

# The Impact of China's Tax Policy Reform on the Gap between Rich and Poor

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**Abstract.** Common prosperity is the goal that the Chinese government is constantly striving for, and the reform of the tax system is the only way to achieve this goal. In the past ten years, China has continuously carried out tax reform and achieved good results. Previous scholars have conducted in-depth research on China's tax reform from multiple perspectives. Previous research has focused on the impact of tax policy on China's economic growth, exploring how taxes stimulate or constrain the development of different industries and regions. And early research focused on social equity issues, examining the impact of tax policies on income distribution, and how to reduce the social gap between rich and poor through taxation. These studies provide lessons and theoretical support for current tax reforms and provide a basis for future research. This article will start from two aspects: personal income tax reform and value-added tax reform, and analyze the impact of personal income tax and value-added tax reforms on the gap between the rich and the poor.

## 1. Introduction

Taxation is the backbone of national finances, providing funds for the government to provide public services and infrastructure. Regulation of the economy through taxation to promote growth and stability. The tax system can also be used to achieve social equality and reduce the gap between rich and poor. This is vital to maintaining the functioning of the country and promoting economic prosperity and social justice. However, the so-called equality is not egalitarianism. Egalitarianism has great negative effects and seriously affects efficiency. Tax reform can only make a trade-off between efficiency and equality [1]. In the past ten years, China has continuously carried out tax reform and achieved a series of achievements. One focus is the reform of the personal income tax system, including adjustments to the tax rate structure and thresholds. Regarding whether personal income tax can alleviate the inequality of income distribution, some relevant scholars have studied the equal opportunity effect of personal income tax in my country based on the empirical paradigm of equal opportunities in income distribution, and believe that reducing personal income tax can reduce the inequality Gini coefficient [2]. On the other hand, value-added tax reform has also attracted much attention. While ensuring that fiscal revenue remains unchanged, using value-added tax to replace social security payments for financing can improve income distribution and promote fairness to a certain extent [3]. In addition, the relationship between local finance and central finance and the reform of the tax collection and management

system are also topics that have attracted widespread attention and discussion [4]. China's tax reform faces some potential gaps and challenges. One of them is that local governments are highly dependent on finance, and reform needs to balance the relationship between local and central finances to ensure sustainable development of the local economy [5]. On the other hand, tax system complexity and opacity are also an issue, requiring clearer and simplified tax policies [6]. In addition, the development of emerging industries such as the digital economy may also cause the tax system to lag, requiring corresponding adjustments to adapt to the new economic form. These gaps require finding a balance in tax reform to ensure that the reform can promote economic development and maintain fiscal sustainability. Studying the impact of taxation on the gap between rich and poor is crucial because tax policy directly affects the distribution of wealth and social equity.

## 2. The impact of tax reform on inequality

### 2.1 China continues to deepen the value-added tax reform.

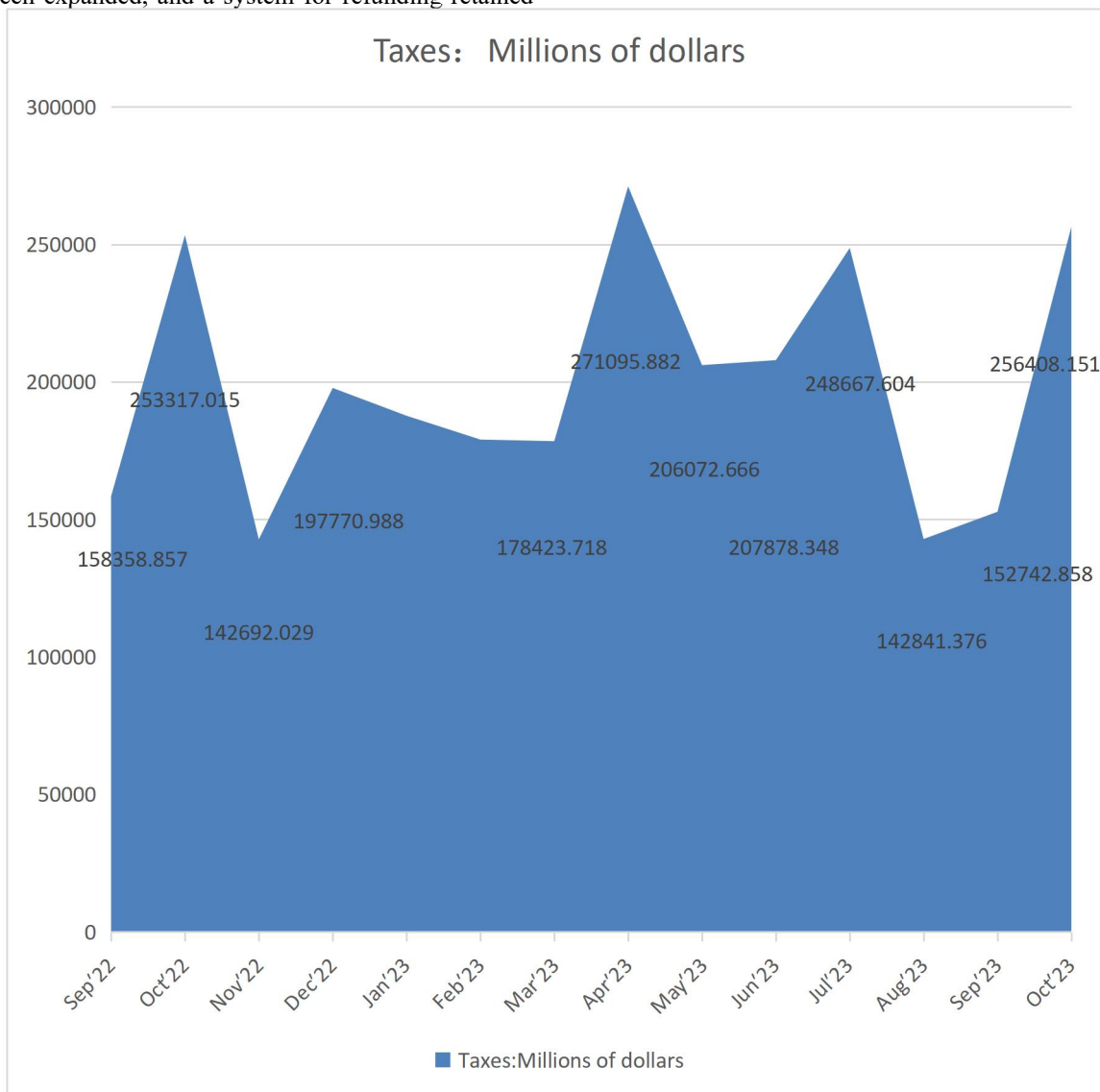
In 2012, the "business tax to value-added tax" pilot was implemented, and in 2016 the pilot was fully launched. In 2017, the 13% tax rate was canceled, and the four tax rates were simplified into three. In 2018 and 2019, the value-added tax rate was continuously reduced, starting from the "13th Five-Year Plan" During the period, the scale of domestic tax cuts and fee reductions exceeded 7.6 trillion yuan. By 2022, the new tax cuts fee

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reductions tax rebates, and tax deferrals will exceed 4.2 trillion yuan. This shows that the structural tax cuts policy has effectively alleviated the burden on residents. and the burden on enterprises [7].

tax at the end of the period has been established. While establishing a modern value-added tax system, the tax burden of all industries has been "only reduced but not increased", significantly reducing the tax burden of taxpayers [8].

At the same time, the scope of input tax deductions has been expanded, and a system for refunding retained



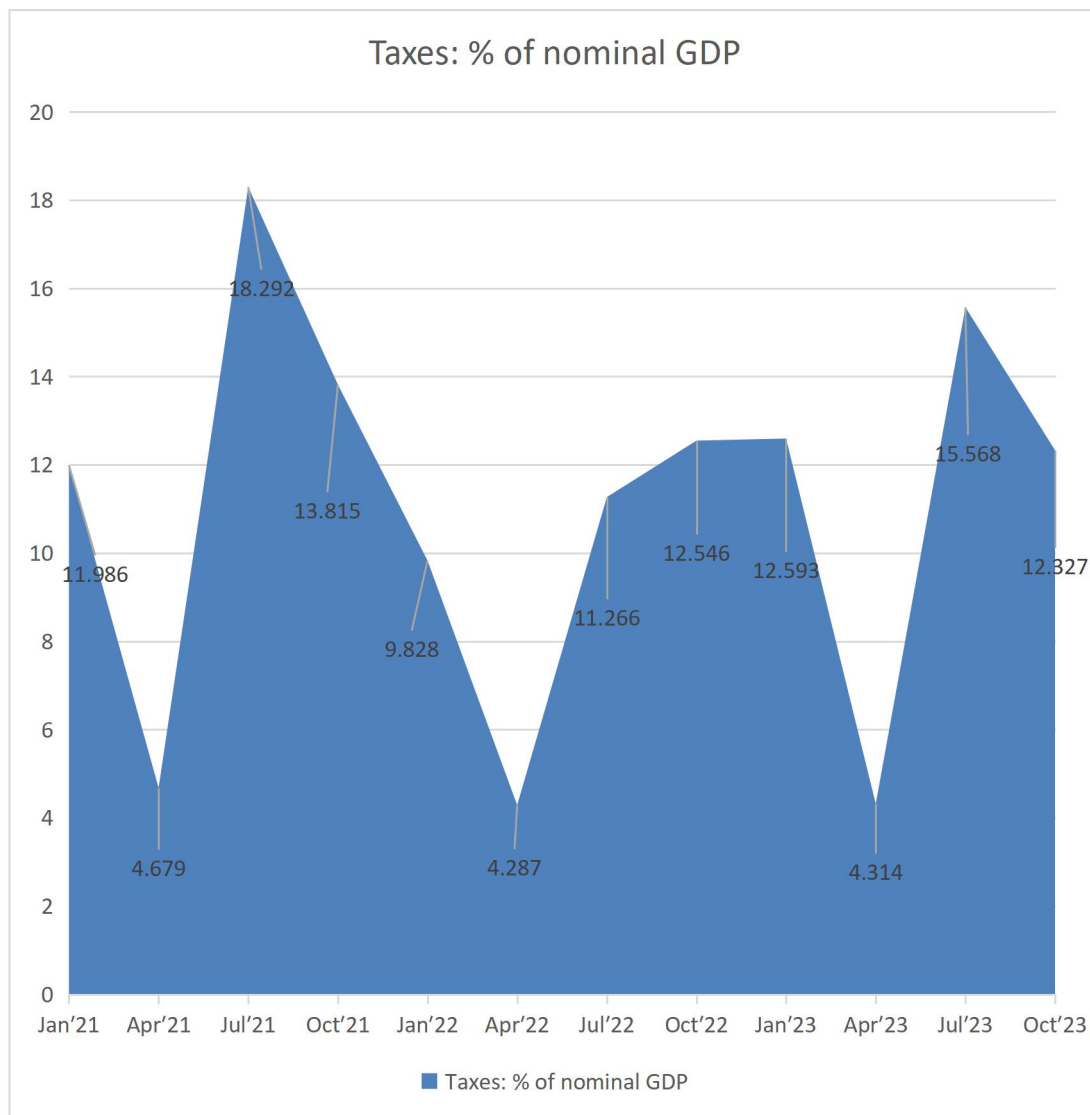
**Fig. 1.** China's taxes from 2022 to 2023 (Picture credit :Original )

As shown in Figure 1, it can be seen that taxes will be the highest in April 2023, and will be lowest in November 2022. The tax rate was the lowest in March. In the tax range from September 2022 to October 2023, the tax change has been rising to around 140,000 million dollars and then rising and has always been stable in the range of 140,000 million dollars to 250,000 million dollars float. Figure 2 can be analyzed in the same way. It can be seen that China's tax flexibility is relatively large and has good stability. As can be seen from the table data above, the Chinese government is implementing a cyclical tax reduction policy. This paper believes that tax and fee reductions will have a positive impact on promoting social equity and narrowing the gap

between rich and poor. Of course, there are also disadvantages. Please see the analysis below.

1. Promote consumption: Lowering the value-added tax may lead to lower prices for goods and services and encourage people to increase consumption. This could be good news for those at the bottom, whose living expenses are relatively high. After the country lowered the value-added tax, commodity prices fell, making it easier for lower-class families to purchase necessities, thus improving their living standards.

2. Stimulate small and micro enterprises: Reducing value-added tax may reduce the tax burden of small and micro enterprises, encourage their development and growth, and promote employment.



**Fig. 2.** Nominal GDP (Taxes:%) (Picture credit :Original )

If a country implements a differentiated value-added tax policy and provides larger tax reductions to small and micro enterprises, it will help these enterprises obtain more funds to expand their business and provide more employment opportunities. However

1. Benefits favor the rich: If the benefits of reducing the value-added tax mainly flow to high-income groups, it may widen the gap between the rich and the poor.

If the effects of falling commodity prices are felt more by wealthier households, while lower-income households fail to fully enjoy them due to other factors, the gap between rich and poor may further widen.

Overall, lowering VAT may have a positive impact on reducing the gap between rich and poor, but there is a need to ensure that its benefits reach more of those at the bottom, while balancing fiscal sustainability.

**2.2 China has implemented personal income tax reform to reduce the tax burden on low- and middle-income groups.**

The threshold for personal income tax has been raised, the scope of comprehensive income taxation has been clarified, special additional deductions have been established, the tax rate structure has been optimized and adjusted, and a personal income tax system that combines comprehensive and classified income has been initially established [5].

**Table 1.** Personal income tax rate table

| Level | Annual taxable income                 | tax rate (%) | quick calculation deductions |
|-------|---------------------------------------|--------------|------------------------------|
| 1     | Not exceeding 36,000 yuan             | 3            | 0                            |
| 2     | More than 36,000 yuan to 144,000 yuan | 10           | 2520                         |
| 3     | More than 144000 yuan to 300000 yuan  | 20           | 16920                        |
| 4     | More than 300000 yuan to 420000 yuan  | 25           | 31920                        |
| 5     | More than 420000 yuan to 660000 yuan  | 30           | 52920                        |
| 6     | More than 660000 yuan to 960000 yuan  | 35           | 85920                        |
| 7     | More than 960,000 yuan                | 45           | 181920                       |

As an important part of tax reduction and fee reduction, personal income tax reform is a key measure to adjust the gap between the rich and the poor. Raising the personal income tax threshold will have a positive impact on reducing the gap between rich and poor.

1. Reduce the tax burden on the bottom group: Raising the threshold can reduce the tax burden on the bottom group, allowing them to retain more income for living expenses. Raise the threshold for personal income tax. As shown in Table 1, the quick deduction number for annual income not exceeding 36,000 yuan is 0, allowing more low-income people to be exempted from personal income tax, which can increase their disposable income and improve their living standards.

2. Promote consumption: After the people at the bottom gain more disposable income, they may increase consumer spending, thus stimulating economic growth. Due to the increase in the personal income tax threshold, lower-income families have more funds available to purchase goods and services, which helps promote market activity. However, this behavior has a drawback, which is that it will affect fiscal revenue and thus the funding sources for public services and social welfare projects.

### 3. Conclusion

China's reforms to value-added tax and personal income tax have complex effects on the gap between rich and poor. VAT reform may help improve the living standards of people at the bottom by reducing the burden on businesses and promoting economic growth. However, care needs to be taken to ensure that the benefits of the reforms are more equally distributed and to avoid benefits flowing primarily to the wealthy.

Reform of personal income tax, especially raising the threshold, will help reduce the tax burden on low-income groups and encourage more people to share the fruits of economic growth. This is positive for narrowing the gap between rich and poor. However, policy implementation needs to be cautious to avoid benefits mainly benefiting high-income groups, thereby widening the gap between rich and poor.

Generally speaking, the impact of tax reform on the gap between rich and poor is related to specific policy

design and implementation. If we can ensure that reform measures benefit more people at the bottom, it will help reduce the gap between rich and poor by promoting economic growth and increasing the disposable income of low-income people. However, reform measures that lead to fiscal imbalances and cuts in social services should be avoided, so as not to negatively impact those at the bottom.

When implementing tax reform, social equity, economic growth, and fiscal sustainability need to be comprehensively considered to ensure that the reform effect is consistent with the overall economic and social development goals. Different tax reforms should be coordinated and coordinated to form a comprehensive tax policy to promote fair, inclusive, and sustainable economic growth, and ultimately reduce the gap between rich and poor.

Generally speaking, tax and fee reductions have a profound impact on the distribution of rich and poor in China. First, by reducing the tax burden on low- and middle-income earners and lowering corporate tax rates, this policy will help narrow the income gap and promote a more balanced distribution of wealth. As a result, low- and middle-income people can enjoy more real income, improve their living standards, and promote social equity.

Secondly, tax and fee reductions encourage business investment and innovation, creating more opportunities and jobs for the economy. This kind of economic growth will help improve the overall social welfare level, enable more people to share the fruits of development, thereby slowing down the widening trend of the gap between rich and poor.

In addition, tax and fee reductions will also help stimulate market vitality and promote the upgrading of the economic structure. By reducing the burden on enterprises and stimulating innovation and competition, it can not only promote industrial upgrading, but also provide more opportunities for more people and promote the development of poor areas.

Finally, the significance of tax reduction and fee reduction on the distribution of rich and poor in China is to promote social equity and improve the living standards of low- and middle-income people. At the same time, by promoting economic growth, it creates

opportunities for a wider range of people and helps achieve the goal of a comprehensively well-off society.

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