

HR & Tax Alert



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China – Circular issued by the State Administration of Taxation on the Transfer of Housing Property in China

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Executive summary

On 18 July 2006, the State Administration of Taxation (“SAT”) issued a circular Guo Shui Fa (2006) No. 108 (“Circular 108”) to further clarify the individual income tax (“IIT”) rules relating to the gains derived from the sale of personal real property in China. It also provides definition on some key terms concerning the personal real property transfer. All such changes were effective on 1 August 2006.

Overview

The People’s Republic of China Individual Income Tax (“IIT”) treatment of the sale of personal real property has been covered in previous laws and regulations. However, due to lack of clear definitions of various terms such as sales proceeds and deductible items, implementation of the IIT treatment for gains derived from the sale of personal real property has been inconsistent.

Circular 108 provides clarification and definition on certain key terms and also the computation formulae for determination of the taxable gain and IIT payable in respect of the sale of personal real property in China. This is set out as follows:

Taxable Gains = Sales Proceeds – Cost – Reasonable Expenses

IIT Payable = Taxable Gains x 20%

Definitions of key terms

Sales Proceeds is defined in Circular 108 as the actual sales price for the transfer of personal real

property. The circular specifies that if the actual sales price is unreasonably lower than the market price, the local tax authorities would have the right to determine the amount of the sales proceeds.

Cost is defined as the consideration paid to purchase the real property (i.e. the “original value of the property”) which shall include transaction-related taxes and expenses that were incurred during the course of acquiring the property. According to Circular 108, the “original value of the property” is determined depending on the classification of “personal real property” as listed below.

- Commercial properties
- Self-constructed properties
- Economical properties
- Purchased public housing properties
- Re-development compensation properties

Transaction-related taxes refer to business tax, city maintenance tax, education surtax, land appreciation tax, stamp duty and any other taxes actually paid by the taxpayer.

Reasonable expenses refers to decoration costs, mortgage interest payments, administration charges, notary fees, handling fees etc. and other expenses actually incurred in relation to the property. Circular 108 provides for certain limitations to apply to the deduction of decoration costs which would depend on the classification of the property as mentioned above.

It is also stipulated in Circular 108 that where the taxpayer is unable to provide complete and accurate documentary proof for the “original value of the property”, the tax authorities may assess the IIT liabilities arising on the transfer of the property as an amount ranging from 1% to 3% of the total sales proceeds. For example in Shanghai, the deemed IIT rates for non-ordinary housing properties is 2% while the rate for ordinary housing properties, self-constructed properties, economical properties, purchased public housing properties and re-development compensation properties is 1%.

Exemption and Reduction Provisions

Circular 108 allows an exemption from IIT on gains from the sale of personal real property which has been held by the individual for over five years where the property is the individual’s sole residential property.

In other circumstances, if an individual intends to purchase a new home within one year from the date of the sale of the residential property, the individual may apply for a complete or partial refund of IIT paid in respect of any sales of residential property.

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