Real Estate Tax: Impact on China's Property Market

Timothy Chen Director | Research | East China

Jerry Shen Associate Director | Research | East China

The release of the upcoming real estate tax marks a crucial step forward in China's real estate tax reform, which is one of the long-term systematic changes intended to ensure the sustainable development of the real estate market. It is a core principle of the real estate tax reforms by the Central Government that holding tax will likely be increased while turnover tax will be lowered in the process of property development, construction and transactions. As a result, indirect taxes such as land appreciation tax (LAT) and administrative fee will probably be lowered, serving to ease the tax burden for developers and investors. Following the tax base changes to appraised value, higher tax burden will likely be exerted on property owners in cities with excessive home prices, which serves to curb speculative demand and promote the sound development of the real estate market.

Background Information

In December, the central economic work conference was held in Beijing, where the Central Committee set the tone for the 2018 economic development objectives. In the real estate sector, it was decided that efforts should be intensified to bring about the reform and long-term systematic establishment of the housing market. As one of the long-term systematic establishment changes, real estate tax reform has been put forth.

The legislation and implementation of real estate tax should be rolled out, said Xiao Jie, the Minister of the Ministry of Finance (MOF) in an article published in the People's Daily on 20 December 2017 where he stressed the establishment of a modern fiscal system in harmony with the thoughts and spirit of the 19th Communist Party of China (CPC) National Congress.

Xiao stated that real estate tax is scheduled to be rolled out by the principles that legislation work will be in place first, discretionary power should be granted to the local governments in the implementation level, and the implementation work will be moved forward city by city. In addition, real estate tax is proposed to be levied on the basis of appraised value for commercial, industrial and residential properties and the tax burden should be eased in the process of construction and transactions to gradually establish China's modern real estate tax system.

Under the principle of "legislation work in place first", the legislation work for the real estate tax is expected to start in 2018, but no specific timetables have been put forth for its official debut. Given the unbalanced real estate development across the country, discretionary power is likely to be delegated to the local governments regarding the applicable tax rate. The real estate tax is more likely to be started in fast-growing Tier 1 and 2 cities first and then extended to Tier 3 and 4 cities gradually.

Difference between property tax and real estate tax

Under the current tax regime, property tax is in place for the property holders, whose tax base is the adjusted book value (10%-30% deductible rate) or the rental income. The taxable properties cover industrial and commercial properties while residential properties are exempted with the exception of Shanghai and Chongqing where mid to high-end homes whose prices exceed the taxable thresholds are subject to property tax. The taxable object of the coming real estate tax is comprised of both land and property, whose tax base is the appraised value of both asset classes.

Property tax's tax bases for different properties:

Property type	Tax base	Applicable tax
Property for self-occupier	levy on book value	1.2% of 70% to 90% of book value
Investment property	levy on rental income	12% of the rental income

Source：PRC's Provisional Rules on Property Tax

*The deductible rate of 10% to 30% is subject to provincial, autonomous regions' and municipal governments' discretions.

Real estate tax's impact on China's real estate market

From the perspective of property owners, residential properties will also be included in the scope of taxation once the real estate tax is levied. We expect that the tax burden will rise notably in accordance with increasing property values as opposed to the levy on book values, assuming no significant changes on the applicable tax rate. As a result, there ought to be a certain impact on speculators with many homes in cities with high home prices. We expect that the pressure from the rising holding cost will compel speculators to reduce the number of homes on hand. This is conducive to increasing the supply volume in the residential market, curbing rising home prices and boosting the steady development of the housing market.

In addition, from the aspect of property development, indirect taxes such as land appreciation tax (LAT) and administrative fee will probably be lowered in the process of property development and transactions, serving to ease the tax burden for developers and investors.

From the perspective of the government's decision makers, since the real estate tax is imposed on the components of both land and property portions, duplicate impositions will occur if the existing land premium system takes hold. As a result, relevant tax reforms will also be progressed simultaneously to ensure the legality of the imposition of the real estate tax.

From the perspective of the industry development, we believe that the imposition of the real estate tax will play a crucial role in optimising resources allocation, eliminating rising stock, and boosting the sound development of the real estate industry. In addition, since the imposition of the real estate tax is based on the properties' appraised value, the new tax should bring numerous business opportunities to the real estate valuation field.

Overseas counterparts' practices

Real estate and/or property tax in typical countries or regions:

Country (Region)	Tax	Taxable property	Tax base	Applicable tax rate	Measurement
U.S.A	Real estate tax	Homes, farms, business premises, and most other real property	Assessed property value (market value times an assessment ratio)	Fixed rate：0%-4%	Assessed property value*tax rate
U.K	Council tax	Homes	Capital value	Subject to a fixed amount set by an assigned band	Capital value is divided into eight bands where a fixed amount is set for each band
Singapore	Property tax	Residential, commercial, industrial premises, etc	Annual rental income	Residential: self-use 0%-16% or otherwise 10%-20%; non-residential：10%	Annual rental income* tax rate
Hong Kong	Property tax	All properties (inc. private and public housing)	Annual rental income	Fixed rate: 5% for 2017-2018	Annual rental income* tax rate

Source: Colliers International

From the perspective of overseas counterparts' practices on real estate or property tax, the taxable properties cover almost all the properties in typical countries or regions except U.K where only residential properties are taxable. Tax bases are primarily measured by the property's appraised value or rental income generated by the property.

Most typical countries or regions enact progressive tax rates to ease the interests of different hierarchies and tax burden in the societies, and differentiate the applicable tax rates between the leased and vacant properties. For instance, the Council Tax in U.K will be uplifted in line with the increased property value, and 50% extra amount will be taken for homes vacant for more than two years in some counties.

Moreover, certain preferential tax policies will be granted to some special entities or groups. For example, in America, real estate taxes will be exempted or lowered on veterans and NGOs, and as an incentive for high quality companies or certain businesses to locate their premises, some jurisdictions will provide broad exemptions for businesses located within certain areas.

These overseas practices will pose a guidance to China's coming real estate tax. It should be taken into account by our decision-makers that certain discretionary powers are granted to local governments to ease the imbalanced real estate development in different regions.

For more information:

Tammy Tang
Managing Director
Executive Director | Industrial Services | China
+86 28 8658 6288
Tammy.Tang@colliers.com

Andrew Haskins
Executive Director
Research | Asia
+852 2822 0511
Andrew.Haskins@colliers.com

Timothy Chen
Director
Research | East China
+86 21 6141 3550
Timothy.Chen@colliers.com