

Extended preferential policies of Deed tax and Land Value Added Tax are released to further benefit taxpayers in China

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In brief

On 5 March 2018, Premier Li Keqiang set out in the 2018 Government Work Report¹ to “extend the applicable period of preferential policies of Land Value Added Tax (“LVAT”) and Deed tax in enterprise restructuring”. To implement this, the Ministry of Finance (“MOF”) and the State Administration of Taxation (“SAT”) jointly released the Notice Regarding the Policy on Deed tax to Further Support the Transformation and Restructuring of Enterprises and Public Institutions (Caishui [2018] No.17, “Circular 17”)² and the Notice Extending the Land Value Added Tax (“LVAT”) Policy for Enterprise Transformation and Restructuring (Caishui [2018] No.57, “Circular 57”)³, extending the preferential policies of deed tax and LVAT in enterprise transformation and restructuring which expired at the end of 2017, and adjusting certain provisions. The valid period of Circular 17 and Circular 57 is from 1 January 2018 to 31 December 2020.

Circular 17 and Circular 57 further implement the State Council’s requirement of “continuously relieving enterprises’ tax burden”, and respond to the expectation of taxpayers. In this issue of China Tax and Business News Flash, we will introduce the key points of the two circulars, and share our observations and suggestions.

In detail

Generally, the transferee of a real property shall be subject to deed tax based on the transaction price at an applicable tax rate ranging from 3% to 5%, while the transferor shall be subject to LVAT based on the value-added amount at a progressive rate from 30% to 60%. In 2015, the MOF and the SAT have jointly issued two circulars, Caishui [2015] No.37 (“Circular 37”) and Caishui[2015] No.5 (“Circular 5”), providing a reduction/exemption treatment of deed tax, and a provisional exemption treatment of LVAT respectively for enterprises undergoing transformation and

restructuring. Both circulars expired on 31 December 2017.

The MOF and the SAT jointly released Circular 17 and Circular 57 recently to extend the preferential policies in Circular 37 and Circular 5 and make certain adjustments. We highlight below the key points of these two new circulars, and set out the preferential policies of deed tax and LVAT under various transaction types in the appendix.

Circular 17: Highlights of the deed tax policies

The newly released Circular 17 basically extends the deed tax incentives for several types of enterprise transformation and restructuring, including: transformation of enterprises and public institutions, merger, split, bankruptcy, asset assignment, debt-to-equity swap.

Circular 17 continues the deed tax exemption treatment for asset assignment. Meanwhile, it also includes a new article stipulating that the injection of capital by a parent company into its wholly-owned subsidiary with real property shall be deemed as an asset assignment and is eligible for the deed tax exemption treatment. This is good news to taxpayers.

Circular 57: Highlights of the LVAT policies

The newly released Circular 57 generally extends the provisional LVAT exemption policy on enterprise transformation as a whole, merger, spin-off, and investment with real property. It also clarifies and adjusts the following issues:

Provisional LVAT exemption policy shall not apply if either party to the real property transfer transaction is a real property development enterprise

Circular 5 stipulates that “the provisional LVAT exemption policy shall not apply to real property development enterprises”. Since LVAT is imposed on the transferor of a real property, the literal interpretation of this provision is that a real property development enterprise as a transferor party is not applicable to such LVAT incentive, however it does not clarify whether such incentive is applicable to a transfer where a real property development enterprise is the transferee. We understand that local-level tax authorities have different interpretations and implementations. Now Circular 57 clarifies this issue by stipulating that in an enterprise transformation and restructuring, the LVAT incentive is not applicable if either party to the real property transfer transaction is a real property development enterprise, which eliminates the inconsistent interpretation of this policy.

Concepts of “investors of the original enterprise remain unchanged”, “investors are the same as those of the original enterprise” and “investors of the original enterprise continue to exist” are clarified:

Under Circular 5, one criteria for enterprises to claim the LVAT preferential policy is “investors of the original enterprise remain unchanged” in an enterprise transformation as a whole, or “investors of the original enterprise continue to exist” in a merger, or “investors are the same as

those in the original enterprise” in a spin-off.

In that respect, tax authorities and taxpayers usually have tax disputes on whether the LVAT exemption is still eligible in the situation where there is a change in the original investors’ capital contribution ratio in the enterprise that acquired a real property from a transformation or restructuring as a result of a subsequent restructuring (such as capital injection by a new investor).

Now Circular 57 is released to clarify that “investors of the original enterprise remain unchanged” and “investors are the same as those of the original enterprise” mean that the investors themselves have to be the same, while the capital contribution ratio may vary after an enterprise transformation and restructuring. At the same time, “investors of the original enterprise continue to exist” means investors of the original enterprise have to continue to exist in the enterprise after an enterprise transformation and restructuring, while their capital contribution ratio may vary. Such clarification allows enterprises to flexibly apply for the LVAT preferential policy, which can substantially relieve their tax burden.

The takeaway

Circular 17 and Circular 57 extend the existing preferential treatment of deed tax and LVAT, and further clarify certain practical issues, which will help both tax authorities and enterprises to better understand and apply the relevant tax preferential policies.

As Circular 37 and Circular 5 have already expired on 31 December 2017, some tax authorities may have already required taxpayers to pay deed tax and LVAT on enterprise transformation and restructuring occurred on or after 1 January 2018. However, since the two new circulars took effect retrospectively from 1 January 2018, qualified taxpayers can theoretically apply for a refund of the deed tax and LVAT that have been paid. It is therefore recommended that the relevant taxpayers should discuss with their in-charge tax authorities so as to fully enjoy the tax policy benefits.

Endnote

1. *The 2018 Government Work Report*
<http://www.gov.cn/zhuanti/2018lh/2018zfgzbg/zfgzbg.htm>

Please refer to our News Flash [2018] Issue 8—An Observation of the Key Fiscal and Taxation Task in China’s Government Work Report in 2018
<https://www.pwccn.com/zh/services/tax/publications/chinatax-news-mar2018-8.html>
2. *Notice Regarding the Policy on Deed tax to Further Support the Transformation and Restructuring of Enterprises and Public Institutions (Caishui [2018] No.17, “Circular 17”)*
http://szs.mof.gov.cn/zhengwuxinxi/zhengcefabu/201803/t20180323_2847410.html
3. *Notice Extending the Land Value Added Tax (“LVAT”) Policy for Enterprise Transformation and Restructuring (Caishui [2018] No.57, “Circular 57”)*
http://szs.mof.gov.cn/zhengwuxinxi/zhengcefabu/201805/t20180518_2900807.html

Appendix:

Policies of Deed tax and LVAT on enterprise transformation and restructuring effective from 1 January 2018

Transaction Types	Deed tax policy (Circular 17) Note: the taxpayer is the transferee of a real property	LVAT policy (Circular 57) ¹ Note: the taxpayer is the transferor of a real property
Enterprise transformation	Exemption treatment if the more than 75% shareholding ratio criteria is satisfied	Provisional exemption
Public institution transformation	Exemption treatment if the more than 50% shareholding ratio is satisfied	No preferential treatment
Merger	Exemption	Provisional exemption
Spin-off	Exemption	Provisional exemption
Enterprise bankruptcy	Creditors inheriting the bankrupt enterprise's ownership of a real property are eligible for the exemption treatment; Qualifying non-creditors inheriting the bankrupt enterprise's ownership of a real property are eligible for the exemption treatment or 50% tax reduction	No preferential treatment
Asset assignment	The following transactions are eligible for exemption treatment: <ul style="list-style-type: none"> Inheriting state-owned land and houses assigned by governments above the county level; Real property assignment between enterprises within the same investor group; Injection of capital by a parent company into its wholly-owned subsidiary with a real property 	Investment with real property is eligible for the provisional exemption treatment
Debt-to-equity swap	For debt-to-equity swaps approved by the State Council, newly established enterprises inheriting real property are eligible for the exemption treatment	No preferential treatment

1. LVAT exemption treatment is not applicable to an enterprise transformation and restructuring where either party to the real property transfer transaction is a real property development enterprise.

Let's talk

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