNY 800 for Chinese.

In 1993, the Individual Income Regulatory Tax and the Private Investors Individual Income Regulatory Tax were consolidated with the existing IIT. Other than the broadening of the tax base by adding business income and contractual and management fees, no other major changes were made to the 1980 IIT legislation. Between 1999 and 2017, the IIT was amended several times, mostly to raise the standard monthly deduction of CNY 800 for Chinese individuals to reflect the increase in the cost of living in urban areas: CNY 1,600 in 2005, CNY 2,000 in 2008, and CNY 3,500 in 2011.

A significant reform took place in 2018. There had been tremendous economic and social changes in China. China's GDP had been rising spectacularly for over three decades. China's national income and individual income also increased. For example, China's GDP was USD306.17 billions in 1980 and USD12,323

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[73] Jinyan Li, International Taxation in China: A Contextualized Analysis (Amsterdam: IBFD 2016), at 589. For further, see Yue Daisy Dai, "China's 2018 Individual Income Tax Reform: A Global Perspective" *Tax Notes Int'l,* May 27, 2019, 849, at 849.

[74] China International Tax Research Institute, Accompanying Reform and Open To the World: 40-year History of Chinese International Taxation (与改革开放同行：中国国家税收 40 年) (Beijing: China Tax Press, 2020）, at 12-13 ("40-Year History").

[75] The IIT implementation rules are more detailed,

[76] Provisional Rules of the People's Republic of China on Individual Income Adjustment Tax] 1986 [中华人民共和国个人收入调节税暂行条例施行细则] (invalid 1997).

[77] State Council Regulations Concerning the Levying of Individual Income Regulatory Tax on Investment Income from Private Enterprises [国务院关于征收私营企业投资者个人收入调节税的规定] 1988 (invalid 1999).

[78] Interim Regulations of the People's Republic of China Concerning Income Tax on Individually Operated Industrial and Commercial Households [中华人民共和国城乡个体工商户所得税暂行条例] 1986 (invalid 1994).

billions in 2017; GDP per capita was USD 312 in 1980 and USD 8,826 in 2017.[79] The IIT (2018) replaced the schedular system with a partial integrated system by combining wages, salaries, personal services, author royalties and general royalties into one category, taxable at progressive rates. It also raised the basic exemption threshold from CNY 3,500 monthly to CNY 60,000 annually, introduced itemized deductions, adopted a general self assessment system, and added a GAAR. The main goals of this 2018 reform were to "modernize" the IIT, address some social concerns about rising cost of education, health care and housing, and increase the degree of taxation by legislation through adding more detailed substantive rules in the IIT Law.[80]

Further reforms are being discussed to broaden the tax base by adding more items of income to the combined income category to reduce the disparity between taxation of income from labour and income from capital or capital gains.[81] Such changes would aid the government's goal of achieving "common prosperity".[82]

2.2.2 Policy Objectives

The policy objectives of the IIT were initially oriented towards promoting economic development and reoriented towards equity gradually. Administrative convenience remains a constant objective.

In 1980, the Deputy Chair of the Legislative Committee of the Standing Committee of the National People's Congress explained that the IIT was necessary to "maintain our country's economic interest" and the law was drafted to "follow the principle of mutual benefits, take into consideration of domestic realistic circumstances, and make reference to foreign norms and practices".[83] It was not introduced to serve any specific political purpose or to achieving a sense of equity or fairness that is commonly associated with progressive income taxation. The main objective in 1980 was to help project an image that China was striving to create a legal system that is familiar to foreign investors by having the new income tax enacted by the National People's Congress and drafting the IIT Law based on high-level international norms (see

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[79] See China NBS National data, "National data - annual - national accounts - Gross Domestic Product" *(Press release). China NBS. March 2021*. Retrieved October 29, 2021.

[80] For further overview of the 2018 reform, see Asian Development Bank, "Reforming the Personal Income Tax System in the People's Republic of China" (Manila, Philippines, ADB, 2020) ("ADB Report")

[81] ADB Report, ibid, at 3-4.

[82] Chinese President Xi Jinping first introduced the concept of common prosperity at the 10th meeting of the Central Committee for Financial and Economic Affairs in August 2021. At the meeting, Xi related common prosperity to raising the incomes of low-income groups, promoting fairness, making regional development more balanced, and stressing people-centered growth. This included a pledge to "reasonably regulate excessively high incomes, and encourage high-income people and enterprises to return more to society." See Huang Panyue, "Xi urges financial risk prevention while seeking high-quality growth" CGTN News, Aug.17, 2021 (http://eng.mod.gov.cn/xb/News_213114/TopStories/4892182.html); Xin Sun, "Decoding China's "Common Prosperity" Drive, LSE !deas, April 2022 (https://www.lse.ac.uk/ideas/Assets/Documents/updates/LSEIdeas-Decoding-Chinas-Common-Prosperity-Drive.pdf); China Daily, Oct.20, 2022, "China Striving to Achieve Common Prosperity", https://www.chinadaily.com.cn/a/202210/20/WS63508281a310fd2b29e7d710.html.

[83] Gu, Ming, Deputy Chair of Legislative Committee of the Standing Committee of the National People's Congress, "Explanation about the Draft Law of the People's Republic of China on China-Foreign Equity Joint Venture Enterprise Income Tax and the Draft Law of the People's Republic of China on Individual Income Tax", 1980) available in Chinese at http://www.law-lib.com/law/law_view.asp?id=95054 (hereinafter "IIT Law Explanation") [全国人民代表大会常务委员会法制委员会副主任 顾明, 关于《中华人民共和国中外合资经营企业所得税法（草案）》和《中华人民共和国个人所得税法（草案）》的说明]

below). The IIT also served a revenue purpose: if China did not tax the income of foreigners working in China, the income would have been taxed in the home countries; and if China collected taxes on the income, the Chinese tax would be credited against the home country tax. Having the IIT would not discourage foreigners from working in China.

Regulating individual income became a more important objective when more and more Chinese people became "rich". For example, the 1993 reform was guided by the following thinking: "to have fair sharing of the tax burden, to strengthen the revenue function and the function of adjusting individual income, to maintain state interest, to enhance citizens' taxpaying awareness, and make the individual income tax system better serve the purpose of economic development and reform and open policies."[84] Pivoting towards social-oriented objectives became more evident in the 2018 reform when itemized deductions were introduced to address wide-spread social concerns. In recent years, there are more calls for using the IIT to adjust individual income to achieve "social fairness and justice" and promoting "common prosperity."[85]

Administrative efficiency has been a constant objective. In the earlier years, there was reliance on source withholding, standardized deductions and the schedular system. Recently, the wide-spread use of electronic filing and tax payment helped tax compliance and speedy processing of tax refund.[86]

2.2.3 The Taxing System

Drafters of the 1980 IIT Law considered best foreign practices and Chinese circumstances and adopted an interesting combination of design features. As to the basis of claiming tax jurisdiction, an individual's domicile and length of physical stay in China as well as Chinese source of income were the basis for charging the tax.

"Domicile" refers to habitual abode or permanent place of residence. Individuals are deemed to be domiciled in China if they habitually live in China because of household registration, family, or economic interests.[87] Chinese citizens living in China are generally required by law to maintain a household registration in China and are therefore domiciled in China by reason of the place of household registration. Chinese citizens who live permanently outside China do not have a domicile in China as they do not habitually reside in China.[88] Non-Chinese citizens may be considered domiciled in China if they make

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[84] Jin, Xin, "Introduction of the Amendment of the Individual Income Tax Law", November 18, 1993 (金鑫，"关于个人所得税法修改情况的介绍") in Collection of Tax Essays by Jin Xin, Vol.2 (金鑫税收论文选，下卷) (Beijing: China Tax Press, 2008), at 818

[85] Han, Jin, Qingxia Zhao, and Mengnan Zhang. "China's income inequality in the global context." *Perspectives in Science* 7 (2016): 24-29; Sonali Jain-Chandra, et al, "Inequality in China – Trends, Drivers and Policy Remedies", IMF Working Paper, WP/18/127; Thomas Piketty and Nancy Qian, "Income Inequality and Progressive Income Taxation in China and India, 1986-2015" in A.B. Atkinson and T. Piketty, eds. *Top Incomes: A Global* Perspective (Oxford: Oxford University Press, 2010), 40-75.

[86] China International Tax Research Institute, Subject Study Team, "International Comparison of the Chinese Individual Income Tax Annual Settlement) (中国国际税收研究会课题组,《中国个人所得税年度汇算的国际比较研究》(2021), http://www.chinatax.gov.cn/chinatax/n810219/n810724/c5171576/content.html

[87] IIT Regulations, article 2.

[88] This depends on whether the person "habitually resides" in China. See Guoshuifa [1994] no.089, Circular of the State Taxation Administration on Issuing the Regulations on Some Issues Concerning the Levy of Individual Income Tax] [国税发[1994]089 号, 国家税务总局关于印发《征收个人所得税若干问题的规定》的通知] (partially invalid). The term "habitually resides" in China is considered in this circular. The criteria for determining whether a person habitually resides in China are registration with the foreign police bureau, family relationships, and economic ties with China.

China their permanent home (it is rare for a foreigner to obtain permanent resident status in China). In 2018, "domicile" was replaced with "residence" as a jurisdictional base, but "resident individual" is defined to be an individual who is domiciled in China or who is not domiciled in China but has stayed in the aggregate for 183 days or more in China.[89] The meaning of domicile remains unchanged.

The tax base is schedular in general, although moving towards a comprehensive system. The IIT Law 1980 imposed tax on six categories of taxable income: wages and salaries; labour services income; royalties for the license of proprietary rights; interest, dividend and bonus dividend income; rent or leasing income; other items to be specified to be taxable by the Ministry of Finance. Only wage and salary income was taxed on a monthly basis at progressive rates, ranging from 5 to 45 percent. Other categories of income were taxed at a flat rate of 20%. Standard deductions were allowed for wages and salaries (CNY 800) and labour service income, royalties, rent and leasing income on a per payment basis (20% of the payment exceeding CNY4000 or CNY800 per payment). Taxes were collected by way of source withholding.

Under the IIT Law 2018, four categories of income become aggregated and taxed at progressive rates (3 to 45 percent on amount exceeding the annual threshold of CNY 60,000): wages and salaries, labour service income, authors' royalties and other royalties. Business income was subject to tax at progressive rates (5 to 35 percent). Rent, leasing income, gains from transfer of property (or capital gains) and incidental income remain taxable separately, on a transactional basis, at the flat rate of 20 percent. The scope of deductions varies: a standardized monthly deduction of CNY5000 for wages and salaries; no deduction for labour service income, author's royalties and royalties, interest, dividend, bonus dividend and incidental income; costs and expenses for business income; 20% deduction for rent and leasing income; and original cost and related reasonable expenses for capital gains.[90]

Income from work (employment, self-employment or unincorporated business) is taxed at progressive rates, while income from capital and capital gains are taxed at flat rate. This is closer to the dual tax system in some European countries.

Resident individuals are required under IIT Law 2018 to file tax returns and self-assess tax liabilities and pay the amount of tax owed. Chinese citizens must use the Citizen Identity Number in filing returns; other residents must obtain an identity number from the tax administration. Since most items of taxable income are subject to source withholding, the annual tax filing is largely a reconciliation exercise for taxpayers.

The electronic filing and processing of tax returns make the tax compliance and administration process largely automatic and administrative. There is little case law on the interpretation of IIT legislation. Having a dispute with the tax authority is like throwing an egg at the rock, largely because the tax administration enjoys broad powers to interpret tax legislation and deference from the judges. The judiciary plays no meaning role in the tax system.[91]

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[89] IIT Law, article 1.

[90] IIT Law, article 6.

[91] Wei Cui, "Foreign Administrative Law and International Taxation: A Case Study of Tax Treaty Implementation in China" (2012) 64:1 Admin L Rev 191; Jingyi Wang (2018) Tax administration in China: is it rule without law?, Asia Pacific Law Review, 26:2, 203-227, DOI: 10.1080/10192557.2019.1576293; Ji Li, *Dare You Sue the Tax Collector? An Empirical Study of Administrative Lawsuits Against Tax Agencies in China*, (2014) 23 PAC. RIM L & POL'Y J. 57.

2.2.4 Tax Expenditures

The IIT Law 1980 and IIT Law 2018 exempt some items of payments from taxation, such as awards for achievement in science, technology or culture; interest on state bonds or treasury bills; welfare or special relief payments; insurance proceeds, retirement fees. The 2018 reform introduced special deductions for charitable donations (up to 30% of the individual's total taxable income); contributions to the basic pension insurance, basic medical insurance, unemployment insurance, and other social insurance and housing provident funds; expenditures for education of children or continuing education; medical treatment of serious diseases; housing loan interest, housing rents; support for elderly parents. The specific scopes, standards and implementation procedures shall be determined by the State Council and filed with the Standing Committee of the National People's Congress.[92]

According to measures introduced by the State Council, the deductible amount is CNY 1,000 per child per month for child education; CNY 400 per month for continued education; CNY 1,000 per month for housing mortgage interest; CNY 800, 1,100 or 1,500 per month for rental expense, depending on the location; up to CNY 2,000 per month for elderly care, depending on the status of the taxpayer (e.g. whether the taxpayer is the sole child or not); qualified self-paid portion above CNY 15,000 of major medical expenses (but capped at CNY 80,000 per year per eligible individual; and CNY 1,000 per child per month for care expense for children under the age of 3.

There are no tax credits, refundable or otherwise, available. Individuals who have insufficient taxable income do not benefit from these special deductions. The IIT is not used to implement income-support programs. There is no annual reporting of tax expenditures. In fact, the topic of tax expenditures is not studied much.[93]

2.2.5 Roles of Personal Income Tax

The two main roles of the IIT are raising revenue and adjusting individual incomes. The following table provides an overview of key indicators in selected years.

Table 3: Selected data on IIT revenue and China's GINI index[94]

[92] IIT Law 2018, art.6. China State Council, Interim Measures on Special Deductions under the Individual Income Tax, Guofa [2018] Number 41, December 13, 2018.

[93] Zhang Zhiyong, "A Discussion of Our Country's Tax Expenditure Budgeting and Legal Rules" (2012) 7 Politics and Law [张智勇, "论我国对税式支出的预算法律规制"] 《政治与法律》2012 年第 7 期 (https://www.aisixiang.com/data/57725.html)

[94] Sources: The threshold data was from the IIT legislation. Data on the amount of IIT revenue and ratio of IIT/total tax revenues are based on Jingyi Wang and Wilson Chow, "Individual Income Taxation Reform in China: What is the Real Change?" (https://ssrn.com/abstract=3442731); https://data.stats.gov.cn/easyquery.htm?cn=C01; Xu, Hua and Huiyu Cui. "Personal Income Tax Policy in China and the United States: A Comparative Analysis." *Public Administration Review,* 1, 2009, 75-81; Liu, Jianwen and Xiang Hu. "Evaluation of the Revisionary Evolution of the Individual Income Tax Law and Our Contemporary Approach." *China Law,* 5, 2018, 124-145. Data on Gini index was based on: Federal Reserve Bank of St. Louis, SIPOVGINICHN, GINI Index for China, Index, Annual, Not Seasonally Adjusted Frequency: Annual Gini index: world bank https://data.worldbank.org/indicator/SI.POV.GINI?locations=CN

Year	Threshold for progressive taxation (CNY) (monthly)	IIT revenue (CNY billion)	IIT/total tax revenue	Gini index in China
1980	800	n/a	n/a	n/a
1986	800 for foreigners; 400 for Chinese			
1994	800	7.267	1.42%	n/a
1999	1,000	41.366	3.87%	0.387
2002	1,000	141.803	7.08%	0.42
2005	1,600	209.491	7.28%	0.409
2008	2,000	372.231	6.86%	0.430
2011	3,500	605.411	6.75%	0.424
2018	5,000	1,833.598	7.57%	0.385

Revenue from the IIT steadily increased from CNY 7.267 billion in 1994 to 1,833 billion in 2018, accounting for an increasing share of the total tax revenues (less than 1% before the 1990s to over 7.57% in 2018. Meanwhile, China's GDP per capita increased at greater speed: rising from USD 195 in 1980 to USD 12,556 in 2021.[95]

The role of the IIT in reducing income inequality is difficult to ascertain, although it is reasonable to assume that it is rather limited, although not insignificant. There is no study on the effect of the IIT on the Gini index. Until the early 1990s, China's income distribution was much more equal than that of other emerging economies. As the result of more than two decades of rapid economic growth in China, while millions have been lifted out of poverty, income inequality increased substantially.[96] The revenue ratio is growing but remains limited to render the IIT a meaningful instrument of redistributing social income. The technical design of the system, such as schedular, flat rate taxation of income from capital and capital gains, de-linking with the taxation of corporations and the existence of "grey income" make it difficult for the IIT to

[95] World bank. https://data.worldbank.org/indicator/NY.GDP.PCAP.CD?locations=CN. The OECD average was 23.5% as a share of tax revenue, including social security contributions, or 8.1% of GDP in 2018: OECD, Revenue Statistics 1965-2019, (Paris: OECD 2020).

[96] Sonali Jain-Chandra et al, "Inequality in China – Trends, Drivers and Policy Remedies", IFM Working Paper, WP/18/127, June 2018, https://www.imf.org/-/media/Files/Publications/WP/2018/wp18127.ashx ("IMF Working Paper"). See also Jinyan Li, "Development and Tax Policy: Case Study of China" *Comparative Research in Law & Political Economy. Research Paper No. 27/2007.* https://digitalcommons.osgoode.yorku.ca/clpe/243

tax the top 1 or 10% of high-income individuals who do not rely on wages or salaries as their source of income.[97] Poor tax compliance is another explanation:

> Besides weak legal and institutional tax enforcement, reasons for low compliance include the lack of a unified and national taxpayer database, which limits information sharing and matching and targeted tax auditing. To tackle these shortcomings, the enforcement of tax laws must be improved to strengthen compliance.[98]

The IIT is not integrated to the enterprise income tax. Unlike the Canadian system, the enterprise income tax does not function as an advance tax on individual shareholders. In fact, owing to the legacy of centrally-planned economy and state-ownership of enterprises and the fact that many enterprises were invested by foreign corporations, the enterprise income tax system is a standalone system.

2.2.6 Underlying Values

It is difficult to discern any social or fiscal contract that underlies the IIT. The IIT was not created to raise revenue or redistribute income to achieve an acceptable notion of fairness. In contrast, it was introduced as a pragmatic measure as part of China's open-door economic policy to share the taxing rights with foreign countries over Chinese-source income earned by foreigners and to signal to foreign investors that China was moving towards a tax and legal system familiar to them. Even though subsequent reforms made the IIT more responsive to domestic social issues, the IIT remains, in essence, an instrument of economic policy.

As mentioned above, the IIT was not designed to reflect the ability to pay principle or achieve tax equity (both in a vertical or horizontal sense). Progressive taxation applied only to employment income, which renders the system regressive, especially in recent years of growing income inequality. Considering the primary objective of maximizing investment and economic growth, not taxing income from capital at progressive rates is consistent with that objective. However, Chinese culture and the communist or socialist ideology do not favour the "underserving rich", such as those "instant" millionaires, pop stars or internet celebrities. When the IIT legislation does not address the popular resentment of the undeserving rich, such as pop or movies stars and instant Internet celebrities, the tax authorities resorted to tax evasion charges to confiscate their income.[99] Under the "common prosperity" campaign, the super-rich were encouraged to donate their wealth for public good – referred to as the "third distribution" following the original distribution of income through the market mechanism and redistribution through the tax system.

The IIT values work and contributions to society through exempting income arising from awards for scientific, technological or cultural achievements and retirement from military forces or public offices. It recognizes the importance of family through the special itemized deductions introduced in 2018. In an

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[97] Dominik Peschel, "Reducing Inequality in the People's Republic of China through Tax and Fiscal Reforms", December 2021, Asian Development Bank; United Nations Development Programme, Issue Brief, "China: Tax Policies and Income Inequality" (2016), https://www.undp.org/china/publications/china-tax-policies-and-income-inequality.

[98] Peschel, ibid., at 22. See also Lustig, N., and Y. Wang, "The Impact of Taxes and Transfers on Income Inequality, Poverty, and the Urban–Rural and Regional Income Gaps in China" 2020 Working Paper, Washington DC: Center for Global Development.

[99] E.g., William Hoke, "Chinese Actress Accused of Tax Evasion Is Fined $46 Million", *Tax Notes Int'l* (vol.103, Sept. 6, 2021) 1364-5; William Hoke, "Chinese Celebrities Draw Tax Office Scrutiny," *Tax Notes Int'l* (vol.103, Sept. 27, 2021) 1751; William Hoke, "China Tells Internet Platforms to Report Liverstreamers' Profits", *Tax Notes Int'l* (vol.106, April 4, 2022) 114.

ironic way, though, the need for these deductions arose from the lack of universal public health, education and social insurance programs and people had to pay for health care, child care and senior care.

It is difficult to say if the IIT reflects any value of democratic participation in policy-making. There has been no comprehensive study of the IIT by an independent commission in China that involved broad consultations with the public. The government provided more and more opportunities for the public to comment on draft legislation in the recent years and most comments were directed at the basic exemption threshold. There is a disconnect between taxpayers and law-makers in the sense that the IIT revenue belongs to local government, but the IIT legislation is made at the national level and there is no direct election of members of the National People's Congress.[100]

Taxpayers' right to tax avoidance is implicitly acknowledged by the introduction of the GAAR. In practice, the line between tax avoidance and tax evasion is very blurry as a result of generally-worded statutory provisions, broad interpretation powers of the tax administration and lack of judicial oversight.

3. CITIZENSHIP AS THE MAIN LINCHPIN

As an economic, social and political instrument, the Canadian ITA and the Chinese IIT implicitly use citizenship as a linchpin to connect the three spheres. This is more evident in Canada where individuals are economic actors, paying tax on their income according to the law passed by their elected representatives and enjoying the benefits of public spending through tax expenditures or transfers. This linchpin is considered in terms of defining the economic and taxing community, fiscal community and political community.

3.1 The Boundary of the Tax Community

Citizenship is not a basis for imposing tax under either the Canadian ITA or the Chinese IIT as it would make no sense as a technical design matter in the historical context. Canadian citizenship was created by the Canadian Citizenship Act, 1946, taking effect on January 1, 1947.[101] The Chinese IIT was introduced in 1980 to tax foreigners.

Residence continues to be the main jurisdictional threshold as it makes sense in terms of capturing the broadest base possible in a manner that reflects the benefit principle and international norm. Canadian citizens living in the country are tax residents, and those living abroad may be tax residents if they maintain some residential ties with Canada. According to the 2021 Census, of the total population (38.25 million) living in Canada, 91.2% were Canadian citizens, and most non-citizens were either permanent resident or non-permanent residents.[102] Approximately 3 million Canadian citizens live abroad, and two-thirds of them were in the United States.[103] There has been no policy debates in Canada about taxing non-resident citizens. Under the typical tie-breaker rules for individuals, these Canadians are mostly likely treated as residents of the other treaty country in any event.

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[100] See heading "Type of Elections" below.

[101] Before January 1, 1947 when the Canadian Citizenship Act, took effect, a person born or naturalized in Canada was considered a British subject.

[102] https://www12.statcan.gc.ca/census-recensement/2021/as-sa/98-200-X/2021008/98-200-X2021008-eng.cfm

[103] Statistics Canada, "The Canadian diaspora: Estimating the number of Canadian citizens who live abroad", https://www150.statcan.gc.ca/n1/daily-quotidien/220413/dq220413b-eng.htm

Chinese nationals living in China are tax residents. Chinese Nationality Law prohibits dual nationality.[104] Chinese nationals who have emigrated to other countries and have dual citizenships continue to have Chinese passports for ease of entry into China, and are thus likely treated as tax residents.[105] China is reportedly the 4th largest source country for immigration, over 9 million mainland Chinese living abroad.[106] About one million non-Chinese citizens live in Mainland China, accounting for less than 0.07% of the total population, which is one of the lowest ratio in the world (lower than tat in Vietnam, Cuba, and North Korea.[107] As such, citizens and tax residents are almost identical in China.

3.2 The Fiscal Community and Sharing

As members of the fiscal community, individuals share the tax burden and benefit from public spending, including welfare. In Canada, eligibility for tax benefits and transfers is based on Canadian residence. As mentioned above, even though Canadian citizens can opt out of this community by living abroad, the same is true for non-citizens. As a result, members of the fiscal community are mostly citizens. In China, on the other hand, tax benefits and social welfare transfers are available only to citizens.

In Canada, the sharing of the tax burden is based on the ability to pay principle. The progressive personal income tax provides "the most important counterweight to regressive elements in the rest of the tax system and in market-determined pretax incomes."[108] Although other factors influence the level of progressivity (such as tax competition (especially with the United States), concerns about possible adverse effect on risk-taking and work incentives and avoidance responses to top tax rates influence how high can the top rate go or how capital income and capital gains are taxed), the progressivity of the income tax is influenced by public opinion and voters' support. Canadians' views of the tax system have been largely contingent on perceptions of equity and fairness: that those less well-off than themselves should pay lower taxes, that their own taxes should increase only a little or not at all, and that those better off than themselves, especially large corporations, should pay more."[109] Reflecting the perceived self-interest of a large majority of taxpayers/voters, the government (whether led by the Liberals or Conservatives) is reluctant to reduce tax rates for upper-income earners. A liberal government tends to raise the tax rate and close "loopholes",[110] while a conservative government tends to increase tax expenditures that benefit upper-middle income

[104] Nationality Law of the People's Republic of China, (Adopted at the Third Session of the Fifth National People's Congress, promulgated by Order No.8 of the Chairman of the Standing Committee of the National People's Congress on and effective as of September 10, 1980) (https://cn.ambafrance.org/IMG/pdf/loi_nationalite_chine.pdf)

[105] See Jisen Zhang, "Interpreting "Settled Abroad" in China's Nationality Law: Theory, Practice, and Problems", (2022) Columbia J. of Asian L. 268-319; "China – Information on Residency for Tax Purposes" https://www.oecd.org/tax/automatic-exchange/crs-implementation-and-assistance/tax-residency/China-Residency.pdf

[106] Centre for China and Globalization, "China International Immigration Report, 2018, at 3. The first three source countries are India, Mexico and Russia. The top five countries receiving Chinese immigrants are: the United States, Canada, Japan, Australia and Singapore.

[107] China International Immigration Report, 2018, ibid., at 30.

[108] Kevin Milligan, "The Future of the Progressive Personal Income Tax: How High Can It Go?" (2019) 67:3, Canadian Tax J., 693-710, at 694.

[109] Hale, supra note 19, at 127.

[110] For example, the current liberal government introduced a new 33% top rate bracket for taxable income over $200,000 in 2015 and the 2023 Budget proposes to raise the alternative minimum tax rate from 15% to 20.5% and to implement Pillar One and Pillar Two to ensure large multinational enterprises pay their fair share of taxes. Budget 2023, "A Fair Tax System".

groups (such as tax shelters for savings). In general, the progressivity of the tax system is affected by public expectations and public opinion. Canadians expect the governments to promote economic growth and raise the standard of living for most social and economic groups.

In China, the IIT has limited progressivity because of the schedular design and flat rate of taxation of income from capital. The IIT is not a meaningful counterweight to regressive consumption taxes or pre-tax economic incomes. It is also not integrated with a flat rate enterprise income tax. The trade-offs between economic growth and equity are not shaped by public opinion.

3.3 The Political Community and the Give-And-Take

Members of the political community are based on citizenship in both Canada and China. The political process dictates the nature of give-and-take or bargaining among members of the community. In Canada, there are different political parties representing the interests of members and tax preferences tend to draw the line between the parties.[111] In China, the Communist Party is the sole governing party.

In Canada, the give-and-take consideration matters for individual taxpayers, interest groups and political parties. Who gives and who takes, how much shape voters' views about tax policy changes. Political parties define themselves by their stance on tax issues.[112] The tax system is a "mirror of democracy" and "nothing shows so clearly the character of a society and of a civilization as does the fiscal policy that its political sector adopts."[113] Through elections, voters as taxpayers express their preferences. To win the support of the majority, tax expenditures and transfers are offered as part of the give-and-take. The history of Canadian taxation shows a close link between the taxing (the give) and spending (the take) sides of the tax system. For example, the expansion of the personal income tax in the 1940s was linked to the introduction of tax expenditures to help families. When capital gains became taxable in 1972, an exemption was introduced to exclude all capital gains from the sale of a family home from tax. When it is not politically feasible to lower the top tax rate for high-income taxpayers, tax expenditures that benefit traditional families (e.g., child fitness credit, child art credit), savings (e.g., tax-free savings account), or senior high-income men (pension income splitting) were introduced by the conservative government. Studies show that many tax expenditures reduce the progressivity of the personal tax system.[114] In fact, the government's success in promoting social and economic objectives is achieved through spending and transfer programs embedded in the income tax system.

The give-and-take dynamic has no equivalent in China. At the inception of the IIT, taxpayers were primarily foreigners who had no membership in the political community. The personal tax expenditures were available to citizens. The IIT has relatively fewer tax expenditures in any event. The IIT is not a meaningful instrument for redistribution or social spending.

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[111] David Tough, "Broadening the Political Constituency of Tax Reform: The Visual Rhetoric of Canadian Taxation, 1919-81" (2012) 46(1) J. of Canadian Studies, 193-212; David A. Wolfe, "Politics, The Deficit and Tax Reform" (1988) 26(2) Osgoode Hall L. J. 347-366.
[112] Neil Brooks, supra note 1, at 353.
[113] Joseph Schumpeter was quoted in Neil Brooks, ibid., at 354.
[114] Brian Murphy et al, "Top-End Progressivity and Federal Tax Preferences in Canada: Estimates from Personal Income Tax Data," (2015) 63(3) *Canadian Tax J.* 661-88.

4. Democracy and Tax Policy Making

4.1 "Tax Law is Shot through Politics"[115]

In Canada, tax issues are prominent in election campaigns and media coverage. "Taxation sits at the nexus of politics and the economy."[116] Canadian citizens elect members of Parliament and the party that wins the majority of seats form government. The Prime Minister and members of the Cabinet are members of Parliament. As such, through the election process, citizens as voters and taxpayers participate in making the tradeoffs. Appealing to most voters is thus important.[117] The wide-spread use of tax expenditures in Canada is a double-edged sword. On one hand, it allows federal political executives (e.g., members of cabinet) to use tax expenditures to deliver visible and popular policy outcomes to the public with minimal interference from other political parties or governmental actors (including provincial-level government).[118] On the other hand, the cost and impact of tax expenditures are "hidden" from voters, and many costly tax expenditures benefit higher-income groups.

In China, the ruling party does not need to seek citizens' support for its fiscal policies. The Central Government does not need to use tax expenditures in the way the Canadian government does. Managing the tax system is part of the macro-economic system, targeting economic development.

4.2 Type of Elections

In Canada, voters elect members of the House of Commons, which is the most important part of Parliament. The other two parts are the king, represented by the governor general and the Senate (senators are not elected). The Prime Minister and Cabinet sit in the House of Commons. The House of Commons votes on the passage of laws and ensures the Government is held accountable. The rule of law is a cornerstone of Canadian democracy. The judiciary is independent of Parliament. Judges are appointed. The Supreme Court of Canada is the final court. Tax Court of Canada is part of the federal court system, and its decisions can be appealed to the Federal Court of Appeal.

In China, citizens participate in electing the basic (county or district) level of legislatures (people's congress), but not members of the National People's Congress that has the power to enact tax laws. National law makers are elected by provincial lawmakers who are elected, in turn, by municipal level lawmakers.[119]

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115 Brooks, supra note 1.

116 Jeremy Bearer-Friend, et al, "Taxation and Law and Political Economy" (2022) 83(3) *Ohio State L. Rev.* 472-527, at 505). See also Walter J. Blum and Harry Kalven, Jr., "The Uneasy Case for Progressive Taxation," (1952) 19 *U. Chi. L. Rev.* 417, at 520 (Because taxation reaches into the private economic life of every person and household and tax revenues sustain and enable all public spending, how to allocate the burden of taxation or balancing progressivity and efficiency are "perhaps the cardinal instance of the democratic community struggling with its hardest problem.")

117 This may render transformative tax reforms difficult in the absence of significant external shocks (such as war or pandemic) and tempt politicians to sprinkle tax expenditure goodies to as many voters as possible. See Neil Brooks, "Policy Forum: The Case Against Boutique Tax Credits and Similar Tax Expenditures," (2016) 64(1) Canadian T. J. 67-129.

118 See Dylan Marando, "Tales from the Canadian Tax Code: The Policy and Politics of Federal Tax Expenditure Instrument Choice" (2021) (https://tspace.library.utoronto.ca/handle/1807/108764).

119 Electoral Law of the National People's Congress and Local People's Congresses of the People's Republic of China (adopted at the second session of the fifth National's People's Congress on July 1, 1979, amended subsequently (http://www.npc.gov.cn/zgrdw/englishnpc/Law/2007-12/13/content_1384080.htm).

The Constitution (2018) describes the system of government as one of "people's democratic dictatorship" and China as a socialist state with a defining feature of "the leadership of the communist Party of China". refers to the term democracy or its variants in several provisions.[120] Article 3 of the Constitution states that the state organs "apply the principle of democratic centralism" and the National People's Congress "are responsible to the people, and are subject to their oversight".

The National People's Congress not only exercises the legislative power but also has the power to amend the Constitution, elect, among others, the President of China, the Premier of State Council, and the president of the Supreme People's Court.[121] The Standing Committee of the National People's Congress has the power to, among others, interpret the Constitution and interpret laws.[122] The State Council is the executive branch of the government. The Supreme People's Court oversees the adjudicatory work of local courts and is responsible to the National People's Congress and its Standing Committee. The Chinese system is described by some as the "complete process people's democracy":[123] since the 1980s, the voter turnout has been around 90% in every direct election"; "people have the right to participate in the management of national and social affairs in day-to-day political activities"; and "latest opinion polls showed that Chinese citizens' satisfaction with their government reached 98%".

The main differences between the Chinese and Canadian system include: lawmakers are directly elected in Canada, but indirectly elected in China; the judiciary is independent of the Canadian Parliament, but under direct control of the Chinese National People's Congress; and the ruling party varies in Canada, but fixed in China. Open debate about political differences or preferences is not limited by the Canadian constitution while Article 1 of the Chinese Constitution says that "disruption of the socialist system (featuring the leadership of the Communist Part of China) by any organization or individual is prohibited".

4.3 Democratic capitalism v. Socialist Democracy

Canada practices democratic capitalism – a marriage of liberal democracy and market capitalism.[124] To ensure the free market works well, tax neutrality and economic efficiency are important tax policy objectives. In case of perceived market failures, tax incentives are used to induce taxpayer behaviors to engage in activities that have significant societal benefits (e.g., research and development, climate change and education). Tax policies are designed to reduce inequality and reflect a collective notion of fairness. There is a marketplace of political ideas and a "competitive" political process for choosing winning ideas. Overall, one can say that Canada has a kind of welfare capitalism and progressive income tax links liberal democracy and market capitalism.

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120 Constitution of the People's Republic of China (Adopted at the Fifth Session of the Fifth National People's Congress and promulgated for implementation by the Announcement of the National People's Congress on December 4, 1982, subsequently amended) ("China Constitution") (http://www.npc.gov.cn/zgrdw/englishnpc/Constitution/node_2825.htm). Article 1 says: "The People's Republic of China is a socialist State under the people's democratic dictatorship led by the working class and based on the alliance of workers and peasants. The socialist system is the basic system of the People's Republic of China. The defining feature of socialism with Chinese characteristics is the leadership of the Communist Party of China."

121 China Constitution, ibid., article 62.

122 China Constitution, ibid., article 67.

123 See, for example, Yun Chen, "Chinese Democracy: A True Solution for China", Monday December 6, 2021, Jakarta Post, available at http://id.china-embassy.gov.cn/eng/sgdt/202112/t20211206_10462957.htm (visited on April 24, 2023).

124 Martin Wolf, *The Crisis of Democratic Capitalism* (Allen Lane, 2023).

China practices socialist democracy that features an authoritarian regime (as all powers are concentrated in the Communist Party and leader of the party is elected by members of the party) and a socialist market economy. The basis of the socialist economic system is public ownership of the means of production and non-public ownership is allowed as "an important component of the socialist market economy".[125] A socialist market is different from a free capitalist market as the state plays a direct and active role in the market. Such direct role in the market reduces the need for using tax policy to address market failures or to promote economic efficiency. The issue of inequality in market-produced incomes is generally not a political issue, although in the recent few years, wealthy individuals were pressured to donate their wealth during the common prosperity campaigns. There has been no serious consideration of using progressive income tax to reduce income inequality.

Under the Chinese constitution, there is no political party that can replace the Communist Party and no political ideas other than those advocated by the Communist Party are acceptable. The 2022 Communist Party Report says that the individual income tax system should be perfected and be more effective in regulating excessively high income and abolish illegal income.[126] Chinese researchers recently suggest that the IIT be reformed to tax income from capital and capital gains at progressive rates.[127]

5. The Interlinking between Income Tax, Citizenship and Democracy

The degree of interlinking between income tax, citizenship and democracy varies, depending on the nature of tax law provisions as technical rules, or rules to promote economic efficiency or social objectives. In general, the interlink is the strongest in the social dimension.

5.1 The Technical Dimension

The scientific or technical design of income tax law can be regarded as universal and thus apolitical. This technical dimension includes rules defining the who, what, when and how questions in the benchmark system. For example, residence is used widely to define who is liable to tax. Source withholding of tax from employment income is universally used. The Canadian ITA and the Chinese IIT rely on residence and source of income as the basis for asserting tax jurisdiction and withholding of tax at source as the main method of tax collection.

The issue of citizenship taxation or international nomads is unlikely a concern for Canada or China, but for different reasons. For Canada, the benefits of a Canadian passport are arguably not significant enough to

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[125] China Constitution, arts. 6-11.

[126] Xi Jinping, "Hold High the Great Banner of Socialism with Chinese Characteristics and Strive in Unity to Build a Modern Socialist Country in All Respects: Report to the 20th National Congress of the Communist Party of China, October 16, 2022 (https://www.fmprc.gov.cn/eng/zxxx_662805/202210/t20221025_10791908.html)

[127] E.g., Zhang Zhiyong, Ji Dongsheng and Tian Zhiwei, "Thoughts on Optimizing the Distributional Effect of Individual Income Tax to Achieve Common Prosperity", (2023) Issue 1, International Taxation, 3-9 (https://www.ctax.org.cn/xsjl/202301/t20230116_1127350.shtml). In practice, identifying and measuring income from business, investment and the "grey" economy has been challenging. The problem of "grey" or "invisible" income is serious. Chinese researchers found that the "invisible income" of Chinese residents was 9.3 trillion yuan, and the "gray income" was 5.4 trillion yuan, accounting for over 12% of China's economy. See Jin Han, Qingxi Zhao and Mengnan Zhang, "China's Income Inequality in the Global Context", (2016) 7 *Perspectives in Science*, 24-29 at 27 and Wang, Xiaolu, "Measuring the Width of the Wealth Gap", Caixin Global, Sept.23, 2013, https://www.caixinglobal.com/2013-09-23/measuring-the-width-of-the-wealth-gap-101014067.html （Chinese version: https://magazine.caixin.com/2013-11-05/100599523.html）

justify worldwide taxation of a non-resident citizen's global income under the benefit principle. As a net immigration country, Canada is better off with residence-based taxation. For China, because of the prohibition of dual nationality, emigrating Chinese citizens will likely retain their citizenship if they wish to retain social and economic ties with China and will thus be treated as tax residents. For emigrating Chinese citizens who sever their social and economic ties with China, it is unlikely that they wish to remain members of the Chinese political community and retain their political allegiance. As such, the ability to pay principle that justifies the American citizenship taxation will not apply to China.[128]

5.2 The Economic Dimension

The economic dimension of the income tax system is somewhat linked to the political system. Growing the economy and improving the standard of living are common goals. Neutrality and economic efficiency are important tax policy objectives in Canada and China. Both countries use tax policy interventions to correct market failures, to encourage certain investment activities or counter-cyclical pressures through loss carryover rules. However, the degree and manner of tax policy intervention may differ in the two countries, reflecting the different role of market and state, which reflects the constitutional framework of the two countries. For example, Canada provides for generous tax subsidies to Canadian-owned small business corporations, in part because they generate jobs for Canadian workers who are taxpayers and voters.[129] China has virtually no tax subsidies to private businesses.

5.3 The Social Dimension

The social dimension of the income tax system is closed tied to societal values and the political system. In Canada, the income tax is democratic as it literally affects every person living in the country. The large number of personal tax expenditures and transfers is attributable to the election process and importance of public opinion. Taxation is considered a way of sharing of the collective burden of financing public goods and services. The tax system is also used to deliver income support to low-income families because of the institutional capacity of the tax administration in identifying low-income families and making timely payments to them. Everyone is thus connected to the income tax system.

In China, only a small percentage (less than 2%) of citizens pay income tax[130] and no citizens directly participate in electing members of the National People's Congress. Citizens' support to tax reforms is not politically necessary. The IIT is not a meaningful instrument for reducing income inequality or implementing social policies. The small number of IIT taxpayers is somewhat puzzling, considering that per capita income in China has been steadily rising from USD194 in 1980 to USD873 in 1999, USD 9,905 in 2018, and $11,880 in 2021.[131] The number of millionaires in China has also been rising from zero to over

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[128] For an explanation of the benefit principle and ability to pay principle in the US context, see Reuven S. Avi-Yonah, "Taxing Nomads: Reviving Citizenship-based Taxation for the 21st Century", *U of Michigan Public Law Research Paper No. 22-035.*

[129] Canada, Tax expenditure report, supra note 40.

[130] In the absence of available official data on the number of individuals paying the IIT, unofficial estimates suggest the number to be from 64 million to 100 million (out of 1.4 billion population). Prior to the 2018 reform that raised the exemption threshold, the number was bigger, roughly about 2% of the Chinese population paid the IIT. See The Economist, "Why only 2% of Chinese pay any income tax"? Dec.1, 2018 (https://www.economist.com/china/2018/12/01/why-only-2-of-chinese-pay-any-income-tax);

[131] See World Bank, https://data.worldbank.org/indicator/NY.GDP.PCAP.CN?locations=CN&name_desc=true

6 million in 2022, ranking the second in the world (after the United States).[132] Unlike many developing countries, China's tax administration has the necessary technological resources to enforce tax collection. In fact, a recent study suggests that the Chinese IIT is administered more efficiently than Canada, the United States, Australia in terms of withholding at source, tax refund, use of e-filing, pre-filling of tax returns and the amount of time for processing tax refund.[133] The political system is thus a more possible explanation for the minor role of the IIT.[134]

6. CONCLUSIONS

The comparative case study of the Canadian and Chinese income tax systems leads to the following conclusions. First, at a high-level, there is no interlinking between the income taxes and the type of political system in the sense that both countries with different political systems have progressive income taxes and the Chinese political system remains the same before and after the introduction of the IIT.

Second, the link between tax law design and political systems is weak in the technical and economic dimensions. The link is stronger in the social dimension. The more "democratic" nature of the Canadian income tax may also be explained by the level of per capita income, the societal values of sharing or inclusiveness[135] or influences of the United States and United Kingdom. The narrow scope of the Chinese IIT may also be explained by the economic structural transformation (from a command agricultural economy to a market-based industrial and technological economy) and an under-developed private law system that clearly delineates private property and contractual rights and helps ascertain who earns what income.[136]

Third, it is difficult to ascertain the extent to which the differences in tax structure and tax-to-GDP ratio in the two countries are attributable to differences in the political system. When compared to democracies at similar economic development level, the Chinese tax-to-GDP ratio compares favorably to India (12%), Argentina (10.9%), Brazil (13%) and South Africa (23.3).[137] Individual income tax accounts for less than 10% of total tax revenues in low-income OECD member countries: Colombia, Costa Rica, and Czechia.[138]

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[132] Selena Li, "Chinese millionaires to double by 2026, Credit Suisse says, despite slowing economy", Sept.20, 2022, Reuters Finance (China had 6.2 million millionaires in 2022), https://www.reuters.com/business/finance/household-wealth-saw-record-growth-2021-expected-slow-2022-credit-suisse-2022-09-20/.

[133] China International Tax Research Institute, "International Comparative Study of China Individual Income Tax Annual Settlement", December 2021 (http://www.chinatax.gov.cn/chinatax/n810219/n810724/c5171576/content.html).

[134] See Lawrence W. Kenny and Stanley L. Winer, "Tax Systems in the World: An Empirical Investigation into the Importance of Tax Bases, Administration Costs, Scale and Political Regime", Kenny, Lawrence W. and Winer, Stanley L., Tax Systems in the World: An Empirical Investigation into the Importance of Tax Bases, Collection Costs, and Political Regime (May 1, 2001). Carleton Economic Working Paper No. 01-03, International Tax and Public Finance, Vol. 13, 2006, Available at SSRN: https://ssrn.com/abstract=280097 or http://dx.doi.org/10.2139/ssrn.280097

[135] See John Ralston Saul, "A Fair Country: Telling Truths about Canada" (Toronto, 2008); Carter Report, supra note 25, Volume 2.

[136] Since the late 1970s, China has introduced many laws to govern private relationships and commercial dealings. However, the grey or underground economy remains a large segment of the economy. Illegal income is considered significant enough to be mentioned in the Party Congress Report in 2022.

[137] World Bank, https://data.worldbank.org/indicator/GC.TAX.TOTL.GD.ZS

[138] OECD, Sources of Tax Revenue, OECD Countries, 2021.

Globalization and international tax competition put pressure on all countries. Capital importing countries may be pressed more to adopt tax and fiscal policies that are more friendly to mobile capital and people. Differences in political regimes may pale in comparison to global pressures.