

# Journal of Chinese Tax & Policy

中国税收与政策

**BALANCING EFFICIENCY AND EQUITY: INSIGHTS  
FROM AUSTRALIA'S ROBODEBT AND CHINA'S  
ROBODEBT PLUS ROBOCREDIT IN AUTOMATED  
WELFARE SYSTEM**

GEORGE TIAN

**REFLECTIONS ON THE TAX DISCLOSURE SYSTEM  
TRIGGERED BY INVESTMENT AND TAX PLANNING  
BY CHINA'S HIGH NET WORTH INDIVIDUALS**

YUAN JI



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## ABOUT THE JOURNAL

The importance of China on the global economic stage cannot be ignored, and its unique legal and tax systems are of great interest to international scholars and business people alike. China's tax system is acquiring western features while remaining entrenched in its rich cultural and historical roots. This makes for interesting study, analysis and comparison as its laws are becoming more accessible.

The Journal of Chinese Tax & Policy focuses on the policy, administrative and compliance aspects of the Chinese tax system. It also welcomes comparative studies between China and other countries. The Journal is an internationally peer-reviewed scholarly publication.

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## Editorial

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The 2024 issue 13 of the Journal of Chinese Tax and Policy features articles discusses Automated Decision-Making (ADM) in welfare administration and the importance of tax disclosure.

Tian's paper investigates the integration of Automated Decision-Making (ADM) systems in welfare administration, drawing on the valuable experiences of Australia and China. Both cases emphasized the need for carefully designed ADM frameworks that address legal, ethical, and operational challenges. The article highlights how lessons from Australia and China can guide policymakers in developing welfare systems that leverage automation to enhance efficiency while safeguarding equity and public trust. This study offers a roadmap for global welfare administration to integrate technology responsibly and effectively by synthesizing these experiences.

Ji's paper discusses the growing demand for tax planning among wealthy Chinese households, emphasizing the need for careful attention to tax planning, potential tax avoidance, and the importance of tax disclosure. As tax authorities want compliance with tax regulations, the significance of tax disclosures is increasingly apparent. Ji argues that by improving tax disclosure, it is possible to reduce criminal activities associated with tax evasion and address the inefficiencies and inequities in the taxation system.

*Eva Huang*

*Sydney, December 2024*

# Balancing Efficiency and Equity: Insights from Australia's Robodebt and China's Robodebt Plus RoboCredit in Automated Welfare System

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George Yijun Tian \*

**Abstract:** This article explores the integration of Automated Decision-Making (ADM) systems in welfare administration, drawing on the valuable experiences of Australia and China. Australia's Robodebt scheme, designed to recover overpaid welfare benefits, revealed critical insights into the importance of transparency, accountability, and robust safeguards in ADM systems. Similarly, China's approach, particularly Guangdong's "Robodebt plus RoboCredit" model, provides lessons on balancing fiscal responsibility with inclusivity by combining automated alerts with human oversight to ensure fairness and adaptability. Both cases underscore the need for carefully designed ADM frameworks that address legal, ethical, and operational challenges. The article highlights how lessons from Australia and China can guide policymakers in developing welfare systems that leverage automation to enhance efficiency while safeguarding equity and public trust. By synthesizing these experiences, this study offers a roadmap for global welfare administration to integrate technology responsibly and effectively.

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## I . Introduction

Automated Decision-Making (ADM) systems have become a cornerstone of modern governance, offering opportunities to streamline processes, reduce human error, and enhance resource efficiency. These systems are increasingly being used by government agencies to assist or replace human decision-makers in tasks that traditionally required public servants' discretion, particularly in the administration of social insurance and welfare programs.<sup>1</sup> Despite their significant promise, ADM systems also raise complex legal and ethical challenges that demand careful consideration.<sup>2</sup>

Australia's experience with ADM in welfare management, most notably through the Robodebt Scheme, serves as a cautionary example of the potential risks. This initiative sought to recover overpaid social welfare benefits using data from various sources, including the Australian Taxation Office (ATO). However, the scheme suffered from significant flaws, such as errors in debt calculations, a lack of transparency, and inadequate safeguards for vulnerable individuals. These shortcomings triggered widespread public backlash, legal challenges, and ultimately led to the government settling a \$1.751 billion class-action lawsuit and issuing a formal apology.<sup>3</sup> The Robodebt failure underscores the financial and reputational costs of poorly designed and implemented ADM systems.<sup>4</sup>

China, similarly, faces risks as it increasingly integrates ADM technologies into its welfare administration. Initiatives such as the Ministry of Civil Affairs' National Low-Income Population Dynamic Monitoring Platform<sup>5</sup> and the Resident Household Economic Status Verification Mechanism<sup>6</sup> illustrate the country's growing reliance on ADM technologies. These developments highlight the importance of learning from past challenges to ensure that ADM systems are implemented effectively and equitably. Australia's Robodebt experience serves as a cautionary tale for China and other nations, offering valuable lessons on the importance of transparency, due process, and human oversight in ADM systems.

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<sup>1</sup> Saabiq Chowdhury, 'Technology is never neutral: Robodebt and a human rights analysis of automated decision-making on welfare recipients' (Pt Taylor & Francis Ltd) (2024) 30(1) *Australian journal of human rights* 20-40.at 20.

<sup>2</sup> Dominique Hogan-Doran, 'Computer says "no": Automation, algorithms and artificial intelligence in Government decision-making' (Pt Judicial Commission of NSW) (2017) 13(3) *Judicial review (Sydney, N.S.W.)* 345-382.at 377.

<sup>3</sup> *The Royal Commission into the Robodebt Scheme Report of the Royal Commission into the Robodebt Scheme* (Report, 7 July 2023) vol 1-3, ('Report').at xxix.

<sup>4</sup> *Ibid.*at 234.

<sup>5</sup> The National Low-Income Population Dynamic Monitoring Information Platform, established by the Ministry of Civil Affairs of China, is designed to monitor and assist low-income groups. As of May 2024, the platform has monitored over 80.15 million people .Shiwen Chen, 'Ministry of Civil Affairs: The National Low-Income Population Dynamic Monitoring Platform Covers Over 80 Million People', *CCTV Chinese News*, May 10, 2024) <<https://news.cctv.com/2024/05/10/ART17ahZldLCaAY4kMH5QLKz240510.shtml>>.[in Chinese]. See also General Office of the State Council of China, 'Notice of the General Office of the State Council on Forwarding the "Opinions on Strengthening the Dynamic Monitoring of Low-Income Populations and Improving Tiered and Categorized Social Assistance Work" Issued by the Ministry of Civil Affairs and Other Departments' 39) <[https://www.gov.cn/zhengce/content/202310/content\\_6911065.htm](https://www.gov.cn/zhengce/content/202310/content_6911065.htm)>.

<sup>6</sup> *Notice from the General Office of the Ministry of Civil Affairs on Issuing the "Interconnected Inquiry Measures for Resident Household Economic Status Information between the Ministry and Provincial Departments (Trial)" 2018.*[in *ibid.Chinese*]

Conversely, China's innovative approach, including its integrated 'Robodebt plus RoboCredit' model and its dual system of 'online verification and offline investigation',<sup>7</sup> provides insights for future policymakers in Australia and globally.

This paper argues that the lessons from Australia's Robodebt experience are twofold. First, Robodebt demonstrates the dangers of deploying ADM systems without sufficient safeguards, rigorous design, and adherence to due process. The reliance on flawed algorithms led to significant errors and injustices, serving as a warning for other nations implementing similar technologies. Second, Australia's response to the crisis—including legal accountability, financial redress, and systemic reforms—illustrates the importance of resilience and commitment to the rule of law. Effective governance involves not only minimizing errors but also addressing mistakes proactively to maintain public trust and credibility.

Similarly, China's experiences in establishing balanced social welfare systems, particularly through its dual-function ADM systems combining Robodebt-style vigilance with RoboCredit inclusivity, provide valuable insights for global policymakers. Its integration of human oversight through online verification and offline investigation demonstrates a flexible and equitable model that other nations can adapt when designing welfare systems.

More specifically, Part II of this paper provides an overview of the Australian Robodebt scheme, including its objectives, implementation, failures, and the government's subsequent responses, such as reforms and legal actions. Part III examines China's social welfare system, focusing on its recent ADM applications and the integration of tax data into welfare administration, while drawing comparisons with Australia's approach to identify similarities and differences. Finally, Part IV synthesizes lessons from both Australia and China, offering practical recommendations for policymakers globally, emphasizing transparency, accountability, and adherence to the rule of law in the development and implementation of ADM systems.

## **II. Overview of Australia's Social Welfare System and Robodebt Scheme**

Australia's welfare system plays a critical role in ensuring social equity and providing financial support to those in need. Administered primarily through Services Australia (SA), the system relies on a combination of legislative frameworks and administrative systems, including automated decision-making, to manage welfare allowances. However, the implementation of such systems has sparked debates regarding their efficacy and fairness, particularly in the wake of the controversial Robodebt scheme.

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<sup>7</sup> See Part III of the article.

## 2.1. Australia's Social Welfare System

### 2.1.1. Authorities in Charge of Welfare Distribution

Put simply, the administration of welfare payments in Australia is primarily the responsibility of Services Australia (SA), operating under the Department of Social Services.<sup>8</sup> SA is tasked with processing applications, assessing eligibility, and distributing payments. Its operations are guided by the *Social Security (Administration) Act 1999* (Cth),<sup>9</sup> which outlines procedural requirements for welfare distribution.

The Administrative Review Tribunal (ART), formerly known as the Administrative Appeals Tribunal (AAT),<sup>10</sup> functions as an independent body responsible for reviewing decisions made by Australian government agencies, departments, and ministers, including those related to welfare, providing individuals with the opportunity to appeal adverse determinations.<sup>11</sup>

Oversight is further provided by the Australian Human Rights Commission (AHRC), which plays a critical role in ensuring that welfare policies and practices align with Australia's anti-discrimination laws, such as the *Racial Discrimination Act 1975* (Cth) (RDA),<sup>12</sup> the *Disability Discrimination Act 1992* (Cth) (DDA),<sup>13</sup> and the *Sex Discrimination Act 1984* (Cth).<sup>14</sup> The AHRC monitors the equitable implementation of welfare measures, addressing systemic inequalities and advocating for fair treatment of all individuals, particularly those from vulnerable or marginalized groups.<sup>15</sup>

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<sup>8</sup> Australian Government - Services Australia, 'Who we are' <<https://www.servicesaustralia.gov.au/who-we-are?context=22#:~:text=We%20are%20Services%20Australia%2C%20an,Medicare>>.

<sup>9</sup> *Social Security (Administration) Act 1999* (Cth) 1999 (Australia) ('*Social Security (Administration) Act 1999* (Cth)').

<sup>10</sup> The Administrative Appeals Tribunal (AAT) was replaced by the Administrative Review Tribunal (the Tribunal) on 14 October 2024. See Australian Government Attorney-General's Department, *A new system of federal administrative review* <<https://www.ag.gov.au/legal-system/new-system-federal-administrative-review>>.

<sup>11</sup> The Administrative Review Tribunal, 'The Administrative Review Tribunal', (Blog Post) <<https://www.art.gov.au/>>.

<sup>12</sup> Australian Human Rights Commission, 'Racial discrimination', *Racial discrimination* <[https://humanrights.gov.au/our-work/employers/racial-discrimination#:~:text=The%20Racial%20Discrimination%20Act%201975,ethnic%20origin%2C%20or%20immigrant%20status](https://humanrights.gov.au/our-work/employers/racial-discrimination#:~:text=The%20Racial%20Discrimination%20Act%201975,ethnic%20origin%2C%20or%20immigrant%20status.)>.

<sup>13</sup> Australian Human Rights Commission, '8 Legal and policy framework', *Our Work* <<https://humanrights.gov.au/our-work/8-legal-and-policy-framework>>. (see section 8.2 Domestic legal framework).

<sup>14</sup> *Sex Discrimination Act - Compilation No.46 1984* (Cth Australia) ('*Sex Discrimination Act - Compilation No.46*'). See Australian Human Rights Commission, *Equality across the board: Investing in workplaces that work for everyone* (Report, June 2021). at 27.

<sup>15</sup> See Australian Human Rights Commission, 'Australian Human Rights Commission Submission to the Access and Equity Inquiry Panel', *Access and Equity: Inquiry into the responsiveness of Australian Government services to Australia's culturally and linguistically diverse population*, 24 February 2012) <<https://humanrights.gov.au/our-work/legal/access-and-equity-inquiry-responsiveness-australian-government-services-australias>>. at para 81 (stated 'While the Access and Equity Strategy has a vital connection to direct frontline services such as employment, health, welfare, tax and education, the Strategy has relevance and applicability to the full suite of Australian Government policies, programs and services')

### 2.1.2. Dual Threshold of Low Income to Access Allowances: Fortnightly vs. Annually

Eligibility for welfare payments in Australia is governed by income and asset thresholds to ensure support reaches those most in need. The *Social Security Act 1991 (Cth)* (SSA) defines these thresholds, while the *Social Security (Administration) Act 1999 (Cth)* (SSAA) focuses on administrative processes.<sup>16</sup> Conditions under which benefits are granted vary depending on the type of payment, with some using ‘fortnightly’ income thresholds and others relying on ‘annual’ income thresholds.

Payments like *JobSeeker* and *Age Pension* use fortnightly income thresholds, adjusting support based on short-term income changes. For example, *JobSeeker* allows single individuals to earn up to \$150 per fortnight without reduction, with payments tapering above this amount.<sup>17</sup> Similarly, the *Age Pension* permits earnings up to \$212 per fortnight as of 20 September 2024, reducing payments by 50 cents per dollar earned beyond this threshold.<sup>18</sup>

Family-related allowances, such as the Family Tax Benefit (FTB), use annual income thresholds, offering stability for long-term financial planning. As of 20 November 2024, families earning under \$65,189 annually receive the maximum payment, with benefits tapering for higher incomes.<sup>2</sup> This dual system balances responsiveness for individuals with variable earnings and stability for families managing predictable finances, addressing diverse needs effectively.

### 2.1.3. Application of Automated Decision-Making Systems: Digital integration and data sharing

Automated decision-making systems are integral to administering welfare payments in Australia, enabling efficient processing and compliance monitoring. A notable example is the *myGov* platform, which allows individuals to lodge applications, report changes in circumstances, and track payments online.<sup>19</sup> Through *myGov*, users can seamlessly access services from 17 government agencies, including the *Australian Taxation Office (ATO)*, *Centrelink*, *Medicare*, and *My Aged Care*, creating a centralized hub for managing interactions with government programs<sup>20</sup>. For instance, applicants can claim a *JobSeeker Payment* directly through their *myGov* account after linking it to *Centrelink*.<sup>21</sup>

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<sup>16</sup> Unlike the *Social Security (Administration) Act 1999*, which focuses on administrative processes—such as how payments are applied for, assessed, delivered, and reviewed—the *Social Security Act 1991* establishes the substantive framework, defining the types of payments (e.g., *JobSeeker*, *Aged Pension*), eligibility criteria, payment rates, and the conditions under which benefits are granted. See Ch 2, Pt 2.2. *Age Pension*, and Pt 2.12 *Jobseeker Payment*, SSA 1991.

<sup>17</sup> Section 1068 of the *Social Security Act 1991* (s1068-G12)

<sup>18</sup> Services Australia, 'Individuals-Ageing-Income test', *Individuals-Ageing-Income test*, 20 September 2024) <<https://www.servicesaustralia.gov.au/income-test-for-age-pension?context=22526>>.

<sup>19</sup> Australian Government, 'About myGov', *About myGov*, 9 September 2024) <<https://my.gov.au/en/about>>.

<sup>20</sup> Australian Government, 'Access government services', *About myGov*, 9 September 2024) <<https://my.gov.au/en/about#access-government-services>>.

<sup>21</sup> Australian Government, 'JobSeeker Payment', *JobSeeker Payment*, 2 January 2025) <<https://my.gov.au/en/services/work/recently-unemployed/payments-to-help-if-you-ve-lost-your-job/payments-to-help-job-seekers/jobseeker-payment>>.

Automation streamlines eligibility assessments by applying income and asset thresholds defined by legislation. For example, *JobSeeker Payment* recipients must regularly report their income, which is automatically cross-referenced against thresholds to adjust payment amounts.<sup>22</sup> Similarly, *data-matching programs* compare welfare claims with ATO tax records, such as the data-sharing initiatives between the ATO, Services Australia, and Centrelink, to identify inconsistencies that may indicate overpayments or fraud.<sup>23</sup>

*Compliance monitoring* is another critical function of automated systems. For example, recipients of *JobSeeker Payment* are subject to mutual obligation requirements, such as attending job interviews or participating in training programs. Non-compliance is flagged automatically, potentially leading to payment suspensions or penalties.<sup>24</sup>

#### 2.1.4. Limits and Risks of Automated Systems

Despite their efficiency, automated systems have notable limitations and risks. Firstly, automated systems are prone to errors in data interpretation. These systems apply rules rigidly, often failing to account for complex or nuanced financial situations. For example, fluctuating incomes or irregular employment patterns can lead to incorrect assessments of eligibility, resulting in overpayments or unjustified debt notices. The *Robodebt scheme* serves as a stark example, where reliance on flawed automated processes caused significant distress among recipients.<sup>25</sup> This issue will be explored in greater detail in a later section.

Secondly, reliance on digital platforms can marginalize vulnerable populations, particularly Indigenous Australians in remote areas, who face barriers such as limited internet access, low digital literacy, and language challenges. A 2023 study by the Australian Digital Inclusion Index (ADII) revealed a 7.5-point digital inclusion gap between First Nations and non-First Nations people, with the disparity widening to 21.6 points in remote areas and 23.5 points in very remote areas.<sup>26</sup> These challenges hinder equitable access to welfare services, making it crucial to address the digital divide to ensure inclusivity in automated welfare systems.

Thirdly, privacy and data security concerns emerge from the extensive use of data-matching programs. In 2023, an independent review of Services Australia's data systems, released by the Office of the Australian Information Commissioner

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<sup>22</sup> Services Australia, 'Employment income reporting', 21 February 2024) <<https://www.servicesaustralia.gov.au/employment-income-reporting?context=51411>>.

<sup>23</sup> See Australian Taxation Office (ATO), 'How we use data matching', 15 May 2023) <<https://www.ato.gov.au/about-ato/commitments-and-reporting/in-detail/privacy-and-information-gathering/how-we-use-data-matching>>.

<sup>24</sup> Regarding Compliance Monitoring and Mutual Obligation Requirements, S42AF of SSAA 1999 outlines compliance actions for mutual obligation failures, detailing the consequences for recipients who do not meet their participation requirements. Specifically, the SSAA outlines the compliance framework for participation payments: ss42E, 42G, 42H. See also Services Australia, 'Demerits and penalties for not meeting mutual obligation or participation requirements', 28 September 2023) <<https://www.servicesaustralia.gov.au/demerits-and-penalties-for-not-meeting-mutual-obligation-or-participation-requirements>>.

<sup>25</sup> Chowdhury (n ) at 24 and 32 (stated 'DPOs compounded the existing financial and mental distress of debt recipients.').

<sup>26</sup> Australian Digital Inclusion Index (ADII), 'Measuring Australia's digital divide - Key findings and next steps') <<https://www.digitalinclusionindex.org.au/key-findings-and-next-steps/>>.

(OAIC), identified several vulnerabilities in identity exchanges and broader cybersecurity measures.<sup>27</sup> The OAIC revealed that Services Australia has not ‘fully implemented’ the recommendations from penetration tests and annual Infosec Registered Assessors Program (IRAP) of Australian Signal Directorate (ASD).<sup>28</sup> The OAIC revealed that ‘the data breach response plan for the identity exchange had never been tested’, and the plan lacked clear protocols, such as identifying key contacts for incident response.<sup>29</sup> These findings emphasized the urgent need for robust safeguards to protect personal information and maintain the integrity of automated systems.

Lastly, the lack of human oversight in automated processes can undermine accountability.<sup>30</sup> Automated decisions, particularly in compliance programs, may fail to consider individual circumstances, leaving recipients struggling to appeal decisions.<sup>31</sup> This issue was vividly demonstrated by the *Robodebt scheme*, which relied on flawed automated processes, leading to widespread criticism and legal challenges.<sup>32</sup> The following section delves deeper into the issues surrounding the Robodebt scheme, focusing on the reasons for its failure and the post-failure actions taken by the Australian government.

## 2.2. The Robodebt Scheme: A Cautionary Tale

The Robodebt scheme, also known as the Income Compliance Program, was implemented between 2015 and 2019 to modernize welfare compliance processes.<sup>33</sup> The scheme utilized automated systems to compare Centrelink records with income data from the Australian Taxation Office (ATO), flagging discrepancies and issuing debt notices based on identified mismatches.<sup>34</sup> Promoted as a cost-saving measure, the program was expected to enhance efficiency and recover significant overpayments to welfare recipients.<sup>35</sup> However, the scheme's heavy reliance on automation, combined with inadequate oversight and flawed methodologies,

<sup>27</sup> Ry Crozier, 'Services Australia finds 'high risk' vulnerability in identity exchange', *itnews*, Feb 23, 2023) <<https://www.itnews.com.au/news/services-australia-finds-high-risk-vulnerability-in-identity-exchange-591218>>. see also Graham Ashton, 'Security Risk Management Review – Key Findings and Recommendations' (Report, Services Australia, July 2023) <<https://www.servicesaustralia.gov.au/sites/default/files/2023-10/services-australia-security-risk-management.pdf>>.

<sup>28</sup> Crozier (n ; see Australian Signals Directorate, 'Infosec Registered Assessors Program (IRAP)', 12 Jun 2019 (last updated: 15 Aug 2024)) <<https://www.cyber.gov.au/irap>>. (stated ‘An IRAP security assessment helps organisations understand their system’s security strengths and weaknesses and provides recommendations that can be utilised as part of their organisational security program.’)

<sup>29</sup> Crozier (n

<sup>30</sup> Ben Green, 'The flaws of policies requiring human oversight of government algorithms' (2022) 45 *Computer Law & Security Review* 105681.at 2.

<sup>31</sup> Emre Bayamlioglu, 'Contesting Automated Decisions: A View of Transparency Implications' (Pt Lexxion Verlag) (2018) 4(4) *European data protection law review (Internet)* 433-446. Monika Zalnieriute, Lyria Bennett Moses and George Williams, 'Title of host publicationTechnology, innovation and access to justice - dialogues on the future of law' in Siddharth Peter De Souza and Maximilian Spohr (eds), *Edinburgh University Press; Edinburgh, UK* (Edinburgh University Press, 2021).

<sup>32</sup> Toby Murray, Marc Cheong and Jeannie Paterson, 'The flawed algorithm at the heart of Robodebt', *PURSUIT*, 10 July 2023) <<https://pursuit.unimelb.edu.au/articles/the-flawed-algorithm-at-the-heart-of-robodebt>>.

<sup>33</sup> Services Australia, 'Information about Robodebt', 28 September 2023) <<https://www.servicesaustralia.gov.au/information-about-robodebt?context=60271#a1>>.

<sup>34</sup> *Report* (n at 12. See also Murray, Cheong and Paterson (n

<sup>35</sup> Chiraag Shah, 'Australia's Robodebt scheme: A tragic case of public policy failure', *Voices*, 26 July 2023) <<https://www.bsg.ox.ac.uk/blog/australias-robodebt-scheme-tragic-case-public-policy-failure>>.

culminated in profound legal, economic, and social failures—regarded as "one of Australia's most egregious and tragic public governance failures."<sup>36</sup>

### 2.2.1 Failures and Consequences

The Robodebt scheme exposed significant failures in design, implementation, and oversight, leading to devastating legal, economic, and social consequences.

First, the scheme's reliance on income averaging proved to be its most critical flaw. As discussed earlier, the conditions under which benefits are granted vary depending on the type of payment, with some payments applying fortnightly income thresholds and others using annual income thresholds.<sup>37</sup> Robodebt, however, assumed that welfare recipients' earnings were evenly distributed across the year, disregarding income fluctuations that are particularly common for casual and seasonal workers.<sup>38</sup> For example, a hospitality worker earning \$15,000 over six months but with no income for the remainder of the year could be assessed as earning \$577 per fortnight. This flawed methodology resulted in inflated debt calculations, leading to unjust claims against recipients.

Second, the automated decision-making process placed an undue burden on welfare recipients by reversing the traditional onus of proof. Instead of requiring the government to substantiate debt claims, the scheme demanded individuals disprove the debts issued against them. This procedural unfairness was declared unlawful by the Federal Court of Australia in 2019, which ruled that the government's method (under the Robodebt scheme) of using averaged income data from the ATO to calculate debts was invalid.<sup>39</sup> Further, in 2021, Justice Murphy described the Robodebt Scheme as a "shameful chapter" in Australian public administration, highlighting its unlawful practice of raising welfare debts against social security recipients by the Commonwealth.<sup>40</sup>

The social consequences of the scheme were equally devastating. Vulnerable populations, including low-income families, single parents, and individuals with disabilities, were disproportionately affected.<sup>41</sup> Incorrect debt notices caused significant financial strain and emotional distress, with reports linking the scheme to cases of severe anxiety, depression, and even suicides.<sup>42</sup> The impersonal and often

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<sup>36</sup> Ibid.

<sup>37</sup> See section 2.1. 2 Dual Threshold of Low Income to Access Allowances: Fortnightly vs. Annually of this paper.

<sup>38</sup> Peter Whiteford, 'Why robodebt's use of 'income averaging' lacked basic common sense', *The Conversation*, March 16, 2023) <<https://theconversation.com/why-robodebts-use-of-income-averaging-lacked-basic-common-sense-201296>>.

<sup>39</sup> in *Amato v The Commonwealth of Australia* (Federal Court of Australia, VID611/2019, 27 November 2019) (*Amato v The Commonwealth of Australia*)..)

<sup>40</sup> See *Prygodicz v Commonwealth* [No 2] [2021] FCA 634; (2021) 173 ALD 277, 280 (Murphy J). See also Fiona Shah, 'A Clouded 'vision Splendid': the Limits of Administrative Review of Executive Action in the Context of the Robodebt Scheme' (2024)(24) *University of New South Wales Law Journal Student Series* 13.

<sup>41</sup> *Prygodicz v Commonwealth of Australia (No 2)* (2021) [2021] VID 1252 of 2019 FCA 634 (*Prygodicz v Commonwealth of Australia (No 2)*).para 331.

<sup>42</sup> Ibid.para 23 (stated 'One thing that stands out from the objections is the financial hardship, anxiety and distress, including suicidal ideation and in some cases suicide, that people say they have suffered through the Robodebt system, and that many say they felt shame and hurt at being wrongly branded "welfare cheats"').

intimidating communication methods used by the program exacerbated these issues, leaving many recipients feeling powerless and stigmatised.<sup>43</sup>

Finally, the scheme failed economically. Instead of achieving the projected savings of \$1.7 billion over its first five years of operation, the government ultimately spent nearly half a billion dollars while causing significant distress to hundreds of thousands of income support recipients.<sup>44</sup> These expenditures, combined with the erosion of public trust in welfare administration, rendered Robodebt an unequivocal failure.<sup>45</sup>

## 2.2.2 Reasons for Failure

The Robodebt scheme's failures were rooted in operational and systemic deficiencies that severely undermined its legitimacy and effectiveness. These issues stemmed from a flawed design, largely due to insufficient prior consultation, inadequate safeguards, and broader shortcomings in welfare administration. Together, these issues highlighted the risks of prioritizing automation without proper oversight and accountability.

First, the *lack of meaningful consultation* during the scheme's development contributed to its reliance on automation, poorly designed algorithms, and outdated IT infrastructure, which created significant operational challenges. As mentioned above, by depending solely on annual income averaging to identify overpayments, the system failed to account for the complexities of individual income patterns. This flaw disproportionately impacted casual and seasonal employees, whose fluctuating earnings were misinterpreted, often leading to erroneous debt notices.<sup>46</sup> The absence of input from legal and social policy experts during the scheme's design underscored the government's inability to foresee the risks and consequences of automating welfare compliance.<sup>47</sup> As the Royal Commission into Robodebt observed, "staff were in a unique position to identify issues with the design of the Scheme," but their insights and expertise were not adequately incorporated into its implementation.<sup>48</sup>

Second, the *absence of sufficient safeguards and human oversight* within the automated system *during* the decision-making process significantly exacerbated the scheme's failures. With minimal human intervention, errors in calculations went undetected, and there was no mechanism for assessing individual circumstances.<sup>49</sup> The Royal Commission noted that 'there was no meaningful human intervention in the calculation and notification of debts under the OCI phase of the Scheme. This meant that debts being raised on incorrect data—or incorrectly applied data—were

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<sup>43</sup> Ibid.

<sup>44</sup> Report (n ) at 471.

<sup>45</sup> Terry Flew, 'The other cost of Robodebt: distrust in technology, media & Government', *Australian Academy of the Humanities*, July 2023) <<https://humanities.org.au/power-of-the-humanities/the-other-cost-of-robodebt-trust-in-technology-media-and-government/>>.

<sup>46</sup> See section 2.2.1. of this paper.

<sup>47</sup> Report (n ) at 392 (stated 'There was a lack of consultation with DHS frontline employees and stakeholder groups prior to the implementation of the Scheme')

<sup>48</sup> Ibid.) at 392.

<sup>49</sup> Ibid.) at 472 (stated 'once the rules had been coded and set in place, the system itself would stay in place until the rules were changed by way of human intervention.)

issued with no review.<sup>50</sup> This rigidity and absence of accountability intensified the scheme's harmful effects, especially on vulnerable recipients. In the absence of human oversight, welfare recipients were left to shoulder the burden of disproving debts, effectively reversing the traditional onus of proof<sup>51</sup> and breaching principles of procedural fairness.<sup>52</sup>

Third, the lack of *effective review pathways following* the decision-making process further compounded the scheme's failings. The absence of channels for meaningful communication with individuals affected by debt decisions denied them the opportunity to challenge inaccuracies or provide context for their circumstances. As the Royal Commission pointed out, 'transparency regarding the use of automation in decision making, and the ability of affected persons to review such decisions, are vital safeguards in the use of automated decision making'.<sup>53</sup> This lack of transparency and recourse deepened the ethical and procedural shortcomings of the scheme, leaving affected individuals with limited options for redress and amplifying its negative impact.

Collectively, these deficiencies reflected a broader neglect of ethical considerations in the pursuit of operational efficiency. The lack of consultation, safeguards, and transparency not only harmed individual welfare recipients but also undermined public trust in the system, leaving a legacy of eroded confidence in government processes.<sup>54</sup>

### 2.2.3. Remedies and Responses of the Australian Government

In response to widespread criticism and legal challenges, the Australian Government implemented several measures to address the failures of the *Robodebt scheme*. These actions aimed to rectify the harm caused, restore public trust, and establish a more accountable welfare compliance system.

The first major reform involved *ceasing the use of income averaging for debt calculations* under the Scheme, and *reinforcing human oversight* in debt assessments. Following the Federal Court's 2019 ruling that declared the practice unlawful,<sup>55</sup> human oversight was reinstated in compliance processes using automated decision-making system. The Royal Commission into the Robodebt Scheme emphasized that 'in the social security context, human oversight of the

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<sup>50</sup> Ibid.at 477 (the OCI is an abbreviation of 'Online Compliance Intervention')

<sup>51</sup> Ibid.at 365 (stated 'Dr Goldie considered (correctly) that Mr Tudge's letter did not address the big problems with the Scheme: "the income averaging, the raising of a debt against that process and the reversing of the onus of proof."');

<sup>52</sup> Ibid.at 482 (stated 'The utilisation of automated decision-making raises a range of rule of law issues, in particular regarding procedural fairness, the transparency of decisionmaking, the protection of personal privacy, and the right to equality.') see also Yee-Fui Ng, 'Institutional Adaptation and the Administrative State' (2021) 44(3) *Melbourne University Law Review* 889.;

<sup>53</sup> *Report* (n at 482 (stated 'The utilisation of automated decision-making raises a range of rule of law issues, in particular regarding procedural fairness, the transparency of decisionmaking, the protection of personal privacy, and the right to equality.') see also Yee-Fui Ng (n ;

<sup>54</sup> *Report* (n at 486.

<sup>55</sup> Casey Tonkin, 'Court finds robodebt unlawful: Debt raised by the algorithm was legally 'irrational'', *ACS Information Age*, Nov 28 2019) <<https://ia.acs.org.au/article/2019/court-finds-robodebt-unlawful.html>>.

system is needed to mitigate the risk of error'.<sup>56</sup> This reform marked a pivotal shift toward a more transparent and accountable approach to welfare administration, ensuring that future decisions complied with legal and ethical standards, including Australian AI Ethics Principles.<sup>57</sup> The Department of Social Services and Services Australia pledged to enhance staff training and actively engage stakeholders in developing future compliance mechanisms to ensure alignment with legal and ethical standards. This initiative includes the establishment of a new Chief Data Officer role at Services Australia, focusing on data governance, reporting, analysis, data science, and mandatory ethics training for in-house legal staff.<sup>58</sup>

Second, the government prioritized *compensation* for those harmed by the scheme. It pledged to refund debts partially or entirely calculated using income averaging if they had been repaid, and to cancel any outstanding debts.<sup>59</sup> This initiative resulted in \$746 million being reimbursed to around 381,000 individuals, alongside the elimination of \$1.751 billion in unpaid debts.<sup>60</sup> In addition, in November 2020, the government settled a class-action lawsuit for \$1.2 billion before it could go to trial, providing further compensation for financial and emotional harm.<sup>61</sup> Additionally, it issued a formal apology, acknowledging the scheme's failures and committing to justice for its victims<sup>3</sup>. Alongside these payments, the government issued a formal *apology*, acknowledging the scheme's failures and attempting to deliver justice to its victims.<sup>62</sup>

Third, the establishment of the Royal Commission into Robodebt in 2022 demonstrated the government's commitment to accountability. The commission's final report, released in 2023, underscored five key values —'lawfulness, fairness, rationality, openness or transparency, and efficiency'—as essential in the design of automated systems.<sup>63</sup> It emphasized the importance of balancing technological efficiency with fairness and compassion, particularly for vulnerable populations impacted by such systems.<sup>64</sup>

The report sets out 56 recommendations, emphasizing the importance of consulting legal and social policy experts, strengthening safeguards to protect recipients, and

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<sup>56</sup> *Report* (n at 487 (stated 'In the social security context, human oversight of the system is needed to mitigate the risk of error: "in some cases partial automation with the final decision made by a human arbiter is the ideal outcome."')

<sup>57</sup> *Ibid.* at 479.

<sup>58</sup> Melissa Coade, 'Shorten lauds Services Australia culture of 'speaking up' and being heard', *The Mandarin* (online, 11 December, 2024) <<https://www.themandarin.com.au/283475-shorten-lauds-services-australia-culture-of-speaking-up-and-being-heard/>>.

<sup>59</sup> *Report* (n at xxix).

<sup>60</sup> *Ibid.* at xxix.

<sup>61</sup> See Luke Henriques-Gomes, 'Robodebt class action: Coalition agrees to pay \$1.2bn to settle lawsuit', *The Guardian* (online, 16 Nov 2020) <<https://www.theguardian.com/australia-news/2020/nov/16/robodebt-class-action-coalition-agrees-to-pay-12bn-to-settle-lawsuit>>. ('Some 400,000 Australians will share \$112m in extra compensation')

<sup>62</sup> See *Report* (n at v. (In June 2020 then prime minister, the Hon Scott Morrison MP, apologised for the Scheme.)

<sup>63</sup> *Ibid.* at 373 and 479 (the ARC Report stated: 'the five values identified by the ARC that should be observed in the design and operation of administrative decision-making processes – lawfulness; fairness; rationality; openness or transparency; and efficiency')

<sup>64</sup> *Ibid.* at 485.

ensuring that compliance initiatives are both fair and equitable.<sup>65</sup> While the majority of these recommendations can be implemented through administrative actions by the Executive branch, the report also highlights the necessity of significant legislative reforms. The Australian Government has formally accepted, or accepted in principle, all 56 recommendations.

In response, these recommendations have driven legislative efforts to enhance oversight and accountability in the use of automated systems within government services. To address recommendations 21.1 and 21.2 from the *Report of the Royal Commission into the Robodebt Scheme*,<sup>66</sup> the *Oversight Legislation Amendment (Robodebt Royal Commission Response and Other Measures) Bill 2024* was introduced to the Australian Parliament in October 2024. This bill aims to strengthen the powers of oversight bodies, such as the Commonwealth Ombudsman and the Inspector-General of Taxation, to ensure robust scrutiny of automated decision-making processes.<sup>67</sup> The proposed reforms include the creation of a statutory duty requiring agency heads and their staff to make every effort to assist the Ombudsman and the IGTO in their work (Recommendation 21.1: Statutory duty to assist).<sup>68</sup> Additionally, the reforms expand the authority of these oversight bodies by obligating agencies to provide all necessary facilities and assistance, ensuring full access to agency records (Recommendation 21.2: Another power to obtain information).<sup>69</sup>

These legislative changes signify a critical step toward reinforcing accountability and ensuring that automated systems in public administration operate transparently, ethically, and effectively.

Collectively, these responses reflect the government's efforts to address the systemic failures of the Robodebt scheme. By acknowledging its mistakes and implementing reforms, the government has sought to rebuild public trust and lay the foundation for a more transparent, accountable, and compassionate welfare administration system.

### III. Overview of China's Social Welfare System & Applications of Its Automated Decision-Making System

China's social welfare system is a complex and evolving structure that has grown alongside the nation's rapid economic development. It operates under a hybrid model that combines central government oversight with significant local autonomy. While the system has made remarkable progress in expanding coverage and incorporating technological advancements, challenges remain in ensuring equity, transparency, and public trust. Unlike Australia, which operates with a relatively unified standard

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<sup>65</sup> Department of the Prime Minister and Cabinet Commonwealth of Australia, *Royal Commission into the Robodebt Scheme - Government Response*, November 2023).at 3.(The Australian Government has accepted or accepted in principle all 56 recommendations)

<sup>66</sup> Edward Fellows (Australia), Attorney General, *Oversight Legislation Amendment (Robodebt Royal Commission Response and Other Measures) Bill No 22, 2024-25 of 2024*, 23 October 2024).

<sup>67</sup> Oversight Legislation Amendment (Robodebt Royal Commission Response and Other Measures) Bill 2024 (Australia) ('Oversight Legislation Amendment (Robodebt Royal Commission Response and Other Measures) Bill 2024').

<sup>68</sup> Fellows (n

<sup>69</sup> Ibid.

for welfare thresholds across the country, China's approach reflects its vast economic disparities and varying levels of development across regions. This section examines the authorities responsible for welfare distribution, the income thresholds for accessing allowances, the use of automated decision-making (ADM) systems, and both the system's successful experiences and its potential limitations and risks.

### 3.1. China's Social Welfare System for Low Income

#### 3.1.1. Authorities in Charge of Welfare Distribution

China's social welfare system is administered through a multi-tiered framework involving central, provincial, municipal, and local governments. At the apex, the Ministry of Civil Affairs (MCA) oversees national welfare policies and ensures consistency in implementation across the country. The MCA plays a central role in designing and coordinating programs such as social assistance, elder care, and welfare for persons with disabilities.<sup>70</sup>

Provincial and municipal governments act as intermediaries, adapting national policies to regional contexts. They manage funding allocations and oversee the implementation of programs within their jurisdictions.<sup>71</sup> For instance, urban welfare programs may differ significantly from those in rural areas due to varying economic conditions and population demographics.<sup>72</sup> At the grassroots level, local governments, sub-district offices, and village committees are responsible for implementing welfare programs.<sup>73</sup> Their duties include processing applications, assessing household incomes, and distributing benefits.<sup>74</sup> These local entities are often the primary points of contact for citizens seeking assistance.<sup>75</sup>

China's dual governance structure allows for flexibility in addressing regional disparities but also creates inconsistencies in service delivery. While affluent regions can allocate more resources to welfare programs, underdeveloped areas often struggle to meet basic needs, leading to uneven access and coverage.<sup>76</sup>

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<sup>70</sup> State Council of China, 'Ministry of Civil Affairs of the People's Republic of China', (Blog Post) <[https://english.www.gov.cn/state\\_council/2014/09/09/content\\_281474986284128.htm](https://english.www.gov.cn/state_council/2014/09/09/content_281474986284128.htm)>.

<sup>71</sup> Kerry Ratigan, 'Disaggregating the Developing Welfare State: Provincial Social Policy Regimes in China' (Pt Elsevier Ltd) (2017) 98 *World development* 467-484.at 469.

<sup>72</sup> See Shen-cheng Wang, Kin-sun Chan and Ke-qing Han, 'Impacts of social welfare system on the employment status of low-income groups in urban China' (Pt Emerald Group Publishing Limited) (2019) 22(2) *Public administration and policy* 125-137.

<sup>73</sup> Ministry of Civil Affairs of the People's Republic of China, 民政部关于印发《最低生活保障审核确认办法》的通知 [Notice of the Ministry of Civil Affairs on Issuing the "Minimum Living Security Review and Confirmation Methods"] [in Chinese], No 57, June 11, 2021. Art 4 (stated 'Applications for minimum living allowance shall be submitted on a household basis. The applicant household shall designate one member of the household who lives together as the applicant, and a written application shall be submitted to the local township (town) government (subdistrict) office at the place of household registration. In regions where online applications are accepted, applications may also be submitted via the internet.')

<sup>74</sup> Ibid.art 10.

<sup>75</sup> Ibid. See also David S. G. Goodman, 'Local Social Governance in China: Spatial politics and social welfare' (2024).at 11.

<sup>76</sup> Kristin Dalen et al, 'Welfare and Social Policy in China: Building a New Welfare State', (Palgrave Macmillan, 2020) 267-290.at 272. (stated 'After the reform and opening-up period, uneven economic growth and social contradictions became increasingly prominent.')

### 3.1.2. Threshold of Low Income to Access Allowances: Central vs Local

Article 14 of the Chinese Constitution states that the government “builds and improves a welfare system that corresponds with the level of economic development.” Unlike Australia, a country of 27 million people with relatively uniform economic conditions across states,<sup>77</sup> China, with its 1.41 billion population, exhibits vast economic disparities across its provinces.<sup>78</sup> This makes implementing a unified nationwide threshold for low-income allowance eligibility impractical and necessitates a more flexible, region-specific approach.

#### 3.1.2.1 General Approach by the Central Government

The income thresholds for accessing welfare allowances in China are shaped by its tiered administrative system. National policies provide general guidelines,<sup>79</sup> but local governments have significant discretion in setting specific thresholds according to regional economic conditions. The *Minimum Livelihood Guarantee Scheme* (Dibao) serves as a prominent example of this decentralized approach.<sup>80</sup>

China's Dibao program, is a social assistance program aimed at providing financial support to individuals and households whose income falls below a certain threshold.<sup>81</sup> This threshold is determined by local governments and varies across regions to reflect the cost of living and economic conditions. It provides unconditional cash transfers to eligible individuals, ensuring a minimum standard of living.<sup>82</sup> Unlike Australia, where thresholds are often annual or fortnightly, China typically calculates income thresholds for low-income qualifications on a monthly basis.

The eligibility criteria for China's Minimum Livelihood Guarantee (Dibao) are primarily based on the monthly per capita income of the household, rather than annual income. Local governments regularly calculate and set Dibao standards for their jurisdictions based on income and expenditure data of urban and rural residents as well as local market price levels. If a household's monthly per capita income falls

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<sup>77</sup> Statista Research Department, 'Australia - Statistics & Facts', *Statista*, Apr 9, 2024) <<https://www.statista.com/topics/752/australia/>>.

<sup>78</sup> C. Textor, 'Demographics of China - statistics & facts', *Statista*, Jan 28, 2024) <<https://www.statista.com/topics/1276/population-in-china/>>.

<sup>79</sup> Ministry of Civil Affairs of the People's Republic of China (n See also State Council of China, 'China to introduce standard guidelines for identifying low-income residents', December 31, 2024) <

<sup>80</sup> See Jiwei Qian, 'Anti-Poverty in China: Minimum Livelihood Guarantee Scheme' (Pt East Asian Institute) (2013) 5(4) *East Asian policy (Singapore)* 53-64. at 58. (This work explores how social welfare programs like Dibao are designed with central guidelines but implemented with local discretion to address regional economic disparities.)

<sup>81</sup> Ibid. at 53.

<sup>82</sup> Asian Development Bank, 'Building Equitable Opportunities into Social Assistance in the People's Republic of China' (2014)(27) *ADB Briefs*.

below the local Dibao standard, and its savings, housing, and other assets meet the prescribed requirements, the household can apply for Dibao assistance.<sup>83</sup>

Based on an example provided by the State Council of China, if the Dibao standard in a given region is RMB 500 (AUD 100) per month and a household of three has a total monthly income of RMB 1,200 (AUD 240), the household's monthly per capita income would be RMB 400 (AUD 80), which is below the local Dibao standard. In this case, provided other asset conditions are met, the household would qualify to apply for Dibao assistance.<sup>84</sup>

Thus, the determination of Dibao eligibility is based on monthly per capita income, not annual income. Applicants must truthfully report the income and asset conditions of all cohabiting family members, including their capacity to provide or receive support.<sup>85</sup> Additionally, applicants must authorize the Civil Affairs Department to verify their declared income and asset conditions—such as savings, vehicles, and housing—through the social assistance household economic status verification mechanism.<sup>86</sup>

### 3.1.2.2. Diversified Approaches by Local Governments

This regional flexibility is a distinctive feature of China's welfare system, contrasting with countries like Australia, where economic uniformity across states allows for centralized welfare policies. Using Heilongjiang, Chongqing, and Beijing in 2024 as examples, local governments in China adapt thresholds for welfare eligibility based on their unique economic circumstances.

In Heilongjiang Province, one of China's least developed regions, the Civil Affairs Department and Finance Department announced that starting July 1, 2024, the urban Dibao standard would rise to RMB 710 (AUD 142) per person per month, while the rural Dibao standard would increase to RMB 517 (AUD 103.4) per person per month. The basic living standards for the most vulnerable individuals were set at 1.3 times the Dibao threshold and could not be lower than 2023 levels. Care-related standards were pegged to the local minimum wage, with thresholds set at one-fourth, one-sixth, and one-tenth of the minimum wage for full-care, semi-care, and self-care needs, respectively. Rural individuals under centralized care were assigned the same standards as urban residents needing care, emphasizing targeted financial assistance across six distinct groups.<sup>87</sup>

In Chongqing, a relatively developed municipality, applies a simpler system. From September 1, 2024, the Chongqing Civil Affairs Bureau and Finance Bureau

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<sup>83</sup> State Council of the People's Republic of China, ““低保”怎么申领？每月能领多少钱？一文看懂 [How to Apply for "Minimum Living Allowance"? How Much Can You Receive Monthly? Explained in One Article][in Chinese]”, (Blog Post, August 30, 2023) <[https://www.gov.cn/zhengce/202308/content\\_6901024.htm](https://www.gov.cn/zhengce/202308/content_6901024.htm)>.

<sup>84</sup> Ibid.

<sup>85</sup> Ministry of Civil Affairs of the People's Republic of China (n (MCA Notice 2021)

<sup>86</sup> State Council of the People's Republic of China (n

<sup>87</sup> Heilongjiang Provincial Department of Civil Affairs and the Provincial Department of Finance, 黑民规(2024) 5 号 省民政厅 省财政厅关于做好 2024 年提高城乡低保和特困人员救助供养标准有关工作的通知 [Notice from the Heilongjiang Provincial Department of Civil Affairs and the Provincial Department of Finance on Improving the Standards for Urban and Rural Minimum Living Allowance and Assistance for Extremely Poor Individuals in 2024y][in Chinese], No 5, June 18, 2024.

increased the urban Dibao standard from RMB 735 (AUD 147) to RMB 750 (AUD 150) per person per month, while the rural Dibao standard was raised from RMB 600 (AUD 120) to RMB 610 (AUD 122) per person per month. The thresholds reflect the economic disparities between urban and rural areas, focusing on two distinct groups.<sup>88</sup>

In contrast, in Beijing, one of China's most developed cities, the Dibao threshold was adjusted to RMB 1,450 (AUD 290) per person per month starting July 2024, according to the city's Civil Affairs Bureau and Finance Bureau.<sup>89</sup> Unlike Heilongjiang and Chongqing, Beijing does not differentiate between urban and rural residents, applying a unified threshold for all. This approach mirrors Australia's centralised welfare policies, where economic uniformity allows for consistent standards across the entire population.

These examples illustrate how local governments in China adapt welfare policies to align with their economic realities. Heilongjiang's multi-threshold approach addresses its diverse and resource-constrained population, Chongqing's dual thresholds reflect its urban-rural economic divide, and Beijing's unified standard demonstrates the advantages of a highly developed economy in simplifying welfare administration.

While the discretion afforded to local governments allows for tailored responses to regional economic disparities, it also presents challenges. Wealthier regions can set higher thresholds and provide more generous welfare provisions, whereas poorer regions often impose stricter eligibility criteria due to budget constraints. This disparity risks exacerbating inequality and undermining the government's goal of achieving a uniform standard of living nationwide.

Moreover, the diverse approaches adopted by local governments make the implementation of a centralized, Australia-style single ADM (automated decision-making) system in welfare administration exceedingly difficult. The lack of uniformity across regions necessitates highly localized systems, further complicating efforts toward centralized standardization.

### **3.1.3 Application of Automated Decision-Making Systems in Welfare Systems: Digital Integration and Data Sharing**

China has embraced digital technology to modernize its social welfare system, integrating automated decision-making (ADM) systems to enhance efficiency and

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<sup>88</sup> Chongqing Municipal Civil Affairs Bureau, 重庆市民政局重庆市财政局关于提高城乡最低生活保障等社会救助保障标准的通知 [Notice from Chongqing Municipal Civil Affairs Bureau and Chongqing Municipal Finance Bureau on Raising Minimum Living Allowance and Other Social Assistance Standards in Urban and Rural Areas][in Chinese], No 9, Aug 30, 2024.

<sup>89</sup> Beijing Municipal Civil Affairs Bureau and Beijing Municipal Finance Bureau, 北京市民政局北京市财政局关于调整本市最低生活保障标准的通知 [Notice from Beijing Municipal Civil Affairs Bureau and Beijing Municipal Finance Bureau on Adjusting the Minimum Living Allowance Standard in the City][in Chinese], No 80, Aug 21, 2024.

accuracy. These systems are pivotal to China's broader Digital China strategy, which emphasizes the use of technology in governance and public service delivery.<sup>90</sup>

China's integration of Automated Decision-Making (ADM) technologies into its welfare systems reflects a commitment to enhancing efficiency and precision in social assistance. Two notable initiatives in this effort are the Ministry of Civil Affairs' *National Low-Income Population Dynamic Monitoring Platform (Dibao Monitoring Platform)* and the *Resident Household Economic Status Verification Mechanism (Minsheng Verification Mechanism)*. These platforms utilise big data and digital tools to monitor and assess the economic status of residents, ensuring the timely and accurate distribution of welfare benefits.

### 3.1.3.1. Dibao Monitoring Platform

The Dibao Monitoring Platform represents a pivotal initiative by the Chinese government to enhance social assistance and safeguard the well-being of its citizens. Since 2021, the Ministry of Civil Affairs has overseen the development of this platform, which dynamically monitors the difficulties faced by various low-income groups.<sup>91</sup> It identifies individuals and families at risk while conducting comprehensive assessments of the severity and types of their difficulties.<sup>92</sup>

In 2023, the Ministry of Civil Affairs, alongside other ministries, jointly issued the *Opinions on Strengthening Dynamic Monitoring of Low-Income Populations and Enhancing Tiered and Classified Social Assistance (Opinions 2023)*.<sup>93</sup> These *Opinions* mandate the Ministry of Civil Affairs to take the lead in building such a monitoring platform. Once operational, the platform will expand its functionality by setting scientifically grounded early-warning indicators and offering information query services and demand-push notifications to support tiered and classified social assistance.<sup>94</sup> This system is designed to enable more precise identification of eligible individuals, improve dynamic monitoring, generate accurate early-warning information, and ensure social assistance policies are better targeted to address the needs of low-income populations.<sup>95</sup>

As of October 2023, the platform had collected basic information on over 66 million low-income individuals, comprising approximately 4.7% of China's total population. The database includes nearly 40 million 'minimum living allowance' ('Dibao') recipients, over 4.6 million individuals in extreme poverty, more than 6 million

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<sup>90</sup> Rebecca Arcesati, 'China's rise in digital governance - Deploying technology to deliver public goods at home and abroad', March 2022) <[https://merics.org/sites/default/files/2022-03/MERICS-Primer-Digital-Governance-2021\\_final.pdf](https://merics.org/sites/default/files/2022-03/MERICS-Primer-Digital-Governance-2021_final.pdf)>.

<sup>91</sup> Changyu Li, '低收入人口数据库已建成 [The low-income population database has been established] [in Chinese]', *China Daily* (online, Jan 27, 2022) <[http://paper.people.com.cn/rmrb/html/2022-01/27/nw.D110000renmrb\\_20220127\\_6-07.htm](http://paper.people.com.cn/rmrb/html/2022-01/27/nw.D110000renmrb_20220127_6-07.htm)>.

<sup>92</sup> Ibid.

<sup>93</sup> General Office of the State Council of P.R. China, 国务院办公厅转发民政部等单位《关于加强低收入人口动态监测做好分层分类社会救助工作的意见》的通知 [Notice from the General Office of the State Council to the Ministry of Civil Affairs and Relevant Departments on Implementing the "Opinions on Strengthening Dynamic Monitoring of Low-Income Populations and Enhancing Tiered and Classified Social Assistance"] [in Chinese], Oct 19, 2023.

<sup>94</sup> Ibid.section 3.1 of the *Opinions 2023*.

<sup>95</sup> Ibid.section 4 of the *Opinions 2023*.

members of households on the brink of qualifying for minimum living allowances, over 3 million individuals under poverty prevention monitoring, and approximately 13 million other low-income individuals.<sup>96</sup>

To further implement the objectives of Opinions 2023, the Ministry of Civil Affairs (MCA) issued the *Notice on Strengthening the Identification and Dynamic Monitoring of Low-Income Populations* (Notice 2024) in April 2024.<sup>97</sup> Firstly, this notice *expanded the scope* of data collection and monitoring for low-income populations. Section 1 directed local authorities to not only identify Dibao recipients and individuals in extreme poverty but also comprehensively identify households on the brink of qualifying for Dibao and those facing rigid expenditure difficulties.<sup>98</sup> Section 2 broadened the monitoring scope further by requiring a risk-prevention approach. On the one hand, the monitoring platform must include individuals under poverty prevention monitoring, applicants ineligible for Dibao or extreme poverty assistance, those who exited these programs within two years, and other individuals with potential difficulties as identified by local governments.<sup>99</sup> On the other hand, the platform's functionality must be enhanced by expanding the content to verify household economic status and gradually increase data items. This includes introducing functional modules for labour capacity, labour conditions, labour willingness, water safety, and housing safety while also improving the monitoring and early-warning system with metrics for medical expenses, schooling, and disabilities.<sup>100</sup> Secondly, *Notice 2024* emphasised strengthening *data integration, data sharing, and timely responses and feedback* across relevant governmental authorities. It outlined the importance of establishing a '*structured workflow*' involving tiered management, dynamic monitoring, need-based notifications, and feedback. Information regarding medical, education, housing, employment, and industrial support needs must be promptly forwarded to relevant departments. These departments are required to respond and provide feedback, forming a closed-loop management system characterised by a 'one household (or individual), one assistance chain' approach.<sup>101</sup>

### 3.1.3.2. Minsheng Verification Mechanism

The Minsheng Verification Mechanism plays a crucial role in verifying the economic conditions of households. Regarding its legal foundation, in October 2008, the State Council approved the issuance of the Measures for the Identification of Low-Income Urban Families by the Ministry of Civil Affairs, in collaboration with the National Development and Reform Commission and ten other ministries.<sup>102</sup> This

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<sup>96</sup> The State Council of P.R. China, '全国低收入人口动态监测信息平台建设已取得积极成效 [The construction of the National Low-Income Population Dynamic Monitoring Information Platform has achieved positive results]', *China Government Network (China's Official Government Website)* (Blog Post, Oct 25, 2023) <[https://www.gov.cn/xinwen/jdzc/202310/content\\_6912006.htm](https://www.gov.cn/xinwen/jdzc/202310/content_6912006.htm)>.

<sup>97</sup> Ministry of Civil Affairs of the People's Republic of China, 民政部办公厅关于加强低收入人口认定和动态监测工作的通知 [Notice from the General Office of the Ministry of Civil Affairs on Strengthening the Identification and Dynamic Monitoring of Low-Income Populations][in Chinese], No 31, April 26, 2024.

<sup>98</sup> Ibid. Section 1 of the Notice 2024.

<sup>99</sup> Ibid. Section 2 of the Notice 2024.

<sup>100</sup> Ibid. Section 2 of the Notice 2024.

<sup>101</sup> Ibid. Section 2 of the Notice 2024.

<sup>102</sup> alongside other ministries Ministry of Civil Affairs of the People's Republic of China, '关于印发《城市低收入家庭认定办法》的通知 [Notice on Issuing the "Measures for the Identification of Low-Income Urban

document explicitly assigned civil affairs departments at all levels the responsibility for managing the verification of income information for low-income urban families.<sup>103</sup>

In September 2012, the *Opinions of the State Council on Further Strengthening and Improving the Work of Minimum Living Security* called for the establishment of a cross-departmental, multi-layered, and information-sharing mechanism to verify the economic status of families applying for assistance. It emphasized the need to enhance institutional frameworks and information verification platforms to ensure that social assistance beneficiaries are identified accurately, efficiently, and fairly.<sup>104</sup> Moreover, in October 2012, the central government approved the establishment of the *Center for Monitoring and Verification of Low-Income Families* under the Ministry of Civil Affairs.<sup>105</sup> This center was tasked with establishing and maintaining a national database on the economic conditions of low-income families (e.g. *Dibao Monitoring Platform*), conducting income inquiries and verifications (e.g. *Minsheng Verification Mechanism*), and undertaking policy research, public outreach, communication, and training related to low-income family programs.<sup>106</sup>

The *Interim Measures for Social Assistance*, effective May 1, 2014, further solidified the legal status of the verification mechanism. It required civil affairs departments at the county level and above to establish platforms for verifying the economic status of families applying for or already receiving social assistance, providing a robust basis for the review and identification of beneficiaries.<sup>107</sup>

With the advancement of digital technology, automated decision-making (ADM) systems have become an essential part of China's household economic condition verification mechanisms, forming a key component of the *Digital China* initiative under the *Gold People Project*.<sup>108</sup> To address their unique social and economic circumstances, many provinces and cities have developed customized verification systems and begun leveraging digital technology to enhance their effectiveness.

For example, Guangdong Province has implemented the *Baseline Livelihood Informatization Verification Management System*, which utilizes big data and ADM technology to assess the economic status of social assistance applicants and automatically generate warning notices for anomalies. By August 2023, this system had flagged 856,500 cases that did not meet the eligibility criteria for assistance. Acting on these system alerts, local civil affairs departments conducted thorough in-

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Families"] [in Chinese] in 关于印发《城市低收入家庭认定办法》的通知 [Notice on Issuing the "Measures for the Identification of Low-Income Urban Families"] [in Chinese], No 156, Oct 22, 2008.

<sup>103</sup> Ibid.

<sup>104</sup> State Council of China, 国务院关于加强和改进最低生活保障工作的意见 [Opinions of the State Council on Further Strengthening and Improving the Work of Minimum Living Security] [in Chinese], No 45.

<sup>105</sup> Centre for Monitoring and Verification of Low Income Families, 'Background of the Establishment of the Center [中心成立背景]', Jul 29, 2022) <<https://www.dsrrd.gov.cn/n461/c14883/content.html>>.

<sup>106</sup> Centre for Monitoring and Verification of Low Income Families, 'Background of the Establishment of the Center [中心职能及机构设置]', Jul 29, 2022) <<https://www.dsrrd.gov.cn/n461/c14885/content.html>>.

<sup>107</sup> 社会救助暂行办法 2014 (2019 修订) Revised Interim Measures for Social Assistance 2014 (2019 Revision) [in Chinese] 2014 ('社会救助暂行办法').

<sup>108</sup> General Office of the Ministry of Civil Affairs of P.R. China, 民政部办公厅关于印发《金民工程一期项目试点工作方案》的通知 [Notice of the General Office of the Ministry of Civil Affairs on Issuing the "Pilot Work Plan for Phase I of the Jinmin Project"] [in Chinese], Aug 2, 2019.

home investigations for each flagged case, promptly removing ineligible beneficiaries from social assistance programs.<sup>109</sup>

In this context, the system bears some resemblance to Australia's Robodebt scheme. However, significant differences set the two systems apart, particularly in the areas of human oversight and proactive engagement. These distinctions, along with their broader implications, will be further explored in the next section.

### 3.2. China's 'Robodebt Plus Robocredit' Mechanism in Guangdong

In line with the requirements set by the State Council of China, many provinces and cities have developed both the Dibao monitoring platform and the Minsheng Verification Mechanism, incorporating digital technologies such as ADM-empowered information systems tailored to their unique social, economic, and technological circumstances.

According to a 2023 notice from the General Office of the Ministry of Civil Affairs, 54 regions across the country launched a two-year pilot program for social assistance reform and innovation.<sup>110</sup> Many of these regions explored the application of digital technologies in social assistance, including the establishment of comprehensive assessment systems for vulnerable groups and the promotion of interconnectivity and information sharing within social assistance systems. In these pilot programs, information systems were utilized to conduct comprehensive assessments and dynamic monitoring of the economic conditions of vulnerable households, significantly enhancing the scientific rigor and fairness of social assistance efforts.<sup>111</sup> Guangdong Province, as one of China's most developed regions, stands out as a prominent example of successful implementation and innovation in this field.

#### 3.2.1. General Achievements of Guangdong Model

To make social assistance applications more convenient, efficient, and precise for vulnerable groups, the Guangdong Provincial Department of Civil Affairs developed the *Baseline Livelihood Informatization Verification Management System* (referred to hereafter as "*Guangdong Minsheng Verification Mechanism*" for consistency with the national schemes introduced above) and the *Dynamic Monitoring System for Low-Income Populations* (referred to hereafter as the "*Guangdong Dibao Monitoring Platform*" for consistency with national schemes). These systems, created as part of the *Digital Government Reform and Construction Plan*, have been implemented across 1,745 units at the provincial, municipal, county, and township

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<sup>109</sup> 广东省民政厅 [Guangdong Provincial Department of Civil Affairs], '广东民政：大数据助力社会救助更精准更全面' [Guangdong Civil Affairs: Big Data Enhances the Precision and Coverage of Social Assistance] [in Chinese], 广东省政务服务和管理局 [Guangdong Provincial Government Service and Data Management Bureau], Aug 28, 2023) <[https://zfsg.gd.gov.cn/xxfb/dtxw/content/post\\_4243712.html](https://zfsg.gd.gov.cn/xxfb/dtxw/content/post_4243712.html)>.

<sup>110</sup> Centre for Monitoring and Verification of Low Income Families [民政部低收入家庭认定指导中心], Notice from the General Office of the Ministry of Civil Affairs on the Social Assistance Reform and Innovation Pilot Program and the Innovation Practices in the Field of Social Assistance for 2022 [民政部办公厅关于社会救助改革创新试点和 2022 年度社会救助领域创新实践活动有关情况的通报] [in Chinese], No 4, Feb 3, 2023.

<sup>111</sup> Ibid. section 1.2 of the Notice.

levels, providing comprehensive support to civil affairs departments throughout the province.<sup>112</sup>

These two systems integrate data from 12 government departments, 28 commercial banks, securities institutions, and other entities, along with 18 categories of information on vulnerable populations. Together, they monitor 4.05 million low-income individuals, offering real-time alerts and enabling precise identification of social assistance recipients. This has contributed to building a comprehensive, multi-layered, and efficient social assistance framework supported by data.<sup>113</sup>

Since the launch of the *Guangdong Dibao Monitoring Platform*, 128,800 alerts have been issued, resulting in home investigations. From these, 13,470 individuals were included in civil assistance programs, while 11,240 were referred to other departments for help. In 2023, the *Guangdong Minsheng Verification Mechanism* produced 1,073,600 reports on the economic conditions of 2.62 million social assistance applicants. Applicants *only* need to provide their ID and an authorization form to apply for assistance. As of 2023, Guangdong allocated RMB 8.45 billion (AUD 1.69 billion) in assistance funds, supporting 1.36 million low-income individuals and 228,900 people in extreme poverty.<sup>114</sup>

### 3.2.2. Guangdong's Robodebt: Automated Warnings

In addressing overpayment detection, similar to Australia's Robodebt scheme, the *Guangdong Minsheng Verification Mechanism* plays a critical role in ensuring accurate social assistance implementation. To date, it has flagged 856,500 anomalies where applicants did not meet eligibility criteria. The provincial Civil Affairs Department requires local staff to investigate each alert through home visits, ensuring timely removal of ineligible beneficiaries. Whether for re-evaluating current recipients or reviewing new applications, the system provides automated warnings when anomalies are detected.<sup>115</sup>

For example, a lady in Taishan City had been receiving low-income support since June 2017. A routine system check in June 2023 revealed that her household owned two properties, making her ineligible. A follow-up investigation confirmed that her family's average monthly income and additional rental property exceeded the threshold. Upon explanation by the staff, the lady accepted the decision to withdraw from the program.<sup>116</sup>

In another case, a man in Shaoguan City applied for assistance in July 2023. The *Guangdong Minsheng Verification Mechanism* revealed he owned two properties. Although he claimed one was used by a family member, further investigation confirmed he held ownership of both. After an explanation of the policies, he agreed to withdraw his application.<sup>117</sup>

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<sup>112</sup> 广东省民政厅 [Guangdong Provincial Department of Civil Affairs] (n

<sup>113</sup> Ibid.

<sup>114</sup> Ibid.

<sup>115</sup> Ibid.

<sup>116</sup> Ibid.

<sup>117</sup> Ibid.

These examples highlight how the *Guangdong Minsheng Verification Mechanism*, through data-sharing and direct bank inquiries, has addressed challenges such as reliance on self-reported information. The system also mandates biannual random re-evaluations of recipients to detect income or asset changes. If a household no longer qualifies, the system issues alerts for timely follow-up investigations and adjustments.<sup>118</sup>

### **3.2.3. Guangdong's RoboCredit: Proactive Approach for Bridging the Digital Divide**

Beyond functions similar to Australia's Robodebt scheme, which focuses on overpayment recovery, Guangdong's welfare monitoring and verification systems include an automated decision-making (ADM) capability that serves the opposite purpose: proactively identifying eligible individuals who have not applied for assistance. This function, referred to here as "*RoboCredit*", aims to reach individuals often excluded from assistance due to a lack of awareness or an inability to navigate social welfare policies.

Guangdong has established open application channels, allowing individuals to apply for assistance at any service window within the province or online through the "Yue Sheng Shi" ('Guangdong Matters') mini-program. However, many eligible households still remain unassisted due to limited knowledge of available policies, social stigma, or a lack of capability to seek help.<sup>119</sup>

To address this, the *Guangdong Dibao Monitoring Platform* was launched in 2021. It integrates data from 12 departments to monitor 4.05 million low-income individuals, using indicators to assign a five-level alert system (red, orange, yellow, blue, green). Local civil affairs departments act on these alerts through home investigations, proactively including eligible individuals in assistance programs or referring them to relevant departments for support.<sup>120</sup>

For instance, in June 2023, the system flagged Ms. Lin, a resident of a rural village in Qingyuan City. Despite severe financial strain due to her disability, her family had not applied for assistance. The system detected a new school enrollment in her household, triggering a green-level alert. Staff visited her family and calculated their income, finding it fell within the threshold for low-income assistance. With guidance, Ms. Lin was approved for monthly assistance and additional disability allowances.<sup>121</sup>

### **3.2.4. Human Oversight: Online Alerts with Offline Verification**

While Guangdong's social assistance systems rely heavily on advanced technology, human oversight plays a critical role in ensuring accuracy, fairness, and responsiveness. The province has developed a comprehensive mechanism that integrates "big data" for automated alerts with "on-the-ground work" for verification

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<sup>118</sup> Ibid.

<sup>119</sup> Ibid.

<sup>120</sup> Ibid.

<sup>121</sup> Ibid.

and intervention, creating an effective balance between technology and human judgment<sup>122</sup> —an element notably absent in the Robodebt scheme.

The *Guangdong Minsheng Verification Mechanism* automatically screens applicants and existing beneficiaries by cross-checking economic data and assets, issuing alerts for anomalies or ineligibilities. However, these alerts are not treated as definitive decisions. Instead, grassroots civil affairs staff conduct in-person investigations to verify the flagged information, ensuring that no eligible individual is wrongfully excluded and that no ineligible beneficiary remains in the system.<sup>123</sup>

For example, in January 2023, Mr. Chen from Yunan District applied for low-income assistance. The Verification System flagged him for owning a registered business, which initially disqualified him. Upon a home visit, social workers discovered the “business” was a small breakfast shop run by Mr. Chen and his wife, with a modest income insufficient to support their family of eight. After recalculating his household income based on comprehensive evaluation indicators, Mr. Chen’s family was found eligible and began receiving RMB1,530 (AUD 306) in monthly assistance starting February 2023.<sup>124</sup>

### ***3.3 Limits, Benefits, and Risks of Automated Systems in China's Welfare System – Decentralized Policy Approach vs. Centralized Data System***

#### **3.3.1. Inherent Challenges & Decentralized Policy Approach: Diversity vs. Inequality**

China, with its population of 1.4 billion, faces the intricate challenge of designing welfare policies that address the nation's pronounced economic and digital divides. These disparities create distinct regional needs, requiring a decentralized approach to tailor welfare policies to local economic, social, and technological circumstances. However, this flexibility often results in uneven access to welfare services, raising concerns about equity and fairness.

Economic inequality is one of the most pressing challenges. In 2021, urban residents in China had a per capita disposable income of 47,412 yuan, while rural residents earned only 18,931 yuan, meaning urban incomes were approximately 2.5 times higher than rural incomes.<sup>125</sup> This stark wealth disparity reflects the uneven development between urban and rural areas, translating into disparities in access to resources, public services, and welfare programs. Consequently, many rural communities face systemic barriers, perpetuating cycles of poverty and limited upward mobility.

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<sup>122</sup> Ibid.

<sup>123</sup> Ibid.

<sup>124</sup> Ibid.

<sup>125</sup> National Bureau of Statistics, 'Income & spending 2021', *China Services Info - Your Online Guide to Govt Services*, Jan 20, 2022) <<https://govt.chinadaily.com.cn/s/202201/20/WS634fc4eb498ea274927a60d1/income-spending-2021.html>>.

Compounding this issue is the digital divide, which continues to pose significant challenges despite substantial investments in digital infrastructure. As of June 2024, the internet penetration rate in rural areas was 63.8%, significantly lower than the 85.3% observed in urban regions.<sup>126</sup> Additionally, older adults are disproportionately affected, with individuals aged 60 and above accounting for 39.8% of the 317 million non-internet users in China as of December 2023.<sup>127</sup> This exclusion limits access to digital welfare systems, leaving vulnerable populations underserved. While automation has streamlined welfare delivery, it risks reinforcing inequalities without deliberate efforts to improve digital literacy and ensure equitable access to technology.

Balancing regional diversity with nationwide equity is essential to creating an inclusive welfare system. By addressing economic and digital divides, China can ensure its welfare policies support all segments of the population and drive sustainable progress.

### **3.3.2. Benefits and Risks of Centralized Data System: Transparency vs. Privacy Risks**

While China's welfare policies, including thresholds for accessing Dibao allowances, are decentralized, the administration of resident data within welfare monitoring and verification systems is highly centralized. This centralization is managed by the *Centre for Monitoring and Verification of Low-Income Families* under the Ministry of Civil Affairs (MCA).

Centralized data systems can enhance transparency and efficiency in welfare distribution. However, they also raise significant privacy concerns. The aggregation of sensitive information, such as financial records and household details, increases the risk of data breaches and misuse. In response, the Chinese government has introduced data protection laws, including the Personal Information Protection Law (PIPL) which was adopted on August 20, 2021, and came into effect on November 1, 2021. This law has been applied in various cases of data breaches, including those involving government-related systems. For instance, in September 2023, a Shanghai-based government information system service company suffered a major data breach during internet testing. Due to inadequate security measures, over 15,000 personal records were leaked and later offered for sale on foreign hacker forum.<sup>128</sup> In response, the Shanghai Internet regulator imposed administrative penalties on the company, including the immediate removal of affected web pages, closure of related cloud service ports, and a financial fine.<sup>129</sup> This incident highlights the critical

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<sup>126</sup> Lai Lin Thomala, 'Internet adoption rate in rural China 2014-2024', *Statista*, Sep 27, 2024) <<https://www.statista.com/statistics/1062706/china-internet-penetration-rate-rural-areas/>>.

<sup>127</sup> Wanjun Lu, 'The impact of internet usage on the mental health of older adults in China: empirical analysis from a multi-dimensional perspective' (2024) 13 *Frontiers in public health* 1.at 2.

<sup>128</sup> Shiwen Chen, 'Citizens' personal information disclosed and sold overseas; a Shanghai government information system service company faces administrative penalties [公民个人信息遭境外披露兜售, 上海市一政务信息系统技术服务公司被行政处罚][in Chinese]', *CCTV Legal News*, September 15, 2023) <<https://news.cctv.com/2023/09/15/ARTI9iO75vnfCiJ7jqpxkOIP230915.shtml>>.

<sup>129</sup> *Ibid.*

importance of robust cybersecurity practices, particularly for organizations handling sensitive government data.

## **IV. Future Use of Welfare-Related ADM Systems: Insights from Australia and China**

### ***4.1. Integrating Robodebt and RoboCredit Functions in Automated Decision-Making Systems***

The future of welfare administration lies in leveraging the complementary strengths of Robodebt and RoboCredit within automated decision-making (ADM) systems. Robodebt emphasizes fiscal responsibility, focusing on identifying and recovering overpayments to ensure that government resources are used efficiently and not subject to misuse. In contrast, RoboCredit prioritizes inclusivity by proactively identifying individuals who qualify for assistance but are excluded due to lack of awareness, systemic barriers, or stigma.

By integrating these two approaches, ADM systems can achieve a dual purpose: safeguarding public funds while promoting equity and inclusivity. For instance, ADM tools could utilize big data analytics to detect anomalies in income or asset reporting for overpayment recovery while simultaneously scanning for indicators of eligibility among underserved populations. This dual functionality ensures a comprehensive approach to welfare management, addressing both resource protection and social support.

The proactive element of RoboCredit ensures that vulnerable individuals are not overlooked, particularly those who may struggle with navigating complex application processes or face social stigma. At the same time, the vigilance of Robodebt maintains the integrity of the welfare system, preventing fraud and ensuring accountability. ADM systems like Guangdong's Dibao Monitoring Platform demonstrate how this balance can be achieved effectively by integrating data from multiple departments and employing a tiered alert system to prioritize resources and actions.<sup>130</sup>

By combining the strengths of Robodebt and RoboCredit into a unified ADM framework, future welfare systems can address the dual objectives of efficiency and equity, fostering public trust while ensuring no one is left behind. This balanced approach can serve as a model for global welfare administration, leveraging technology to support both government sustainability and individual well-being.

### ***4.2. Human Oversight in ADM Systems – Dual System***

Australia's Robodebt scheme offers valuable lessons on the risks and challenges of implementing automated decision-making (ADM) systems in welfare administration. While its objectives of cost savings and operational efficiency were well-intentioned, the scheme's failures underscore the dangers of excessive reliance on automation without proper safeguards or human oversight. These shortcomings

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<sup>130</sup> See Part 3 of the article.

highlight the necessity of integrating human judgment into ADM frameworks to prevent errors and ensure equitable outcomes.

To address such pitfalls, future regulators must embed robust human oversight into ADM systems.<sup>131</sup> China's welfare administration provides a compelling example, particularly *Guangdong's Minsheng Verification Mechanism*, which effectively combines advanced technology with human intervention to promote fairness and adaptability. Automated alerts powered by big data enhance efficiency by rapidly processing vast amounts of information and identifying anomalies or ineligibilities. However, unlike fully automated systems, China's approach ensures that these alerts are not treated as conclusive decisions. Instead, field investigations and personalized follow-ups are conducted to verify flagged cases, minimizing errors such as wrongful exclusions or unjustified inclusions.

Human oversight is essential in addressing the complexities and nuances that automation may fail to capture. Grassroots civil affairs staff play a pivotal role in refining automated findings and adapting decisions to individual circumstances. For instance, as highlighted earlier, the case of Mr. Chen from Yunan District demonstrates how manual verification corrected an initial automated disqualification, ultimately ensuring that his family received the assistance they needed.<sup>132</sup>

This dual system—integrating online alerts with offline verification—reduces the risk of systemic errors, upholds fairness, and fosters public trust. By striking a balance between technological efficiency and human judgment, China's ADM systems present a flexible and equitable model. This approach avoids the pitfalls of over-reliance on automation while maintaining accountability and a commitment to social responsibility, serving as an example for welfare administrators globally.

### ***4.3 Transparency, Due Process, Review Mechanisms, and Public Trust***

Transparency and accountability are critical to the success of Automated Decision-Making (ADM) systems in welfare administration. However, challenges such as the lack of public consultation during system design, opaque decision-making processes, and inadequate review mechanisms undermine confidence in these systems and their outcomes. Addressing these gaps is essential for building trust and ensuring equitable welfare delivery.

One major issue is the absence of public input during the design phase of ADM systems. For example, the Robodebt scheme in Australia lacked stakeholder consultation, leading to calculation errors that could have been identified and corrected earlier. Engaging stakeholders during design ensures systems are robust and meet public needs.

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<sup>131</sup> *Report* (n at 487 (the Report pointed out, as systems containing automation, and artificial intelligence, become more common, it is still the case that human intervention appears to be one of the most effective safeguards against the system failing.')

<sup>132</sup> See section 3.2.4 of the article.

Another concern is the opacity of welfare eligibility determinations. Citizens often lack clarity on access standards and decision-making processes, leading to perceptions of unfairness. Discrepancies in income verification or asset assessments, for instance, can result in denied applications without clear explanations or recourse. This lack of transparency erodes confidence in the system and hampers accountability.

The cumulative effect of these issues is a significant erosion of public trust. Impersonal automated processes, coupled with perceived inequities, alienate citizens and discourage engagement with welfare programs. Addressing this requires enhancing transparency, improving data security, and providing digital literacy programs to empower users.

The Australian Royal Commission highlighted the importance of “honest, transparent, and fair appeal processes” to promote confidence among all stakeholders.<sup>133</sup> This principle should guide regulators worldwide in creating welfare systems that balance efficiency with equity and accountability.

## V. Conclusion

The integration of Automated Decision-Making (ADM) systems into welfare administration offers transformative opportunities, but it also presents complex challenges that require careful navigation. This article has examined the experiences of Australia and China, drawing valuable insights from their implementation of ADM technologies in social welfare systems. These experiences underscore the importance of balancing technological efficiency with principles of equity, accountability, and transparency.

Australia’s and China’s approaches to ADM systems reflect different priorities and contexts, yet both offer critical lessons for policymakers. Australia’s Robodebt scheme demonstrates the need for robust safeguards, public consultation, and clear appeal mechanisms to prevent errors and maintain public trust. Meanwhile, China’s initiatives, including the “Robodebt plus RoboCredit” model in Guangdong, highlight the potential of ADM systems to proactively identify underserved populations while maintaining rigorous oversight to prevent misuse of resources. Both nations illustrate the necessity of integrating human oversight into ADM systems to ensure flexibility and responsiveness to individual circumstances.

Key takeaways from these experiences emphasize the need for transparency in system design, decision-making processes, and eligibility criteria. Public engagement during system development and the implementation of accessible appeal and review mechanisms are essential for fostering trust and accountability. Additionally, human oversight must remain integral to ADM frameworks, enabling systems to adapt to complexities that automated processes may overlook.

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<sup>133</sup> *Report* (n at 555. (stated ‘...A guiding principle was to “provide for honest, transparent and fair appeal processes and practices which balance[d] all relevant considerations and promoted confidence in the system for all stakeholders....’

For policymakers globally, the experiences of Australia and China provide a rich repository of knowledge for designing and refining ADM systems in welfare administration. By integrating lessons from both countries, governments can develop systems that harness the benefits of automation while safeguarding equity and accountability. A balanced approach—one that prioritizes transparency, public trust, and adaptability—will be critical to ensuring ADM systems effectively meet the needs of all citizens, particularly the most vulnerable.

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## Reflections on the Tax Disclosure System Triggered by Investment and Tax Planning by China's High Net Worth Individuals

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**Yuan Ji**

**Abstract:** As China's macroeconomic situation has continually improved, China's private wealth market has also steadily expanded. According to the Hurun Research Institute, investment assets owned by wealthy Chinese households account for about thirty percent of total asset wealth.<sup>1</sup> This wealth continues to grow by as much as ten percent annually. Since there has also been a significant demand for tax planning from wealthy Chinese households, we must pay attention to tax planning, possible tax avoidance and the importance of tax disclosure. At the same time, tax disclosures appear to be becoming more significant, as tax authorities seek to ensure that tax planning complies with the requirements of tax regulation. In this paper, we will discuss if it is possible to reduce the criminal behaviour associated with and the inefficiency and inequity of taxation through inadequate tax disclosure. With adequate tax disclosure, inefficiency and inequity in taxation can be resolved.

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<sup>1</sup> China Private Wealth Report China's Private Banking Industry: Embracing rivers to form the sea, 2022

## I. Introduction

### 1.1 *Inquiring*

I would like to begin with a straightforward question: what is the profile of the wealthy in China? From a taxation perspective, how do China's high-net-worth individuals differ from others? How do they plan their taxes?

What are the issues raised by tax disclosures for high-net-worth individuals (HNWIs)? For a long time, the high-net-worth population has used their unique access to resources to plan their wealth for tax purposes. Now that a requirement for tax disclosure has been introduced what are the implications for Chinese HNWIs in terms of wealth? By implementing CRS2, tax planning with CRS-compliant status will be subject to due diligence procedures and obligations to declare information, and their current activities, such as tax planning, will be impaired. Is it possible to describe the current state of development of CRS in China? In what ways can the government obtain timely and accurate information on the overseas earnings and investments of such high-net-worth individuals? Furthermore, what can the government do to ensure that taxes are collected?

Tax disclosure can influence and regulate the behavior of HNWIs. How does the CRS deal with the dilemma it faces in China? Is it possible to regulate or disclose taxes effectively? How can other countries benefit from these lessons?

How adequate is information disclosure in improving tax efficiency and fairness? In the absence of anti-avoidance efforts, what are the associated problems? How can fairness and efficiency be achieved through tax disclosure? Is there anything that can be done to make tax disclosures more practical?

As a final point, it is worth examining the positive impacts of the CRS under COVID19 and how it has affected the asset allocation of high-net-worth individuals, like investment into the country with no CRS or other type of assets.

### 1.2 *Literature Review*

The number of multinational companies active in China, as well as the number of Chinese high-net-worth individuals, has increased in recent years.

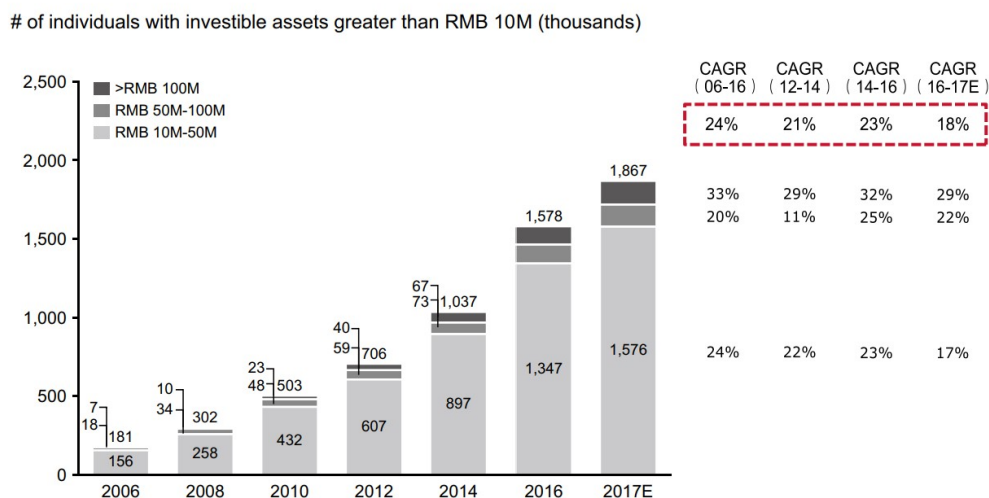
As shown in the chart below, between 2006 and 2017, the number of HNWIs in China increased from 180,000 to 1.87 million, an almost tenfold increase.<sup>3</sup> Based on a study of the structure of HNWI investments inbound and outbound, the percentage of HNWIs investing overseas has risen from 19% to 56% since 2011.

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<sup>2</sup> Knobel, A., & Heitmüller, F. (2018). Citizenship and residency by investment schemes: Potential to avoid the Common Reporting Standard for automatic exchange of information. Available at SSRN 3144444.

<sup>3</sup> China Private Wealth Report China's Private Banking Industry: Steady wins the race, 2017

Figure 2: The size and segments of HNWI, 2006-2017



Source: Bain HNW income-distribution model

HNWIs in China and their investable assets are increasing faster than in previous years. In 2020, there were 2.62 million HNWIs in China. Compared to 2018, there has been an increase of approximately 650,000, representing a compound annual growth rate of 15% from 2018-2020, up from 12% in 2016-2018. The reason for this is primarily due to the excellent performance of the capital markets over the past two years, the rebound in the real estate market in first-tier cities, and the increased number of domestic and international IPOs as wealthy HNWIs continue to emerge. By 2020, Chinese HNWIs will hold RMB 84 trillion in investable assets, representing a compound annual growth rate of 17 percent. Approximately 32.09 million RMB is held in investable assets on average.<sup>4</sup>

There are 5.08 million 'affluent households' with assets over RMB 6 million in China, according to Chart 2 (Wealth size in China), which represents an increase of 70,000 households or 1.33% over the previous year.<sup>5</sup> There were 1.83 million 'affluent households' with investable assets exceeding RMB 6 million as of 2016. There were 2.06 million high-net-worth households with assets over RMB10 million, an increase of 40,000, or 1.95%. 1.1 million households with investable assets of 10 million RMB and 133,000 households with assets of over 100 million RMB were classified as high-net-worth households, an increase of 3,300 households or 2.54% from the previous year. There were 4 million 'affluent households' in mainland China with assets of RMB 6 million, an increase of 80,000 households or 2.08% over the prior year. The number of 'affluent households' with assets of 30 million yuan, excluding Hong Kong, Macau and Taiwan, reached 89,000, an increase of 2.79 percent compared with last year's 2,400.

A total of 1.48 billion so-called 'rich households' exist in China, with investable assets exceeding 6 million yuan. Furthermore, there are 1.66 million high-net-worth

<sup>4</sup> China Private Wealth Report China's Private Banking Industry: Embracing rivers to form the sea, 2022

<sup>5</sup> Yi Tsai. Hurun China Wealth Report 2021, 2021

households with assets exceeding 10 million yuan, an increase of 50,000 households or 3.12 percent over last year. The number of high-net-worth households with investable assets of more than \$10 million is estimated at 896,000. The number of ultra-high net worth households with assets over \$100 million increased by 4,000 or 3.7% over the previous year, including 66,000 households with assets over \$100 million. Approximately 74,000 international households with US\$30 million, an increase of 2,930 or 4.1% over the previous year, including 47,000 individuals with US\$30 million in investable assets.<sup>6</sup>

**Chart 2: The scale of the wealth in China**



Among these HNWI households, 50% are business owners, 30% are large conglomerates and prominent executives, 10% are property speculators, and 10% are investors. Business owners and property speculators account for 75% of households' wealth, an increase of 10% - 15% over the proportion of professional investors with billion-dollar assets. The majority of household wealth is derived from corporate profits, real estate investments, and stock futures.<sup>7</sup>

The purpose of this paper is to analyse and discuss the importance of tax information disclosure for business owners, real estate investors, and shareholders.

It is common for Chinese businesses to be both owned and managed by their owners. The majority of the owner's income is derived from the company.

As argued by Rego and Wilson (2012)<sup>8</sup>, corporate CEOs with lower tax rates tend to have a higher risk appetite, and low effective tax rates are associated with a reduced efficiency of investment, reduced efficiency of capital allocation, an

<sup>6</sup> Ibid., at 5.

<sup>7</sup> Ibid., at 5.

<sup>8</sup> Rego, S. O., & Wilson, R. (2012). Equity risk incentives and corporate tax aggressiveness. *Journal of Accounting Research*, 50(3), 775-810.

increase in audit costs, a decline in operating performance, and an increase in bank lending rates.

There is a trade-off between risk and reward regarding corporate tax evasion. Due to the complexity of information and the secrecy of transactions, information asymmetries are common. Managers have the opportunity to manage earnings.

Real estate investors must comply with tax laws as part of their tax planning efforts for real estate enterprises. In addition, tax planning by real estate enterprises is only considered legal if the relevant tax authorities recognize it. During the actual tax enforcement process, the staff's understanding of the criteria is used to interpret some tax planning activities of real estate enterprises as tax evasion. To minimise these risks, the author suggests strengthening to comply the requirement of the disclosure of tax information. In addition, all tax policies should comply with applicable tax laws. By doing so, HNWI's will be able to communicate more effectively with the tax authorities and reduce the risk for real estate enterprises.

The tax transparency of financial accounts is of significant concern to investors. Automatic exchange of tax information on financial statements represents a new model for international tax cooperation and a new trend in international tax information exchange. It can also be used to enforce tax collection and administration laws against criminals who conceal their assets and income through overseas monetary institutions.

In its Twelfth Action Plan on Base Erosion and Profit Shifting (AP-BEPS)<sup>9</sup>, the OECD proposes mandatory disclosure requirements. In order to achieve effective global transparency of tax-related information on financial accounts, the automated Exchange of Information on Financial Accounts (AEOI)<sup>10</sup> standard addresses two international tax rules. The AEOI and the Multilateral Convention on Mutual Assistance in Tax Matters (hereafter referred to as the Tax Administration Convention) are the two agreements.

Due to the fact that China is still in the early stages of rapid development. China's policy has not attracted the attention of many scholars. Many overseas scholars, however, have conducted extensive research on the subject. According to one study, Balakrishnan et al. argue that although tax avoidance activities can generate revenues for companies, they usually require complex transactions in order to conceal these revenues.<sup>11</sup> As a result, corporate information is distorted in the capital markets and its transparency is reduced. Through strengthening tax collection, corporate tax avoidance can be reduced, thereby improving corporate information transparency. A study by Carrillo et al. found that effective tax collection facilitates the collection of actual income data.<sup>12</sup> Various perspectives on the quality of corporate information disclosure are examined in this paper. Thanks to Spain's strong income tax audit

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<sup>9</sup> OECD (2013), Action Plan on Base Erosion and Profit Shifting, OECD Publishing.

<sup>10</sup> Standard for Automatic Exchange of Financial Account Information in Tax Matters | en | OECD. (2022).

<sup>11</sup> Balakrishnan, K., Blouin, J. L., & Guay, W. R. (2019). Tax aggressiveness and corporate transparency. *The Accounting Review*, 94(1), 45-69.

<sup>12</sup> Carrillo, P., Pomeranz, D., & Singhal, M. (2017). Dodging the taxman: Firm misreporting and limits to tax enforcement. *American Economic Journal: Applied Economics*, 9(2), 144-64.

requirements, those firms near the threshold tend to minimize their income in order to avoid being audited<sup>13</sup>, and thus the profits of the company is distorted. Companies are accordingly more likely to conduct weak tax audits, which can result in income adjustments and, as a result, reduce the quality of information.

Balakrishnan et al.'s evidence suggests that the administration and collection of taxes can have a significant impact on corporate disclosure.<sup>14</sup> In times of low taxes, firms tend to prefer more complex transactions in order to reduce their tax burden. Furthermore, complex transactions reduce information transparency and the quality of corporate disclosures. As a result, taxes are tracked and administered more inefficiently and information is less transparent.

A resident of one country who has economic dealings with a resident of another country may be taxed on income earned abroad. Since the taxpayer has a personal relationship (e.g., nationality) with the country of the other taxpayer, all income is taxable there, regardless of where it was earned.

As a result of the banking secrecy of foreign banks, taxpayers are able to avoid scrutiny by their domestic tax authorities. As a result, tax evasion abroad is a serious issue. Many countries are concerned about the collection of taxes from overseas. International tax cooperation is being enhanced by a number of countries in an effort to curtail international tax evasion.

As a positive example, the US has taken advantage of its global economic position to pursue FATCA (Foreign Account Tax Compliance Act).<sup>15</sup> In the area of multilateral cooperation, the Automated Exchange of Tax-related Information on Financial Accounts Standard (AFE), a measure for the automatic exchange of tax information, published by the Group of Twenty (G20) and the Organization for Economic Cooperation and Development (OECD) in July 2014, is intended to reduce secrecy in the banking sector. Taxpayers who have evaded taxes abroad should be brought under the jurisdiction of the national tax authorities in order to improve the transparency of the tax system.<sup>16</sup>

Offshore tax evasion is a serious problem that is being studied through the tax disclosure system. Zuckerman estimates that 10% of global GDP is held in banks in tax havens, most of which are unknown to the public.<sup>17</sup> In order to evade taxation, perpetrators utilise cross-border banking secrecy, resulting in a significant loss of tax revenue. An estimated \$30B-\$40B in tax revenue is lost each year in the United States alone.<sup>18</sup>

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<sup>13</sup> (Almunia, M., & Lopez-Rodriguez, D. (2013). Firms' responses to tax enforcement strategies: Evidence from Spain.)

<sup>14</sup> (Ibid., at 9.)

<sup>15</sup> (Bean, B. W., & Wright, A. L. (2014). The US foreign Account tax compliance act: American legal imperialism. *ILSA J. Int'l & Comp. L.*, 21, 333.)

<sup>16</sup> (Alberto Gil Soriano, 'Toward an Automatic but Asymmetric Exchange of Tax Information: the US Foreign Account Tax Compliance Act (FATCA) as Inflection Point', (2012), 40, *Intertax*, Issue 10, pp. 540-555.)

<sup>17</sup> (Zucman, G. (2013). The missing wealth of nations: Are Europe and the US net debtors or net creditors?. *The Quarterly journal of economics*, 128(3), 1321-1364.)

<sup>18</sup> (Gravelle, J. G. (2009). Tax havens: International tax avoidance and evasion. *National Tax Journal*, 62(4), 727-753.)

Accordingly, it is necessary to strengthen the management of offshore tax evasion through the study of tax information disclosure, and by obtaining information regarding foreign trade and the financial accounts of tax residents in order to facilitate cross border tax evasion. Obtaining such information will assist tax authorities to address issues of jurisdictional scope, access to information about international tax-receiving countries, and cooperative management. Tax information exchange is the standard method.

There are a number of ways in which tax information can be exchanged. Since its implementation in recent years, automatic exchange of information (AEOI) has overcome many of the disadvantages of other methods, and has had a significant deterrent effect on taxpayers who try to evade taxes across borders. It has become increasingly important to cooperate with international tax authorities in order to collect taxes.

There are two frameworks for sharing information in the Automatic Exchange of Tax Information (AEOI): 1. With its economic strength and power to act as a deterrent, the United States promotes unilateral tax information exchange, the Foreign Account Tax Compliance Act (FATCA), and 2. Multilateral regulatory cooperation centered on participation in the Automatic Intergovernmental Exchange of Information (AEOI), known as the Common Reporting Standard (CRS).<sup>19</sup>

In December 2015, China signed the Agreement on Competent Authorities for the Automatic Exchange of Information on Multilateral Financial Accounts as a party to two framework agreements.<sup>20</sup> The agreement has been signed by a hundred and eight countries and regions as of 24 December 2019. Every year, China will exchange financial account information with these countries and regions.

Although China signed FACTA with the United States only in principle in 2014, the exchange of financial account information with the United States continues, even in the absence of the final agreement.

Despite the fact that automatic tax information exchange is highly targeted and can help combat tax evasion by firms using offshore accounts, the large-scale implementation of this scheme is accompanied by a tax issue: the treatment of undeclared historical income.

As of 2010, at least US\$21 trillion to US\$32 trillion was stored abroad from the US for tax evasion, and this issue becomes even more severe when non-financial assets (real estate, yachts, etc.) are taken into account.<sup>21</sup> If bank secrecy comes to an end, many clues concerning tax evasion by taxpaying residents will be revealed. If a tax penalty mechanism is introduced, more detailed investigations of taxpayers will be

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<sup>19</sup> Cusi, E., Spengel, C., & Stage, B. M. (2020). Cross-border tax evasion after the common reporting

<sup>20</sup> Hasim, M. P., Priyono, F. J., & Sa'adah, N. (2018). Karakter Multilateral Competent Authority Agreement On Automatic Exchange Of Financial Account Information Dan Implikasinya Pasca Program Tax Amnesty Di Indonesia. *Diponegoro Law Journal*, 7(4), 345-363.

<sup>21</sup> Henry, J. S. (2012). The price of offshore revisited. *Tax Justice Network*, 22, 57-168.

required, and tax administration costs will be likely to increase. For these reasons, offshore voluntary disclosure is a better choice.

### ***1.3 Research Methodology***

In this paper, the following research methods are employed to study the link between investment and tax planning for high-net-worth individuals, to analyse the tax-related information exchange mechanisms for high-net-worth individuals, and identify and improve the legal loopholes in these mechanisms.

The paper adopts a qualitative research approach. It attempts to identify and summarise the lessons learned from other countries' offshore voluntary tax disclosure systems by analysing and comparing them.

#### **1.3.1. Literature analysis**

The objective of this study is to establish a tax collection and management system with the primary objective of assisting the Chinese tax authorities to prepare offshore tax and combat offshore tax evasion.

An overview of the literature is provided, as well as an interpretation of the relevant legal documents of the CRS. However, using purely theoretical to methodologies analyse the advantages and disadvantages of the voluntary offshore tax disclosure system places the author in a difficult intellectual position. Through examples and experiences, theoretical reasoning is illustrated by focusing on current social or disciplinary realities. A case study of the tax-related information exchange mechanisms of China and other countries is presented in this paper to analyse the social information exchange mechanism of CRS.

#### **1.3.2. Method of comparative analysis**

A two-fold comparative analysis of the offshore tax voluntary disclosure regime is presented in this paper. In the first comparative analysis, the effectiveness of the offshore voluntary disclosure system is compared to the current system. In addition, the advantages of the offshore voluntary disclosure system are clarified. A second part of the comparative analysis focuses on countries that have implemented overseas voluntary disclosure systems, and China may benefit from learning from the experience of these countries as it constructs its own overseas voluntary disclosure system. It is necessary to conduct an analysis of the current state of tax disclosure in China and the deficiencies that exist. A discussion of overseas experience is also provided, and based on China's national conditions, suggestions will be made for improvement. As far as the field of law is concerned, comparative analysis is the method most commonly used in legal studies to compare the relevant systems of China and foreign countries. Through a comparative analysis of laws and regulations in various countries, we analyse and explain the current situation of CRS legislation in China.

## ***1.4 Ideas***

Chapters 2 and 3 present a description of the wealthy in China and their characteristics; the theoretical origins of tax disclosure will be discussed, and the concept of tax disclosure introduced.

In Chapters 4 and 5, we examine the issues arising from the tax disclosure system and how they relate to the development of China's high net worth individuals.

Chapter 6 discusses the current status and deficiencies of tax disclosures for high-net-worth individuals in China. In this chapter, we will examine the current tax disclosure regulations in China. This analysis identifies the shortcomings in the application of the regulations to the HNWI group, the shortcomings of the regulations themselves; the overall taxation system, and the timing of taxation.

Chapter 7 describes better developed systems in other countries and examines the possibility of establishing them in China; briefly compares China's laws with overseas approaches and analyses their theoretical foundations.

A discussion of China in the context of global tax disclosure is presented in Chapter 8. Further, it suggests a series of steps China can take to improve tax disclosure, including improving multilevel legislation, strengthening legal responsibility, and improving the path to relief, as well as the means of achieving fairness.

In Chapter 9, in light of the Covid-19 epidemic, the implications of tax disclosure for HNWI asset allocation are examined and discussed.

A discussion of the limitations of this study is presented in Chapter 10.

## ***1.5 Innovation And Significance***

Innovation is determined by the novelty of the topic chosen.

In spite of the short period of time since the introduction of CRS and the fact that tax planning for HNIVs differ from person to person, very few independent studies have been conducted. The novelty of this paper lies in the combination of these two approaches. The purpose of the paper is to provide a longitudinal analysis of the legal aspects of the information exchange mechanism within the context of the implementation of the Common Reporting Standard.

In addition, this study presents an innovative approach to identifying legal loopholes within the tax-related information exchange mechanism, starting with the act of circumvention, identifying the loopholes and legislation issues related to the specific acts of circumvention, and recommending specific improvement strategies for those loopholes.

The purpose of this study is to clarify the development of CRS and the characteristics of tax avoidance methods, to identify the tax-related information exchange mechanism for high-net-worth individuals under CRS, to examine the legal loopholes and regulatory issues under this mechanism, and to identify tax avoidance

behaviours of relevant taxpayers, so that these loopholes, issues and behaviours addressed.

It is possible to divide the significance of the research according to its conceptual and practical implications. By combining CRS with the investment and tax planning behaviours of high-net-worth individuals, this paper demonstrates the link between CRS and investment and tax planning. It refines CRS reporting requirements for tax planning, and classifies investment behaviours from the perspective of CRS. It also provides a new perspective for the theoretical study of the mechanism for exchanging tax-related information among HNWI's under the Common Reporting Standard. The paper provides a new perspective on the theoretical study of tax-related information exchange mechanisms for high-net-worth individuals under the CRS.

This paper has practical significance because, after analysing the legal loopholes in the exchange of tax information for high-net-worth individuals under the CRS, it proposes practical methods and improvements for supplementing the gaps in the existing CRS model, allowing financial institutions to conduct due diligence in a timely manner in order to detect account holders' tax avoidance intentions, and to facilitate the detection of gaps by tax authorities for effective regulation of financial practices. As a result, it facilitates the efforts of the tax authorities to identify gaps and to regulate financial practices effectively.

## II. Portrait of The Wealthy in China and Their Characteristics

Let me begin with a straightforward question: who are the wealthy in China?

Wealth has been growing in China thanks to the rapid development of the economy, and the number of high-net-worth individuals is increasing every year. In 2020, China Merchants Bank statistics indicated that investable assets in China would soon reach 241 trillion RMB, the number of Chinese high-net-worth individuals with investable assets exceeding 10 million RMB would reach 2.62 million, and the number of this group was expected to exceed 3 million by the end of 2021, with a total investable asset value of over 90 trillion RMB.<sup>22</sup>

Despite this huge accumulation of wealth, the personal tax rate of the HNWI population is not commensurate with the extent of their wealth.<sup>23</sup> Considering that potential income tax revenue from the high-net-worth population is being lost in China and that income tax derived from the working class is the main source of personal income tax revenue, it is worthwhile to examine this phenomenon.

In terms of tax administration, the HNWI population exhibits the following characteristics. The tax-related business sector is complex, and the sources of income are diverse. As well as earning salary and wages, they may also run their own businesses and make investments in capital and real estate, which may be subject to various types of taxes, such as personal income tax, value-added tax, property tax,

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<sup>22</sup> Ibid., at 4.

<sup>23</sup> 招商银行, <2021 中国私人财富报告> [China Merchants Bank, China Private Wealth Report 2021)]

and stamp duty. In addition, there are a number of cross-border businesses. HNWI typically have residences and investments in multiple countries, and their assets are spread across various enterprises at home and abroad. Tax administration for HNWI becomes more complex as a result of differences between tax jurisdictions and tax systems in different countries.

HNWI groups can evade taxes in a variety of ways, and it is difficult for tax authorities to gain a complete understanding of financial information from them, because there is a low level of information sharing among jurisdictions regarding tax sources. Moreover, it is difficult for tax authorities to monitor effectively whether HNWI evades taxes by using inter-regional information asymmetry and transfer of income to family members within the country. Here are some of the most common tax evasion methods. The first is the concealment of income, other than salary derived from property transfers or property leasing. The second, expensing income, is the listing of personal consumption as an expense related to running a business; thirdly, conversion is the process of providing housing, public transportation, and other high welfare benefits to disguise salary payments. Fourthly, conversion of income to a achieves a lower tax rate by declaring lower salaries and transferring personal income to the company's share capital. The economic transactions are made 'underground', using private transactions between buyers and sellers to adjust the transaction price and conceal the actual income artificially; and fifthly, tax avoidance offshore, by transferring property to low-tax countries through migration, offshore trusts, and registering companies in tax havens. Since high-net-worth individuals employ such a variety of tax avoidance strategies, tax administration has become more complicated and requires more professional and efficient management from tax authorities.

How do HNWI plan their taxes? The purpose of this article is to describe the tax avoidance phenomenon and the methods used by Chinese HNWI to tax planning.

#### 1) Adopt a migration strategy

There has been a qualitative change in the legal relationship to taxation in China due to the migration of some high-net-worth individuals to tax havens or low-tax countries to obtain tax residency. As a result, eminent domain rights also migrate simultaneously. Since these assets have remained hidden, the tax authorities are not able to determine accurately the value of this property in various types of accounts. This behaviour circumvents the income tax obligations a Chinese tax resident should bear both within and outside the country these Chinese individuals cause a loss of tax revenue as a result of such behaviour. Increasingly, high-net-worth individuals are allocating their assets overseas in accordance with the development of economic globalisation. In spite of the fact that their investment activities are no longer limited to China, they still maintain their status as Chinese tax residents. In the past, Chinese tax authorities had difficulty taxing foreign financial assets because of the lack of cooperation in the exchange of social information on financial accounts between countries. With the implementation of CRS in more and more countries and regions, Chinese citizens with overseas assets are no longer able to conceal their financial accounts in CRS member countries. Accounts of Chinese HNWI with financial assets abroad constitute non-resident accounts within the reporting scope of other countries that have adopted CRS, and financial institutions will report account

information to the tax authorities of the place where the financial assets are held and to the Chinese tax authorities when required. Thus, the government will receive comprehensive information regarding Chinese tax residents' allocation of assets abroad, enabling adequate supervision of these offshore financial accounts. It is important to note that if a person emigrates to a country that is not covered by the CRS, but still lives and works in China or leaves the country for no more than ninety days in a year, he or she remains a Chinese tax resident.<sup>24</sup> If one has financial assets in a CRS participating country (region), the tax-related information of the financial account will be shared with the Chinese tax authorities, meaning that migrants cannot bypass the CRS.

## 2) Avoiding taxes by transferring pricing between related parties

Some HNWIs conduct business with related parties in order to maximize their profits. As a result, by using transfer pricing, the transfer price may be artificially set higher or lower than the market price of the transaction; for example, insufficient gain on equity transfer. The result will be a reduction in personal income or taxable income, as well as a reduction in personal tax payable in the PRC.

Other common tax avoidance methods used by HNWIs include transactions involving transfer pricing between related parties as well as the direct transfer of wealth and capital. Setting up offshore structures in international tax havens and accumulating profits there for a long period of time without distributing them; avoiding taxes by using tax treaties to transfer equity to offshore companies or trusts; all of these practices have been used. Despite the diversification of cross-border tax avoidance by HNWIs through trusts, funds, China's anti-avoidance regime remains undeveloped, with no special anti-avoidance provisions or even general anti-avoidance provisions. Not until 2018 did the seventh amendment to the Personal Income Tax Law introduce anti-avoidance provisions.<sup>25</sup> Despite the fact that the automated exchange of tax-related information on accounts has increased transparency regarding high-net-worth individuals' overseas accounts and reduced the incidence of tax avoidance by moving capital overseas, cross-border tax avoidance can be prevented only through a robust anti-avoidance system and strong tax supervision capabilities, as well as through access to tax information. Some of China's high-net-worth individuals have deployed resources to diversify their cross-border tax avoidance, which has seriously eroded the tax base. In addition to causing a loss of tax revenue, HNWIs increases the gap between the rich and the poor.

## 3) Avoiding tax by setting up short-selling foreign companies in international tax havens.

Some HNWIs establish foreign-controlled companies in tax havens and then transfer their domestic assets or property to these companies. Consequently, the controlled companies accumulate profits in tax havens, leaving zero or lower profit

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<sup>24</sup> 国家税务总局. (n.d.). [State Administration of Taxation. (n.d.).] Retrieved October 20, 2022)

<sup>25</sup> 郝琳琳. (2021). 我国个人所得税反避税规则的优化. 中国社会科学院研究生院学报.[ Hao, Linlin. (2021). Optimization of anti-avoidance rules for personal income tax in China. Journal of Graduate School of Chinese Academy of Social Sciences.]

distributions attributable to residents. Finally, tax avoidance is achieved by exploiting tax havens' absence of or low tax rates.

#### 4) Avoidance of tax through the indirect transfer of domestic equity

The shell companies are then used to control and invest in subsidiaries in China. As a result, HNVI's sell overseas shell companies in order to transfer domestic equity and acquire real estate indirectly. Non-resident high-net-worth individuals whose income comes from the transfer of offshore shell companies are not taxed in China. As a result, they are able to avoid paying personal income tax in China, or pay less personal income tax.

### III. Origins of Tax Disclosure Theory

A Common Reporting Standard (CRS)<sup>26</sup> was developed by the OECD to facilitate the automatic exchange of tax information between countries. China signed the Multilateral Inter-Authority Agreement Between Multilateral Authorities on Automatic Exchange of Tax-related Information on Financial Accounts in December 2015<sup>27</sup> and implemented the Administrative Measures for Due Diligence on Social Information on Non-Resident Financial Accounts on July 1, 2017, and the CRS on September 1, 2018.<sup>28</sup> CRS was officially implemented on 1 September 2018, and information began to be exchanged with other jurisdictions participating in the CRS. As a result of the implementation of the CRS, information on the financial information of its account holders and beneficial owners has been declared, thus completing the exchange of tax related information. Financial institutions<sup>29</sup> are required to understand the tax residency status of account holders or controllers, identify non-resident financial accounts and mobile phones, and report relevant information in accordance with the Due Diligence Management Measures.

However, information technology in the internet age has made it possible to exchange information automatically on accounts, and the economic difficulties of countries caused by the global financial crisis have gradually led to the establishment of FATCA<sup>30</sup> (Foreign Account Tax Compliance Act) and CRS (Common Reporting Standard). To combat cross-border tax evasion, the Organization for Economic Co-operation and Development (OECD) issued the Standard for Automatic Exchange of Tax-Related Information on Accounts (AEOI)<sup>31</sup> as early as 2014. AEOI is a

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<sup>26</sup> Casi, E., Spengel, C., & Stage, B. M. (2020). Cross-border tax evasion after the common reporting standard: Game over?. *Journal of Public Economics*, 190, 104240.

<sup>27</sup> 金融账户涉税信息自动交换标准简介.(n.d.). [Standard for Automatic Exchange of Tax-related Information on Financial Accounts Interpretation]

<sup>28</sup> 姜晨. (n.d.). 关于发布《非居民金融账户涉税信息尽职调查管理办法》的公告.[ Jiang, Chen. (n.d.). Notice on the issuance of the Administrative Measures on Due Diligence of Tax-related Information of Non-Resident Financial Accounts.] 关于发布《非居民金融账户涉税信息尽职调查管理办法》的公告\_部门政务\_中国政府网. Retrieved October 20, 2022.

<sup>29</sup> 朱英. (n.d.). 《非居民金融账户涉税信息尽职调查管理办法》的解读.[ Zhu, Ying. (n.d.). Interpretation of Due Diligence Management Measures for Tax-related Information of Non-resident Financial Accounts.] 《非居民金融账户涉税信息尽职调查管理办法》的解读\_解读\_中国政府网. Retrieved October 20, 2022.)

<sup>30</sup> 《习近平主持召开中央财经委员会第十次会议》[Presiding over the 10th Meeting of the Financial and Economic Commission of the CPC Central Committee]

<sup>31</sup> *Ibid.*, at 8.

standard for the automatic exchange of financial account information in tax matters.<sup>32</sup> There are two main components of the standard, the CRS and the Model Agreement between Competent Authorities. Institutions are required to collect and report information on the accounts of foreign tax residents (individuals and corporations) as part of the CRS. Under the auspices of the G20, the CRS has rapidly led to several countries joining together to weave a grid of information exchange, achieving a goal that has been difficult for the international community to achieve in the past: exchanging information on offshore accounts with the country of the individual's tax residence. As of July 2019, 106 countries (regions) have signed the multilateral competent authority agreement to implement the AEOI standard, of which 92 have already begun exchanging information. As a result of their institutional advantages and confidentiality, offshore structures such as trusts were the main method of avoiding international taxes for high-net-worth individuals prior to the implementation of the CRS.<sup>33</sup> As part of the CRS compliance requirements, offshore trusts are required to report and identify information regarding their accounts. A metallurgical institution is required under the CRS to report the non-resident account information of its domestic branches, including their tax identification number, in aggregate. (ii) If the account holder is a non-resident non-metallic institution with non-resident control, the non-resident control information should also be disclosed. By 31 December 2018, the institution should complete due diligence on accounts with a combined balance of more than USD 25 million as of 30 June 2017. In the context of the CRS, the owner, controller, and even the wealth beneficiary must adhere to the trend of transparency.

The government can ensure that personal taxes are accurate at a macro level. A lack of agreement between governments can complicate international tax procedures, which may also result in governments not being able to be recorded in the system, and this may lead to tax evasion.

By ensuring the accuracy of personal information, the disclosure system prevents conservatism and misrepresentation.

The purpose of this paper is to examine from a practical perspective whether the agreement allows access to valid information between China and other countries. According to Chinese tax practice, it is not possible even in countries that have signed. Another limitation is that the CRS primarily exchanges financial information related to financial assets – as a result, real estate, antiques, paintings are not disclosed. Tax exemptions are still available to high-net-worth individuals.

It is impossible for the state to verify an applicant's income if the government does not make the information public. A number of instances have occurred in which taxpayers illegally transferred income overseas and avoided tax liability. Tax revenues are accordingly reduced, wealth is distributed unfairly, and criminal activity (corruption, gangs, drug trafficking) is encouraged.

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<sup>32</sup> Standard for Automatic Exchange of Financial Account Information in Tax Matters

<sup>33</sup> *Ibid.*, at 27.

In China, shares or other financial accounts held are not required to be declared to the government, leaving it with only partial information about the investor. In other countries, investors must declare their domestic gains and pay capital gains tax and global taxes.

It is common for offshore tax evasion to involve opening accounts in foreign banks and then using bank secrecy to avoid scrutiny by domestic tax authorities. To combat tax evasion, the international community has strengthened cooperation between taxing countries through the Automated Exchange of Tax Information (AEOI).

As a result of the implementation of the AEOI jurisdiction, foreign banks will be required to report information regularly on the financial accounts of their tax residents to the local tax authorities.

Taking the example of Chinese tax residents who have bank accounts in Switzerland and who report Swiss information to the Chinese tax authorities: this would be a weapon against offshore tax evasion, and evidence of offshore tax evasion would be presented to the Chinese tax authorities. An offshore voluntary disclosure mechanism could provide them with such an opportunity to be honest.

First and foremost, tax evaders are able to invest in non-financial assets offshore. In accordance with FATCA and CRS, foreign tax authorities do not report ownership of non-financial assets (such as real estate, precious metals, art, and collectibles). In addition, cryptocurrencies (such as Bitcoin) are not subject to AEOI since they are not considered financial assets.<sup>34</sup>

In addition, some tax evaders may transfer their original financial assets to countries with no automatic exchange of tax information, such as the United States. Since 2014, China and the United States have been in agreement on the content of the Foreign Account Tax Compliance Act (FATCA), but no bilateral cooperation agreement has been signed.

There is thus no requirement to exchange financial account information between the US and China, and tax evaders are still able to exploit this loophole in order to hold undeclared offshore financial assets.

As a result, AEOI tax transparency with automatic tax information exchange is relatively limited. Since state's taxes are not made public and some people provide false tax information, taxation is an ineffective way to deter crime in many countries. Keeping tax information confidential costs a country a great deal.

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<sup>34</sup> Noked, N. (2018). Tax evasion and incomplete tax transparency. *Laws*, 7(3), 31.

## VI. Tax Disclosure Issues Facing Chinese Hnwis

### *4.1 How Will the Introduction of the CRS Affect Chinese High-Net-Worth Individuals?*

The CRS ushers in a new era of tax transparency by shifting property concealment to information exchange. As indicated in the previous section, high-net-worth individuals are able to plan their wealth for tax purposes by using resource allocation, and the tax authorities are unable to obtain accurate information regarding their assets in various types of accounts, and thus their assets have remained hidden for tax purposes.

Following the development of tax-related information and exchange and global asset transparency, particularly since the introduction of CRS, more and more countries or regions are participating in CRS, and in accordance with the mechanism for sharing social information outlined in CRS, acts involving tax avoidance will be initiated by due diligence procedures and the first tax information will be declared, avoidance will become more difficult. HNWI may resort to legal loopholes to protect their interests and avoid the exchange of tax-related information, resulting in substantial losses to international anti-avoidance and national tax administrations.

In this paper, the development of tax planning and its fundamental connotations are explained. The paper summarises the main features and functions of tax avoidance that are generally favoured by high-net-worth individuals in terms of secrecy and tax planning. The legal factors that concern its advantages are analysed. The reasons for the formation of CRS, its legal composition, its mode of operation, and the current state of legislation are also examined. Under the CRS regime, a due diligence procedure is initiated, and tax-related financial information is declared along with the identification of account holders and beneficial owners.

During the implementation of the CRS, offshore trust may opt to avoid tax-related information exchange for purposes such as tax planning, reflecting the loopholes that remain to be resolved at the CRS level. There are numerous issues, including inconsistent exchange models among participating jurisdictions, insufficient regulatory measures for financial institutions, unclear provisions regarding asset conversions and unclear provisions regarding beneficial owner disposition, as well as problems at the national level. It is necessary to address a number of issues, including the lack of clarity in the definition of legal concepts, disagreements between different laws regarding standards, and inadequacy of the sharing mechanism.

The loopholes and problems previously listed at the CRS level need to be addressed by promoting the implementation of the multilateral swap model, regulating the supervision measures of financial institutions, establishing a new asset conversion registration system, and improving the legal effectiveness of the relevant interpretations. Alternatively, domestic legislation should be clarified, the standards between the different laws should be unified, and relevant laws and regulations should be revised and implemented.

## ***4.2 Seven Key Groups of People are Affected by the CRS***

The first category of people affected consists of Chinese citizens who have already emigrated. A number of high-net-worth individuals hold Chinese passports, but have already obtained permanent residency status in another country or have recently received a green card or a passport from another country. A number of popular countries to which HNWI's prefer to emigrate require tax residents to disclose their global assets annually and file annual tax returns. The majority of Chinese immigrants keep a low profile and are not accustomed to declaring their assets fully, let alone paying their income tax to their country of immigration in a truthful manner. As part of the CRS agreement, it is likely that hidden financial assets in China will be disclosed to the country of immigration, and also likely that such individuals will be subject to back taxes, various fines, and even criminal prosecution.

There is a second category of those who have financial assets located abroad. Whether an immigrant or not, if individuals have financial assets overseas (including deposit accounts, custodial accounts, cash value policies, annuity contracts, securities accounts, futures accounts, equity/debt interests in financial institutions, etc.), the Chinese tax authorities will inform the local tax authorities about their financial asset holdings in the country or territory where these assets are located. Suppose, for example, that a person with an ID card from mainland China deposits \$5 million with HSBC in Hong Kong. In this case, HSBC in Hong Kong will report the deposit to the Hong Kong tax authority. In turn, this bureau will report the deposit information to the mainland tax authority. Now it is time to consider a few questions. Is the money leaving mainland China legal income or not? Is this an illegal underground transfer of funds in order to avoid foreign exchange regulations? In China, have the funds been taxed legally? Is there proof that the depositor has paid taxes? In any case, criminal liability may be involved.

### **Category 3: Shell companies abroad**

A company is established in a tax-friendly offshore jurisdiction. Assets are held in a bank or other financial institution, and money is managed or spent through the company's account. The implementation of the CRS standard requires that a company disclose the assets owned by the actual controller and both layers of the company (commonly referred to as a shell company.) This type of business may be regarded as a 'negative non-financial institution' (also known as a shell company.) In the past, using the shell company name to avoid tax was possible.

### **Category 4: Domestic civil servants with money overseas.**

The consequences are quite serious, possibly criminal, for civil servants or state employees who have not emigrated but have hidden large sums of money abroad. In Chinese criminal law, there is a crime specifically aimed at state employees: the crime of unexplained sources of large amounts of property. According to Chinese criminal law, state employees who have deposits outside of China are required to

declare them in accordance with state regulations.<sup>35</sup> The consequences may be a fixed-term prison sentence of up to two years or detention if the amount is large and concealed; if the circumstances are less severe, an administrative punishment may be given at the discretion of the unit.

#### Category 5: High-net-worth individuals

In recent years, many HNW clients have attempted to allocate more US dollar assets to cope with the depreciation of the RMB. Many people have chosen to purchase insurance policies overseas, such as those issued in Hong Kong or the United States. Hong Kong is also a CRS signatory territory, and the Hong Kong legislature introduced the Taxation Amendment Ordinance No. 3 of 2016 on 30 June 2016.<sup>36</sup> A requirement of the Ordinance is that insurance companies in Hong Kong must also provide the mainland Chinese tax authorities with information on the assets of comprehensive policies owned by domestic high-net-worth individuals. The disclosure applies not only to policies purchased in 2017 but also to policies purchased in the past. Domestic HNW clients may not be comfortable with this situation. In spite of this, Hong Kong's policy assets are not at risk. Researchers have found that if life insurance is planned wisely, both within and outside the country, it can play a significant role in handling the CRS crisis.

The majority of China's wealthiest have established family trusts abroad, and their preferred jurisdictions include the Virgin Islands, Cook Islands, Guernsey, Singapore, Hong Kong, New Zealand, Cayman Islands, and others. For the HNVI's, most of the family trust jurisdictions have become signatories to this CRS, and the CRS agreement stipulates that information about established family trusts must also be disclosed, including the trustee (i.e., settlor), protector, trustee (through the trust), and beneficiaries. It is thus unrealistic to suggest that financial assets held in family trusts can be exempt from the CRS provisions. An essential function of a family trust is to transfer wealth and segregate debt risk, rather than to avoid taxes. When used wisely, a family trust instrument can serve as a tax deferral tool.

#### Category 6: owners set up companies overseas to engage in international trade.

Financial account information for overseas trading companies is not included in the current CRS information exchange content. It has been discovered that many wealthy individuals derive their overseas income from international trade. Typically, they set up a physical company in another country to conduct production and export activities.

Most investors will establish another company in a tax-advantaged offshore location in order to complete the offshore collection function of overseas trade. With the tax exemption benefits, a large portion of foreign exchange income will go directly into the offshore company's account. As a result of the simultaneous implementation of CRS in China and abroad in this case, the financial assets of the owners will have to

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<sup>35</sup> 时延安. (2002). 巨额财产来源不明罪的法理研析. 法学, (3), 39-43.[ Shi,Yan-An. (2002). Legal theory analysis of the crime of unexplained source of huge property. Journal of Law, (3), 39-43.)]

<sup>36</sup> 香港版 CRS: 内地富人的"裸奔"时代. (n.d.).[ Hong Kong version of CRS: The "streaking" era of the Mainland rich. (n.d.).]

be disclosed (which cannot be a small amount), and when the Chinese tax authorities audit, they will find that the money was not exchanged out of China, but was income from dividends received by the owners directly from overseas companies. According to the Income Tax Law and the famous China Taxation Administration Circular 698, Circular 82, and others<sup>37</sup>, some enterprises set up by Chinese owners abroad are considered Chinese tax resident enterprises.

Category 7: financial institutions and private wealth management related practitioners.

CRS may bring new challenges to the careers of owners of financial institutions and private wealth management-related practitioners. A number of leaders of financial institutions will be affected by the implementation of CRS, including bank account managers, insurance agents, wealth advisors of trusts, offshore investment managers, family offices, and inbound and outbound tax practitioners. It is true that CRS will have an impact on certain industries because it will change the geographic location and type of asset allocation of clients. As well as considering whether to change their existing financial assets to another kind of property, clients will also have concerns regarding the allocation of their future overseas assets. As a result of the implementation rules for the CRS landing, financial institution practitioners may be asked about the clients they serve, and bear specific professional risks, as the CRS standard stipulates that a financial practitioner is responsible for deceiving a financial institution by failing to make truthful statements if they induce their clients to make false statements. It is possible that they will be criminally prosecuted and imprisoned in addition to being fined. This results in a sensitive and delicate relationship between the account manager and the client.

There has been a steady increase in the number of multinational corporations and high-net-worth individuals in China in recent years. Cross-border investment has also increased significantly.

Although CRS bring economic benefits to China, they also create significant problems for the country with regard to international tax avoidance. The Chinese government does not adequately regulate offshore taxable income. It is common for multinational corporations and individuals to evade China's tax obligations by shifting profits overseas in a variety of ways. In addition to an inflated GDP, China often lacks tax revenue, resulting in a significant erosion of its tax base.

Nevertheless, the system does not depend on automatic occurrence of AEOI; combating tax evasion requires AEOI from an external audit perspective. Voluntary offshore disclosure is a means of communication between the taxpayer and the tax authorities. The voluntary disclosure of tax issues by taxpayers is consistent with the requirements of the legal system. As a result, the international community would be taking new measures to combat international tax evasion as well as increasing tax audits and encouraging more people to make voluntary disclosures. It is possible that this could reduce tax evasion if people wish to maintain a legal status. Voluntarily

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<sup>37</sup> 中华人民共和国企业所得税法. (n.d.). [Enterprise Income Tax Law of the People's Republic of China] Retrieved October 20, 2022.

disclosing offshore assets should be encouraged as China's tax collection system improves.

As other countries require overseas investors to disclose tax information, China faces both opportunities and challenges. As a result of this regime, cross-border tax avoidance, money laundering, and investment returns are regulated. The requirement that overseas investors disclose their tax information in other countries also presents opportunities and challenges for China. There are, however, challenges associated with these developments, since China has not yet established an adequate financial system. Several problems may make it difficult to replicate the current tax system, and these should be addressed through legislation.

## **V. Towards a More Transparent Tax Environment for China's High-Net-Worth Individuals**

The next step is to discuss the impact of CRS on global asset allocation. As long as they do not violate anti-money laundering regulations, offshore investments, such as local asset allocation through overseas insurance policies and family trusts, are legal; further, CRS can only disclose the status of assets that are in place currently, and addressing the issue of their origin is problematic; however, CRS will affect disclosures of future assets acquired. In this paper, the origins and rationale for the CRS have been explained.

The report analyses the people and types of assets affected by the CRS as well as its impact on global asset allocation.

### ***5.1 the Impact of The CRS on Global Asset Allocation.***

#### **5.1.1 Impact on asset allocation regions**

Chinese tax residents in CRS participating countries (territories) will not necessarily have their financial accounts collected and exchanged with the Chinese tax authorities, as the conditions to be met for the exchange of information include being a CRS participating country (territory) and having an automatic bilateral or multilateral matching agreement with China for the exchange of financial account information. China does not have a matching relationship with some of the CRS countries (territories). By the end of November 2016, the Cayman Islands only had matching relationships with thirty-two countries (territories), and information on Cayman Islands residents was exchanged only between these thirty-two countries (territories). Some investors allocate their assets to these countries or regions or to countries or regions that do not participate in the CRS. There are, however, risks associated with moving assets from their original location, and the safety and value of the assets may not be ensured after the move. Furthermore, the assets may not be able to be realised or may be subject to a high tax burden.

Taxpayers who have two or more tax resident statuses at the same time when engaging in cross-border business activities may be required to provide information on assets to the tax authorities of more than one country or territory because of conflicting national laws. Because of these requirements, HNWI's may reduce their

investments abroad and turn to domestic investments, resulting in a change in their investment structure to replan their assets.

### 5.1.2 Impact on asset allocation structure

In respect of asset structure, CRS information exchange is limited to financial assets, such as overseas bank deposits, trust income rights under trust structures, insurance policies that have cash value, and shares of bond companies. The financial assets category excludes real estate, specific physical goods, and non-debt direct interests, and therefore no information exchange is required. A number of other assets are also excluded from the exchange, including property, jewellery, paintings, aircraft, yachts, company shareholdings, and precious metals held in an investor's own name, as well as critical illness and term life insurance policies. Therefore, some investors may prefer to invest in assets that are not disclosed under the CRS or in assets that are disclosed but that carry a lighter tax burden. Dividends and bonuses are subject to taxation under the Chinese income tax law. However, dividends and bonuses received from insurance are tax-free, which may encourage investors to invest more in life insurance.

In accordance with 'Measures for the Administration of Social Information Due Diligence on Non-Resident Financial Accounts (Draft for Public Comments)' <sup>38</sup>, financial accounts include several types of deposit accounts, including demand deposits, time deposits, traveller's cheques, credit cards with pre-deposit capabilities, and others.

The business of managing assets entrusted to trustees on behalf of clients includes the activity of financial institutions initiating, establishing or managing financial products, funds and trust plans without independent legal personality. A financial investment product may be a wealth management product, a fund, a trust plan, a unique account or a pooled asset management plan. Accounts that meet one or more of the following conditions: (1) equity or bond interests in investment institutions, including partnership interest in private investment funds and income rights; (2) insurance contracts or age contracts with cash values.

Further, to prevent individual taxpayers from attempting to avoid CRS investigations in the future, the CRS standard provides for the 'see-through principle' which requires identifying the beneficial owner via an intermediary company (conduit company or shell company)<sup>39</sup>, and if the beneficial owner of the business is a Chinese tax resident taxpayer, then the business' financial assets and the controller's personal information are disclosed to the Chinese tax authorities through this exchange mechanism.

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<sup>38</sup> 林巧婷. (n.d.). 非居民金融账户涉税信息尽职调查管理办法（征求意见稿）. [Lin Qiaoting. (n.d.). Administrative Measures on Due Diligence of Taxrelated Information of non-resident Financial Accounts (draft for public comments).]非居民金融账户涉税信息尽职调查管理办法（征求意见稿）\_国务院部门政务联播\_中国政府网. Retrieved October 20, 2022.

<sup>39</sup> Dixon, A. (2022, September 27). What is a Shell Company (shell corporation)? - smartasset blog. SmartAsset.

There are, of course, certain types of assets for which no information exchange is required. Investments in kind, such as real estate and non-debt equity investments, are not included in the declaration. Information regarding investments in overseas property, (craft) collectibles, company shares, precious metals, and other value-protected products in an individual's name is not exchanged. A report is not required for the categories of term and critical illness insurance.

## 5.2 Consequences of The Failure to Disclose Tax Information

It has long been a principle of the Chinese Personal Income Tax Law that tax is levied on income of tax residents in China that originates from within and outside the country.<sup>40</sup> Previously, it was not possible for individuals outside of China to declare their income adequately for tax purposes, primarily due to a lack of tax collection capacity. Prior to the exchange of tax information, the tax authorities were unable to obtain accurate information regarding the status of a person's property abroad which caused difficulty in recovering tax due in respect of income earned abroad. Through the exchange of international tax information, tax authorities are able to obtain information regarding resident taxpayers' offshore accounts automatically. If they fail to file their tax returns, these taxpayers are liable. The Tax Collection and Administration Act (TCA) specifies that the tax authorities may impose a fine on the taxpayer in addition to the amounts owed for taxes that were not paid or underpaid.<sup>41</sup> "A person who commits the offense of tax evasion is subject to a maximum penalty of imprisonment for a term of not less than three years and not more than seven years and a fine pursuant to Article 201 of the Criminal Law".<sup>42</sup>

<sup>40</sup> 中华人民共和国个人所得税法 (1980) [Individual Income Tax Law of the People's Republic of China (1980)] Retrieved October 20, 2022

<sup>41</sup> 根据《税收征收管理法》第 64 条规定,“纳税人不进行纳税申报,不缴或者少缴应纳税款的,有税务机关追缴或者少缴的税款、滞纳金,并处不缴或者少缴的税款百分之五十以上五倍以下的罚款” 中华人民共和国税收征收管理法. (n.d.).[ According to the "tax law" the 64th regulation, "taxpayer to tax returns, not capture is little perhaps of payable taxes, the tax authorities have recovered, or pay less tax, fine for delaying payment, and not to pay or pay less tax fines of more than five times the fifty percent of the" tax administration of the People's Republic of China] Retrieved October 20, 2022.

<sup>42</sup> 根据《刑法》第 201 条的规定,“纳税人采取欺骗、隐瞒手段进行虚假纳税申报或者不申报,逃避缴纳税款数额较大并且占应纳税额百分之十以上的,处三年以下有期徒刑或者拘役,并处罚金;数额巨大并且占应纳税额百分之三十以上,处三年以上七年以下有期徒刑,并处罚金”;“有第一款行为,经税务机关已发下达追缴通知后,补缴应纳税款,缴纳滞纳金,已受行政处罚的,不予追究刑事责任;但是,五年内因逃避缴纳税款受过刑事处罚或者被税务机关给予二次以上行政处罚的除外” 刑事诉讼法第 201 条规定的合理性\_中华人民共和国最高人民检察院. (n.d.). According to Article 201 of the Criminal Law, "Taxpayers who evade paying a relatively large amount of tax and account for more than 10 percent of the tax payable by making false tax returns or failing to make tax returns by means of deception or concealment shall be sentenced to fixed-term imprisonment of not more than three years or criminal detention and shall also be fined; If the amount involved is huge and accounts for more than 30 percent of the tax payable, he shall be sentenced to fixed-term imprisonment of not less than three years but not more than seven years and shall also be fined "; "No criminal responsibility shall be investigated for any person who, after a notice of recovery has been issued by the tax authorities for the act referred to in the first paragraph, makes up the taxable tax and pays the overdue fine and has been subject to administrative punishment; However, those who have received criminal punishment for evading tax payment within five years or who have been given more than two administrative punishments by tax authorities shall be excluded "Reasonableness of Article 201 of the Criminal Procedure Law \_ Supreme People's Procuratorate of the People's Republic of China. (n.d.). Retrieved October 19, 2022.

Many HNWI's in China once again sought offshore tax avoidance in response to the 'two-pronged' anti-avoidance rules of the CRS and the revised Personal Income Tax Law in the last two months of 2018. In an effort to avoid taxation, they upgraded offshore structures by setting up offshore family trusts in countries that do not participate in the CRS. Singapore has been implementing a Registrant of Beneficial Ownership regime since March 2017, which requires the establishment of a registry of beneficial ownership information for all types of companies, partnerships, and other business entities, including non-resident companies, and an anti-money laundering system. According to the central register<sup>41</sup> system that was to be implemented in 2020, the companies, partnerships, and non-resident enterprises listed above will be required to register beneficial ownership information centrally on a website designated for 'beneficial ownership' by the Accounting and Corporate Regulatory Authority of Singapore (ACRA)<sup>42</sup>. It is necessary to register 'beneficial owners', who own or control a company in a material or significant manner. Singapore since delayed the registration of the Central Register from May 2020 to July 2020.<sup>43</sup> During 2018, the Cayman Islands and British Virgin Islands enacted the International Tax Cooperation (Economic Entities) Act<sup>3</sup> and the Economic Entities (Companies and Limited Partnerships) Act<sup>4</sup>, respectively.<sup>44</sup> As a result, Chinese tax authorities will be able to track the tax responsibilities of Chinese residents in the Cayman Islands and British Virgin Islands more easily.

Because the CRS has not yet been implemented in the US, some tax planners advise Chinese HNWI's to transfer their overseas funds there. Would this be an effective tax-avoidance strategy?

The OECD, in explaining the relationship between the CRS and FATCA, notes that the US has already begun exchanging information under FATCA, and that China and the US have also begun exchanging information about tax-related accounts since 2014. Consequently, China and the US have confirmed that the date of exchange of account information based on FATCA is the date of tax transparency for HNWI's moving to the US. Transferring financing assets to the US to avoid CRS is not a sustainable compliance solution. As a result, in the new era of global tax information transparency following the optimisation of anti-avoidance rules for personal income taxes, HNWI's cannot obtain any favoritism or shelter from financial institutions in countries adopting the CRS rules, even as VIPs. Sustainable and holistic tax planning based on compliance is the only way to protect an individual's assets. Even though information has been exchanged, many high-net-worth individuals continue to transfer their financing assets to the United States and establish offshore family trusts in order to avoid the anti-avoidance requirements of the new rules. Presidential Income Provisions is a disclosure rule that requires taxpayers and preparers to notify tax authorities of potentially malicious or abusive tax planning arrangements as soon as possible. Information required to be disclosed to the parties to the transaction includes fundamental information about the parties involved, the name of the

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<sup>43</sup> 《2000 亿资金蜂拥离岸信托雷军等富豪“移师”境外》 [Rich people like Lei Jun 'move' Overseas]

<sup>44</sup> 《新加坡注册局 (ACRA) 宣布新政策“实际控制人”》 [Registration Authority of Singapore (ACRA) Announces New Policy as "Actual Controller"]

<sup>43</sup> International Tax Co-operation(Economic Substance) Act,(2021)

<sup>44</sup> Economic Substance (Companies and Limited Partnerships) Act,(2019)

transaction, the manner in which the transaction was conducted, and the method by which the expected tax benefit was realised. By obtaining this information, the tax authorities can identify the preparer and the user of the planning arrangement at an early stage and enhance the efficiency of the tax authorities in compliance activities such as risk assessment, tax audit and legal improvement. In the event that a taxpayer's behaviour changes, the tax authorities can respond quickly through the use of the mandatory disclosure rule, which can serve as a deterrent to taxpayers and intermediaries.

It should be noted that the CRS mandatory disclosure rules do not affect the substantive provisions of the CRS legislation in individual countries. The primary purpose and function of this information collection tool is to ensure the integrity of CRS information reporting by discouraging intermediaries from promoting specific tax planning schemes, and to enhance compliance with the CRS information reporting obligations of all participants.

## **VI. Current Status and Deficiencies of Tax Disclosure in China**

There are complex investigation procedures, tight deadlines, and high investigation costs in financial institutions. These factors can hinder tax disclosure in China, affecting the quality of tax-related information. The anti-avoidance provisions still have flaws, and although it can close the loopholes, its provisions are insufficient. In addition, the difficulty in accessing tax-related information in China today constitutes a significant barrier to the recovery or to the proper declaration of income.

China has signed a number of agreements concerning offshore double taxation and the exchange of tax information, but the exchange and use of the information is inefficient. Further, the current tax information exchange focus is primarily on legal persons rather than natural persons, and as a result, high-net-worth individuals have been less targeted. The information exchange provisions in tax treaties are in fact not very effective in preventing high-net-worth individuals from avoiding taxes.

China's anti-avoidance efforts present a number of challenges.

- 1) The anti-avoidance provisions are only preliminary legislation and are not very effective;
- 2) The tax administration has difficulty providing sufficient support for anti-avoidance efforts;
  - a. High-net-worth taxpayers lack practical tax administration tools
  - b. Tax-related information is difficult to access
- 3) Further improvement is needed in the level of international cooperation in combating tax avoidance.

## VII. Experience in Other Countries

In China, where the disclosure of tax information has been poor, it is helpful to learn how other countries have handled this issue. In 1861, the United States passed the Tax Act requiring the disclosure of tax assessment information, which led to the tax information disclosure in foreign countries. Ever since that time, there has been a heated debate in many countries regarding the disclosure of tax information. The following two aspects are primarily responsible for its development.

### *7.1 the Need For Disclosure of Corporate Tax Information*

Pointer (1973) examines the disclosure issues associated with corporate tax policies from an accounting perspective, arguing that companies must disclose the financial impact of their tax policies.<sup>45</sup> Weidenbruch (2004) discusses the role of the IRS in disclosing tax information to poor people, as well as the principles and difficulties associated with such disclosures. In this article, he discusses whether tax information should be disclosed, the principles on which the rules are based, as well as the difficulties associated with such disclosure.<sup>46</sup> He argues that taxpayers should have confidence in and understanding of the tax system, despite the problems associated with the disclosure of private tax information. Combined reporting entails combining the corporate income tax of the parent company and multiple subsidiaries into a single entity, consolidating profits on a national basis. Through this policy, better tax information will be made available to the public, and corporate tax avoidance policies rendered ineffective. The article also examines the tax avoidance policies of a number of corporations. It explains how integrated reporting has contributed to the creation of a tax environment in which companies pay corporate income tax fairly. By adopting these policies, improper disclosure of tax return information can be reduced, and the associated financial and reputational risks can be reduced.

### *7.2 Status and Content of Corporate Tax Information Disclosure*

Following SEC Release No. 149 in 1973, Stickney (1979) studied the significant changes in the corporate income tax information required to be disclosed in annual reports.<sup>47</sup> A number of critical issues remained unresolved, including the measurement of income tax expenses for group companies. The issues of application of specific criteria for reversing differences between accounting and taxable income, and the disclosure of current income tax effects when deferred income tax expenses also arise. The changed policy provides recommendations for improving the measurement of income tax expense and the disclosure of income tax information by means of an analysis of a list of annual reports.

Using US GAAP Statement 109 on Income Taxes as a basis, Hanlon (2002) conducted a comprehensive study of Microsoft, Cisco and General Motors' income

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<sup>45</sup> Pointer, L. G. (1973). Disclosing corporate tax policy. *Journal of Accountancy (pre1986)*, 136(000001), 56.

<sup>46</sup> Thompson, R. B., & Langevoort, D. C. (2012). Redrawing the Public-Private Boundaries in Entrepreneurial Capital Raising. *Cornell L. Rev.*, 98, 1573.

<sup>47</sup> Clyde P Stickney. Current Issues in the Measurement and Disclosure of Corporate Income Taxes[J].The Accounting Review, 1979(2):421-433.

tax disclosures for 2002.<sup>48</sup> The three companies were found to not fully comply with Statement 109 regarding income tax disclosures, and the changed policy was the existence of the 109 standard itself.

A study conducted by Shackelford & Slemrod (2003)<sup>49</sup> studied the history of tax return disclosure and assessed the public disclosure of corporate tax return information from an accounting, economic, and legal perspective, concluding that full disclosure of income tax return data is not appropriate. The income statement can disclose taxable gains and losses or reconcile taxable gains and losses with accounting gains and losses.

According to Levi and Nissim (2004), accounting-tax differences are classified based on the profitability of a company, whether it is domestic or foreign, as well as its industry, and the difference between accounting and tax earnings is greater for profitable companies than for loss-making companies.<sup>50</sup> The study found that the difference between accounting earnings and taxable income was more significant for profitable companies than for loss-making companies. It was concluded that disclosure of the difference between accounting earnings and taxable income would improve transparency in accounting information and facilitate decision-making by users of financial reports.

Nevius (2010) notes that the IRS had issued interim proposed regulations that expanded the circumstances in which the preparer may disclose or use tax return information.<sup>51</sup> The IRS had also issued two revenue regulations exempting tax return preparers from criminal or civil liability in connection with the disclosure or use of tax return information in accordance with Sec. 7216. Tax return preparers were prohibited from knowing or recklessly disclosing tax return information pursuant to Section 7216. A violation of Section 7216 could result in criminal charges, including \$1,000, one year of imprisonment, or both, as well as prosecution costs. This legislation prohibits tax return preparers from disclosing or using tax return information "knowingly or recklessly."

Through a company case study, Loraas and Key (2010) demonstrated issues related to income tax accounting calculations and disclosures.<sup>52</sup> These authors argued that to improve corporate tax disclosures, spreadsheets and word processing tools should be used to create footnote disclosures of tax information.

August (2013) states that the IRS required corporate taxpayers to disclose a certain amount of information regarding their income tax return status, which was a new

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<sup>48</sup> Michelle Hanlon. What Can We Infer about a Firm's Taxable Income from Its Financial Statements [J]. 863.

<sup>49</sup> Lenter, David, Douglas. Shackelford, Joel Slemrod. Public Disclosure of Corporate Tax Return Information: Accounting, Economics, and Legal Perspectives [J]. National Tax Journal, 2003, 56(4):803-830.

<sup>50</sup> Baruch Lev, Doron. Nissim, Taxable income, future earnings, and equity values [J]. The Accounting Review (October), 2004:1039-1074.

<sup>51</sup> Alistair M. Nevius, J.D., IRS Issues Regs. and Guidance on Disclosure of Tax Return Information [J]. The Tax Adviser March (February), 2010:157-159.

<sup>52</sup> Tina M. Loraas and Kimberly Galligan Key. Integrating AIS and Accounting for Income Taxes: From Calculation to Disclosure [J]. Accounting Education, 2010, 25(3):583-597.

weapon in the fight against tax avoidance.<sup>53</sup> Fixed assets with a fair market value of over US\$1 billion were required to be declared as unique and disclosed on the tax return in order to avoid an "uncertain" outcome – depending on the time of year. As a result, the first step was to determine whether a tax position should be reviewed on an ongoing basis based on its technical level. Further, any tax item for which there was more than a fifty percent probability that the tax benefits would not be realised should be treated as a tax reserve in the financial statements.

Since 2006, US public companies have been required to disclose uncertain tax positions (UTPs) under published accounting standards and FIN 48.<sup>54</sup> During early 2010, the IRS announced that it would require corporate taxpayers with assets of \$100 million or more to report their uncertain tax positions under the UTP list. Lipin (2011) analyses the causes of UTP and describes how UTP should be accounted for under GAAP and IFRS. Identifying unidentified tax positions is a new direction in the study of corporate tax information disclosure.

The American Bar Association ABA held its 36th Annual Tax Fraud Criminal Defense Conference in Las Vegas at the end of 2019. The conference was attended by ABA members, tax attorneys, judges, as well as senior Treasury Department and IRS officials. Known for his rigorous tax law credentials, IRS Commissioner Charles Rettig delivered an unprecedented speech at the conference that left American taxpayers around the world on notice as he warned them that “the days of filing disclosures of financial accounts and assets outside the United States are numbered and that the IRS' Easy Disclosure Program is about to expire”.<sup>55</sup> There was to be a new round of major audits, and audits launched to take stricter measures against U.S. taxpayers who failed to report or underreport their foreign bank accounts.

The OVDP is a program administered by the Treasury Department's Financial Crimes Investigation Task Force (FINCEN) and is implemented by the IRS.<sup>56</sup> Taxpayers participating in the OVDP program are primarily interested in the reduced tax rate of 27.5%, which is an attractive offer and an excellent opportunity. However, the FBAR mechanism generally deters U.S. taxpayers from participating in the OVDP program. As part of the U.S. tax system since the 1970s, sound reporting and disclosure rules have been established for overseas bank accounts owned by U.S. taxpayers. A tax compliance procedure for overseas financial accounts, FBAR, is led by FINCEN, the Financial Crimes Investigation Unit. In recent years, the regime introduced by FATCA, the IRS-led legislation, has increased anti-avoidance and anti-money laundering efforts on U.S. taxpayers' global financial assets, making it very difficult for Americans to hide their wealth.

In relation to disclosures of overseas bank accounts and overseas financial assets, it is important to mention the IRS's previously introduced OVDP particular disclosure program. OVDP has been in place since 2009 and requires taxpayers both abroad or

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<sup>53</sup> Jerald David August. Mandatory Disclosure Of Uncertain Tax Positions On Income Tax Returns Filed By Corporate Taxpayers: The IRS's New Weapon[J]. *The Practical Tax Lawyer*, 2011:7-12 [29].

<sup>54</sup> Lipin, I. A. (2013). Uncertain tax positions and the new tax policy of disclosure through the Schedule UTP. *Va. Tax Rev.*, 30, 663.

<sup>55</sup> *Commissioner Charles P. Rettig*. Internal Revenue Service. (n.d.). Retrieved October 20, 2022

<sup>56</sup> OVDP: (new) offshore voluntary disclosure requirements 2022. International Tax Attorn.

onshore to disclose their overseas financial assets and accounts in order to comply with tax compliance requirements. In 2011, 2012, and 2014, the program was introduced, revised, and implemented with good results. As of mid-2018, more than fifty-six thousand taxpayers had voluntarily enrolled in the disclosure program to declare and disclose financial assets and accounts. The IRS has since also identified over fifteen hundred taxpayers who knowingly evaded taxes during the program, and those individuals have paid a significant price for doing so.

## VIII. How Tax Disclosures Achieve Fairness

We will now discuss the principles of taxation, including fairness and efficiency. This article discusses the main principles of taxation and how the tax system can be made fairer and more efficient, allowing tax information to be monitored more effectively.

Despite the fact that tax efficiency and equity are both legal principles, they often conflict with each other. In order to ensure tax fairness, tax efficiency may have to be sacrificed, and vice versa. The bias towards fairness or efficiency may have to be weighed against the specific social context and background. However, as Meade (1993) points out, the idea of matching equity with efficiency is inspired by the work of a leading British scholar, Ward, in the 1960s in his book *Efficiency, Equity, and Property Rights*: Equity and efficiency must be properly matched.<sup>57</sup>

Fairness and efficiency are considered to be both dialectical and unified by academics.<sup>58</sup> Tax equity increases the size of the economic pie, yet the contradiction between tax equity and tax efficiency is reflected in the fact that pursuing economic efficiency and neglecting tax equity might neglect the wealth created by tax equity.

As a result of information exchange, the information asymmetry between tax authorities and taxpayers will change. Tax authorities will be able to access the tax-related information of taxpayers automatically through the exchange of information. The tax authorities are thus provided with the information they require when conducting antiavoidance investigations.

In order to achieve tax fairness, tax efficiency is an important factor. To achieve social equity, there must be a sufficient share of the economic pie, and it is not very sensible if complete equity hinders economic growth.

Tax efficiency is predicated on tax fairness.

It is difficult to maintain a stable social order without a degree of fairness, and efficiency is the primary indicator. There should be a balance between fairness and efficiency when it comes to offshore tax voluntary disclosure. An offshore voluntary disclosure scheme should strike a balance between providing sufficient disclosure incentives for non-compliant taxpayers and combating non-compliance. In order to

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<sup>57</sup> Meade, J. E. (1993). Efficiency, equality and the ownership of Property. *Liberty, Equality and Efficiency*, 21–81.

<sup>58</sup> Ward, I. (1994). Fairness, Effectiveness and Fundamental Rights: The Case for a Unified Administrative Law Within The European Community. *Touro Int'l L. Rev.*, 5, 279.

increase tax rates, governments may use instruments such as late payment fees for tax evasion and discounts for penalties. Delaying or failing to report income is an example of tax evasion, much like tax evaders borrowing from the government.

Late payment of taxes constitutes a loan, and that that gives them an unfair advantage. As a result, there would be a gap between similar businesses. An offshore voluntary disclosure regime should strike a balance between efficiency and equity. A 'tax pyramid' model for analysing public needs has been developed by Bouzenita and Boulanouar (2016), based on Maslow's hierarchy of needs. The model divides investors' needs into six levels, from high to low.<sup>59</sup>

1. Additional reporting requirements: the requirement for additional returns on certain investments.
2. The investment needs of individuals and families for medium and long-term life goals.
3. The need for continued growth of in the short to medium term.
4. Pensions are necessary to ensure a good standard of living during retirement.
5. In the event of an emergency.

For China to achieve fairness and efficiency, it must have a robust anti-avoidance regime. To strengthen supervision and accountability for the information declared, international exchange and cooperation should also be strengthened.

China must also enhance and clarify its anti-avoidance provisions. China must enhance the primary management of anti-avoidance activities.

- a. Establish a dedicated tax administration for high-net-worth individuals.
- b. Create a database of high-net-worth individuals' tax-related information.

Utilise the anti-avoidance experience of the United States, the United Kingdom, Canada, and other countries. The implementation of a mandatory disclosure mechanism for tax planning facilitates the detection of tax avoidance planning arrangements by the tax authorities as early as possible and to respond promptly to it. Such a mechanism will have a strong deterrent.

Enhance international cooperation on anti-avoidance measures.

There is a need for the Chinese government to strengthen the international exchange of tax information at the individual level. The Chinese government should also

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<sup>59</sup> Bouzenita, A. I., & Boulanouar, A. W. (2016). Maslow's hierarchy of needs: An Islamic critique. *Intellectual Discourse*, 24(1).

participate actively in global anti-avoidance initiatives. In order to improve the efficiency of anti-avoidance activities, tax authorities must have access to cross-border tax-related information of high net-worth individuals. The accelerated progress of economic globalisation and the in-depth development of international cooperation mean that it is necessary to expand the scope of tax information exchange agreements, improve the content of tax information exchange information, and initiate active campaigns to determine information such as the offshore assets of HNVIIs. It is impossible to combat tax avoidance by high-net-worth individuals without the support and cooperation of the international community. China should further strengthen its anti-avoidance cooperation with countries worldwide.

As reflected in the metallic pyramid model of tax compliance, in terms of compliance with the CRS information reporting obligations, those at the top of the pyramid are often few, but they have a strong incentive to plan to avoid the CRS reporting obligations, and they are the group that needs to focus on the mandatory disclosure requirements.

Many people are required to report under the CRS, but they are unaware of their reporting obligations, or may have misunderstandings and misconceptions, and belong to the group of people who are ‘ignorant but not afraid’.

To this end, it is recommended that an easy-to-understand version of the CRS compliance booklet be produced as soon as possible, converting complex rules into simple scenario-based questions and answers and demonstrating how standard practices have been used to avoid CRS reporting obligations. This would enable those who are willing to comply, to meet their compliance obligations more easily. It would also reduce the risk of individuals being lured into planning arrangements by unscrupulous intermediaries. Such a regime would allow tax authorities to deploy sufficient resources in order to fully respond to planning structures or arrangements involving mandatory disclosure.

The proportion of high-net-worth individuals in China is increasing because of the rapid development of society and the economy and the associated tax-related risks are also rising. The collection of large volumes of data with characteristics such as a variety of types, a low level of value density, and a fast processing speed is known as ‘big data’. Such data also enhances risk analysis. Through the correlation of data, it is possible to locate tax-related risks quickly and accurately, effectively reducing the risk of tax losses. Meanwhile, as the extent of information sharing increases, the automatic exchange of tax-related information on accounts (CRS) is implemented, more and more personal information, such as information on foreign assets and credit information, will be included in tax returns. In this context, it is important to consider and study how high-net-worth individuals can better manage their tax risks.

## IX. Tax Disclosure Implications for HNWI Asset Allocation in the Context of The Covid-19 Epidemic

There have been a series of "black swan effects"<sup>60</sup> on the capital markets as a result of the worldwide epidemic, and the market environment is currently in flux. A global recession, excessive issuance of money by the US government, and high inflation have been observed in recent years.<sup>61</sup>

According to the 14th Five-Year Plan<sup>62</sup>, China's GDP per capita will reach the level of medium-developed countries by 2035, as opposed to its current median GDP per capita of US\$24,500. How should HNWIs allocate their assets in order to maximise their wealth growth in 2021, the first year of the 14th Five-Year Plan?

The increased uncertainty brought about by the economic slowdown and unexpected epidemic has led to an unprecedented focus on risk prevention and control capabilities among China's high-net-worth individuals and middle-class families, and it is gradually becoming the consensus to ensure that quality of life will not be affected by unexpected events, through a more comprehensive asset allocation. Due to the current twin challenges of the epidemic and the economy, the government and the public are increasingly concerned about taxes. It is now common for governments worldwide to run large deficits and have levels of debt that are unprecedented. These circumstances have significant implications for national as well as global tax policies. Wealthy individuals have engaged in significant tax evasion by using opaque entities in recent years (including using low-tax jurisdictions and tax secrecy jurisdictions), leading to increased attention being paid to their taxation.

In the post-epidemic era, we found that it is important to protect the sound growth of assets and prevent the impact of significant shocks causing unanticipated risks to the wealth position of families and to the quality of family life. In order to meet different needs and investment patterns, household assets must be allocated reasonably.

High-net-worth individuals are not unfamiliar with tax havens and offshore centres. Traditional tax havens include countries such as Luxembourg, the Cayman Islands, Jersey, Ireland, Mauritius, Bermuda, Switzerland, Monaco, and the Bahamas. The gradual transparency of global taxation has meant that use of traditional tax havens has declined.

There are a number of new tax havens that offer favorable tax policies and other opportunities, such as status. With their status and other benefits that come with it, investors are given the right to travel freely. A tax-free haven can significantly reduce the tax burden on individuals and corporations. During the process, however,

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<sup>60</sup> Yarovaya, L., Matkovskyy, R., & Jalan, A. (2021). The effects of a "black swan" event (COVID19) on herding behavior in cryptocurrency markets. *Journal of International Financial Markets, Institutions and Money*, 75, 101321.

<sup>61</sup> Ron Surz. (n.d.). Money printing and inflation: Covid, cryptocurrencies and more. Nasdaq.

<sup>62</sup> Outline of the 14th five-Year plan (2021-2025) for national economic ... (n.d.). Retrieved October 19, 2022.

investors normally have to relocate to the destination, which is a disadvantage for many. Is it possible to achieve sensible tax planning without relocating?

Citizenship has become a much more valuable asset as a result of the Covid-19 epidemic. As a result of the Covid-19 and CRS, transfers of domestic assets abroad have also been restricted. HNWIs have realised that transferring assets overseas is not sufficient to protect their assets. The reason for this is that, under the general trend of CRS, the assets of the wealthy cannot be hidden. With the globalisation of lives and investments of HNWIs, asset information and tax information will remain 'naked' for the foreseeable future, with no privacy being maintained. Affluent individuals should engage in long-term planning with their advisors.

A second citizenship with a high degree of security, along with its advantages for global access, asset allocation, tax planning, and educational shortcuts, can provide an additional level of choice and protection in life. Having multiple identities as a 'global citizen' is not only safer, but also an important strategy for protecting wealth. Wealthy and middle-class investors should plan their taxes carefully, optimize their asset allocations, and diversify their investments. It is a proven hedge against volatility that having a second status is precisely one of the safest, most intelligent, and most sustainable investments that can be made at this point in time. Investment naturalisation programs in Montenegro, Saint Lucia, and Saint Kitts are first choices for those seeking a home that will protect their family and provide easy freedom of travel.

Saint Lucia is an ideal destination for investors looking to invest in offshore banking and financial products. The availability of a wide range of financial products, such as offshore accounts, trusts, and companies, and various other incentives, have made Saint Lucia a favorite destination for entrepreneurs and high-net-worth individuals.<sup>63</sup> Above all else, Saint Lucia is highly regarded for its ability to protect the privacy of its clients and companies in its region. Furthermore, Saint Lucia enjoys a good reputation and is listed on the EU 'tax allow' list. Investors are also attracted to the simplicity of the processes, the low annual fees, the flexible share structure, the low tax rates, the absence of tax treaties, and the common law regime in the United Kingdom.

A global crackdown on offshore finance has intensified since 2008, particularly in relation to accounts associated with tax-free havens. Many traditional offshore havens have disclosed information regarding their accounts as a result of pressure, sanctions, and coercion from major world powers.

Aside from its low tax rate, non-global taxation, and lack of inheritance or gift tax, Saint Kitts and Nevis is an ideal investment destination for those seeking tax advantages.<sup>64</sup> With a personal income tax rate of only 9%, Montenegro has one of the lowest rates in Europe. The tax rate on marine-related and tourism services is

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<sup>63</sup> International Offshore Jurisdiction spotlight - st. lucia as a tax haven. St. Lucia as a Tax Haven: Is St Lucia a Offshore Jurisdiction? (n.d.). Retrieved October 20, 2022.

<sup>64</sup> Saint Kitts and Nevis: A very beguiling tax haven. RiskScreen. (2022, April 6). Retrieved October 20, 2022.

7%, and the tax on real estate and estates is 3%, but is tax-free if transferred to children, parents, or spouses as a gift or inheritance.

In addition, Montenegro has signed double taxation avoidance treaties with more than forty countries/territories around the world.<sup>65</sup> There are very few barriers to entry for new businesses, and the labour force is well-educated and well-qualified. In order to ensure efficiency, a straightforward procedure has been developed for investors to follow, with the euro serving as the official currency, thereby eliminating the issues of money transfers and currency exchanges. Foreign investors have equal rights to local investors, privatisation is open to all, foreign companies may own a hundred percent of their properties. Montenegro has aligned itself with EU standards by adopting more than twenty business-related laws in preparation for EU membership.

## **XI. Limitations**

The study format was limited. As a result of the epidemic, it was not possible to conduct formal interviews, observe and confront respondents in order to obtain more accurate and direct information.

As a result of the chosen perspective, there are a limited number of cases in support of the theoretical analysis. Tax information is available from a limited number of sources. Since tax information is relatively confidential for both individuals and the government, there is relatively little information available in this field, and the sources of information (sources of information exchange between countries) are difficult to access in a timely manner. Combined with the novel international context of CRS, the issue of taxpayer information protection is relatively obscure both in the tax and civil law fields.

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