

# *CPA-Lawyers*

2024, Issue No. 9

Cumulative No. 254 (Chinese Edition)

ForTran Lawyers —

*Professional Lawyers with Expertise in Finance and Taxation*

## Table of Contents

- **Insight: *Can the Net Assets of a Branch Be Used for the Capital Contributions to a Wholly Owned Subsidiary?* by Susan Yang, p. 02**
- **Q&A: *How Should Real Estate Enterprises Account for the "Land Cost" When Settling Land Value-Added Tax (LVAT)?* by Clara Yang, p. 04**
- ***Regulatory Updates* by Man Xu, p. 07**
- ***ForTran News* by Lawrence Sun, p. 12**

**Editor-in-Chief of This Issue:** Susan Yang

**Editorial Board Member of This Issue:** Clara Yang, Lawrence Sun, Man Xu

## Insight: Can the Net Assets of a Branch Be Used for the Capital Contributions to a Wholly Owned Subsidiary?

By Susan Yang

Recently, a client inquired whether it is possible to use the net assets of a branch to contribute to a wholly owned subsidiary when transferring the branch's assets, liabilities, and personnel to the subsidiary. The client mentioned that many listed companies seem to have adopted this practice. In addressing this query, it is essential to clarify whether net assets meet the legal requirements for capital contribution.

### Legal Perspective on Forms of Capital Contribution

Net assets, in their legal context, do not satisfy the statutory requirements for forms of capital contribution. Article 48 of the Company Law (2023 Revision) stipulates that "shareholders may make capital contributions in cash, or in the form of non-monetary assets that can be monetarily appraised and legally transferred, such as physical assets, intellectual property, land use rights, equity, or receivables. However, assets that are prohibited by law or administrative regulations from being contributed are excluded." This provision highlights that capital contributions must consist of specific assets. In contrast, "net assets" refer to the residual value of a company's total assets after liabilities are deducted, serving as an accounting measure of an entity's overall financial position. It is not a specific transferable asset and therefore cannot qualify as a form of capital contribution.

### Potential Misunderstanding of Contributions based on Book Value

Given the client's mention that many listed companies engage in asset transfers and use net assets for contributions, I researched related announcements from listed companies. Upon reviewing these announcements, I found that they referred to making contributions based on book value instead of using net assets. Below are three examples from companies registered in different provinces:

#### 1. November 2022: Guangdong Shantou A Co., Ltd.

In its announcement titled "Announcement on the Transfer of Assets, Liabilities, Business, and Personnel from a Branch to a Wholly-Owned Subsidiary, Capital Increase in the Subsidiary, and Subsequent Deregistration of the Branch," the company disclosed that it planned to transfer the assets, liabilities, and personnel of its Copper-Clad Laminate Plant branch to its wholly-owned subsidiary, Ultrasonic Copper-Clad Laminate, based on the audited book value as of September 30, 2022. Ultrasonic Copper-Clad Laminate would assume all related assets, liabilities, businesses, and personnel from the branch. Upon completion of the transfer, the Copper-Clad Laminate Plant branch would be deregistered. The transferred assets included real estate and land-use rights, as listed

in the appendix to the Asset Transfer and Capital Increase Agreement between the company and Ultrasonic Copper-Clad Laminate.

Based on the audited book value as of the reference date (September 30, 2022), the total book value of the transferred assets was RMB 567.5565 million. Of this, RMB 379 million was subscribed to the increase in registered capital of Ultrasonic Copper Clad Laminate, and the remaining RMB 188.56 million was recorded as capital reserve of the subsidiary. Any changes in assets and liabilities between the benchmark date and the actual transfer date would be adjusted based on the actual situation. The final assets and liabilities transferred would be subject to the results of the implementation.

## **2. December 2022: Jiangsu B Co., Ltd.**

Jiangsu B Corporation issued "Announcement on the Reorganization of a Wholly Owned Indirect Subsidiary into a Wholly Owned Direct Subsidiary and the Transfer of Certain Branch Assets to the Subsidiary," which disclosed the following:

The company planned to transfer the assets, liabilities, businesses, and personnel related to its dye business from the Lianyungang Branch to Jiangsu X Limited, a wholly owned subsidiary of B Corporation. The transfer would be based on the audited book value of the assets and liabilities as of the reference date and would serve as a capital increase for Jiangsu X Limited. This reorganization would not alter the substantive business operations of the transferred assets.

Under the plan, the assets and liabilities transferred at their audited book value as of the reference date would be contributed as follows: the real estate assets would be contributed as paid-in capital in the amount of RMB 100 million, while any excess value will be recorded as capital reserve. Other transferred assets and liabilities will also be recorded as contributions to the capital reserve.

## **3. November 2021: Zhejiang C Co., Ltd.**

In its announcement titled "Announcement on the Transfer of Assets, Liabilities, and Personnel from a Branch to a Wholly Owned Subsidiary and the Change of Certain Fundraising Projects' Implementation Entities.", Zhejiang C company disclosed:

It planned to transfer the assets, liabilities, and personnel related to the fine chemical intermediate business of its Taizhou New Agricultural branch to its wholly owned subsidiary, New Agricultural Technology, based on the unaudited book value as of October 31, 2021. New Agricultural Technology would assume all relevant assets, liabilities, businesses, and personnel from the branch. Following the completion of the transfer, the Taizhou New Agricultural branch would be deregistered. The transferred assets included real estate and land-use rights, as detailed in the appendix to the Asset Transfer and Capital Increase Agreement signed by the company and New Agricultural

Technology.

Based on the unaudited book value as of October 31, 2021, the total value of the transferred assets was RMB 107.4167 million. Of this, RMB 99 million was subscribed to the increase in registered capital of New Agricultural Technology, and the remaining RMB 8.4167 million was recorded as capital reserve. The final transferred assets and liabilities were subject to adjustments based on their actual status on the transfer date.

### **Clarifying the Nature of "Contributions Based on Book Value":**

In the above cases, assets used for contributions were specific assets such as real estate and land use rights that were listed item by item in the agreements. Their book value was used as the basis for valuation when making capital contributions to the subsidiary. This aligns with Article 48 of Company Law (2023 Revision), which requires the valuation of non-monetary assets for capital contributions

The difference between all assets and liabilities transferred from the branch to the subsidiary does constitute net assets. However, this does not mean that the net assets themselves were used as the contributed assets. As explained earlier, net assets are merely a financial benchmark for reflecting the overall financial position of the transferred assets; they are not specific assets, therefore cannot be used directly for capital contributions.

## **Q&A: How Should Real Estate Enterprises Account for the "Land Cost" When Settling Land Value-Added Tax (LVAT)?**

**By Clara Yang**

Recently, the attorneys at our firm have encountered several contentious cases related to the land value-added tax (LVAT) settlement for real estate enterprises. Most of these revolve around the recognition and allocation of "land cost". Land value-added tax is one of the most significant taxes for real estate enterprises, characterized by a high tax rate, a complex and varied basis for assessment, and a long settlement cycle. Land costs typically represent a substantial portion of the development costs, and the determination of the deductible amount and the method of deduction can significantly impact the amount of LVAT. This article provides a brief analysis of key issues surrounding land cost accounting in LVAT settlements.

### **1. Settlement Unit**

The "Notice on the Administration of Land Value-Added Tax Settlement for Real Estate Development Enterprises" (State Administration of Taxation [2006] No. 187) first introduced the concept of the "settlement unit." Article 1 of this notice stipulates that LVAT settlement is conducted on a per real estate development project basis, as approved by

relevant state authorities. For phased development projects, settlement is performed on a per phase basis. Additionally, Article 17 of the "Notice on Issuing the Regulations on Land Value-Added Tax Settlement Administration" (State Administration of Taxation [2009] No. 91) specifying that, during the settlement review, it should be checked whether the real estate development project is being settled on a per approved project basis and whether phased developments are being settled on a per phase basis. It should also be confirmed whether different types of real estate are treated separately for the calculation of value-added amount and tax rate.

While the national regulations establish the basic framework for defining the "settlement unit," they do not provide clear guidance on the specific form in which "approval by the relevant national authority" should be expressed. Furthermore, the concepts of "phased development" and "phased project" are not explicitly defined in these regulations. Instead, the regulations provide an authorization clause: "Local tax authorities may develop specific settlement management measures based on the provisions of this notice and local circumstances." As a result, local tax authorities have been granted the discretion to formulate specific measures tailored to local conditions. This has led to regional variations in how the "settlement unit" is determined.

In practice, local governments have adopted different standards for determining settlement units, which are generally based on one or more of the following documents: the "Construction Land Planning Permit," the "Construction Engineering Planning Permit," the "Building Construction Permit," or approval documents from the National Development and Reform Commission. These standards vary from province to province.

## **2. Allocation of "Land Costs"**

From the perspective of the state policy, taxpayers may allocate costs using a reasonable method based on the principle of the benefiting object. Article 21 of the "Notice on Issuing the Regulations on Land Value-Added Tax Settlement Administration" (State Administration of Taxation [2009] No. 91) stipulates that, for projects developed in phases or for multiple projects developed simultaneously, or for a single project containing different types of real estate, costs should be allocated based on the benefiting object using reasonable allocation methods. Article 9 of the "Implementation Rules of the Interim Regulations on Land Value-Added Tax of the People's Republic of China" (Finance Law [1995] No. 6) stipulates that if a taxpayer acquires land use rights in bulk and subsequently develops or transfers real estate in stages or batches, the determination of the deductible amount may be calculated on a pro-rata basis either by the ratio of the area of the transferred land use rights to the total area, or by the building area, or by other methods confirmed by the tax authority.

Common methods for allocating the deduction items of land value-added tax include: the building area method, the land area method, and the direct cost method. The building area method allocates costs based on the ratio of the building area of the real estate

project to the total building area. The land area method allocates costs based on the ratio of the land area of the real estate project to the total land area. The direct cost method directly accumulates costs based on the benefiting object or settlement unit. The method of allocation directly affects the deductible items for the settlement unit, which in turn influences the value-added amount, the value-added rate, and the applicable tax rate, ultimately affecting the amount of LVAT payable.

Typically, when different types of real estate are developed on separate parcels of land, it is more appropriate to allocate land costs using the land area method. In contrast, when a building contains different floors or different sections with varying types of use, it is more reasonable to allocate costs based on the building area method.

In some provinces and cities, regulatory documents on LVAT allow for the direct cost method to be prioritized. When costs can be directly attributed to a cost object, they should be directly included in the cost. Only when direct attribution is not possible should allocation methods be used. For example:

The "Announcement on Several Issues Concerning Land Value-Added Tax" (Jiangsu Provincial Local Taxation Bureau Announcement [2015] No. 8) stipulates that, when allocating land costs between different settlement units or between different types of real estate within the same unit, costs that can be directly attributed should be included directly in the land cost of the relevant settlement unit or type of real estate. If direct attribution is not possible, allocation may be made using the building area method or other reasonable methods recognized by the tax authorities.

However, relevant documents in Shandong Province stipulate that, when land costs are allocated using the direct cost method, the land must be governed by independent land agreements to reflect the independence of its costs.

Announcement by the State Taxation Administration Shandong Provincial Taxation Bureau on the Issuance of the "Regulations on the Settlement Management of Land Value-Added Tax by the State Taxation Administration Shandong Provincial Taxation Bureau" (State Taxation Administration Shandong Provincial Taxation Bureau Announcement No. 10, 2022) states in Article 30 that deductible items for real estate development shall meet the following requirements: (6) The land costs and other costs and expenses within the same settlement unit shall be allocated based on the proportion of saleable building area for each type of real estate relative to the total saleable building area. For projects that can provide independent land transfer contracts, allocation agreements, or investment agreements, land costs may be directly attributed to the beneficiary object.

## Regulatory Updates

By Man Xu

### **I. Announcement on Stamp Duty Policies Regarding Corporate Restructuring, Reorganization and Institutional Reform (Announcement No. 14 [2024] by the Ministry of Finance and the State Taxation Administration)**

To support corporate restructuring, reorganization and institutional reform, further stimulate the intrinsic drive and innovative vitality of various market entities, and promote high-quality economic and social development, the following stamp duty policies are announced:

#### **1. Stamp Duty on Business Account Books**

(1) For newly established enterprises formed during corporate restructuring, reorganization or institutional reform, the paid-in capital (share capital) and total capital reserves recorded in their newly opened business account books shall be exempt from further stamp duty for the portion that has already been taxed. The unpaid portion and any subsequent increases must be taxed as prescribed.

(2) Increases in paid-in capital (share capital) and total capital reserves resulting from debt-to-equity conversions are subject to stamp duty. However, such increases in restructuring projects approved by the State Council are exempt.

(3) Increases in paid-in capital (share capital) and total capital reserves resulting from asset revaluation during corporate restructuring, reorganization and institutional reform shall be subject to stamp duty as stipulated.

(4) Funds recorded under other accounting items that are converted into paid-in capital (share capital) or capital reserves shall be subject to stamp duty.

#### **2. Stamp Duty on Taxable Contracts**

For taxable contracts executed before but not yet fulfilled at the time of corporate restructuring, reorganization or institutional reform, stamp duty already paid on such contracts shall not be levied again if the successor entity assumes all rights and obligations without altering the original basis of tax.

#### **3. Stamp Duty on Property Transfer Documents**

Stamp duty exemptions apply to property transfer documents executed in connection with:

- Corporate restructuring, mergers, demergers, liquidation or institutional reform;
- Administrative adjustments made by the people's governments at or above the county level, or their affiliated departments responsible for managing state-owned assets, regarding the ownership of land use rights, buildings and structures, as well as equity shares, in accordance with regulations;
- Transfers of ownership of land use rights, buildings, structures, or equity within the same investment entity.

#### 4. Scope of Policy Application

(1) **Corporate Restructuring:** Includes the conversion of non-corporate enterprises into limited liability companies or joint-stock companies, the transformation of limited liability companies into joint-stock companies, and vice versa. The original investment entity must hold more than 75% of shares after restructuring and the new company must assume the original rights and obligations.

(2) **Corporate Reorganization:** Includes mergers, demergers, equity or asset contributions and transfer, debt restructurings, etc.

- **Merger:** Combining two or more companies into a single entity with the original investors remaining. This includes mergers between a parent company and its wholly owned subsidiaries.
- **Demerger:** Splitting a company into two or more entities with the same original investment entities.

(3) **Continued Existence of Investment Entities:** Original investors must remain in the restructured or reorganized entity, though their investment proportions may change.

(4) **Same Investment Entity:** Investors remain unchanged after demergers, with possible changes in their investment proportions.

(5) **Institutional Reform:** Transformation of public institutions into enterprises in accordance with relevant national regulations, where the original investor (including entities performed the duties of state-owned asset investors) holds more than 50% of shares (or equity) in the resulting enterprise.

(6) **Transfers within the Same Investment Entity:** Includes transfers between a parent company and its wholly-owned subsidiaries, between subsidiaries under the same company, or between individuals and their sole proprietorships, single-member limited liability companies, or individual businesses.



(7) **Definition of Enterprises and Companies:** Refers to entities established under Chinese laws and regulations and registered in China.

This announcement shall take effect on October 1, 2024, and remain valid until December 31, 2027. The “Announcement on Stamp Duty Policies Regarding Corporate Restructuring (Announcement No. 183 [2003] by the Ministry of Finance and the State Taxation Administration)” is simultaneously repealed.

**Ministry of Finance & State Taxation Administration**  
**August 27, 2024**

**II. Notice on the "Zero Tariff" Policy for Pharmaceuticals and Medical Devices in Hainan Free Trade Port by Ministry of Finance, National Health Commission, General Administration of Customs, State Taxation Administration and National Medical Products Administration (Finance, Customs and Taxation No. 21 [2024])**

**To Hainan Provincial Government, Haikou Customs, and the Hainan Provincial Taxation Bureau of the State Taxation Administration:**

To support the development of the Hainan Free Trade Port, expand the scope of "zero tariff" goods, and enhance pressure testing for closed-off operation, the "zero tariff" policy for pharmaceuticals and medical devices is announced as follows with the approval of the State Council:

**1. Exemption from Import Duties and Import VAT**

Before the full implementation of closed-off operations in Hainan, independently registered legal entities located in the Hainan Boao Lecheng International Medical Tourism Pilot Zone (hereinafter referred to as the "Pilot Zone") that have been recognized as eligible entities, including medical institutions, higher education institutions for medical education, and pharmaceutical research institutes, may import pharmaceuticals and medical devices specified in Article 3 of this notice and use them under the provisions of this policy without paying import duties or import-stage value-added tax (VAT).

Eligible entities that voluntarily pay import-stage VAT may apply for exemption when completing relevant procedures.

**2. Recognition of Eligible Entities**

The list of eligible entities shall be determined by the Pilot Zone Administration in coordination with Hainan provincial departments of health, drug regulation, education, science and technology, finance, Haikou Customs, and the Hainan Provincial Taxation Bureau. The list shall be dynamically adjusted and communicated to Haikou Customs and the Hainan Provincial Taxation Bureau.

### **3. Scope of Duty-Free Pharmaceuticals and Medical Devices**

Pharmaceuticals and medical devices exempt from import duties and import-stage VAT (hereinafter referred to as "duty-free pharmaceuticals and medical devices") include:

1. Import pharmaceuticals and medical devices already approved for registration in China;
2. Specially approved pharmaceuticals (excluding vaccines) and medical devices that are not yet approved for registration in China but are permitted for import and use in the Pilot Zone by the Hainan Provincial Government according to relevant regulations by State Council (hereinafter referred to as "specially approved pharmaceuticals and medical devices").

### **4. Import Procedures**

Before importing duty-free pharmaceuticals and medical devices, eligible entities must have each batch verified by the Pilot Zone Administration and the Hainan Provincial Drug Administration to confirm compliance with this policy. The verified information shall be forwarded to the customs and tax authorities in the entity's location.

Applications for duty-free import must be filed with customs by the eligible entities, and the Pilot Zone Administration shall manage these pharmaceuticals and devices according to existing special-use regulations. All relevant data must be uploaded to the Pilot Zone traceability platform for end-to-end regulatory oversight.

### **5. Restrictions on Use**

Duty-free pharmaceuticals and medical devices imported by eligible medical education institutions and pharmaceutical research institutes are limited to self-use within the Pilot Zone.

### **6. Sales Regulations**

Medical institutions may sell duty-free pharmaceuticals and medical devices to patients treated on-site, based on prescriptions or medical orders issued by their physicians. Sales must comply with clinical needs and prescription management regulations. Taxes on such sales shall be applied according to domestic tax policies. Duty-free items shall not be transferred to individuals outside these contexts.

### **7. Customs Supervision**

Duty-free pharmaceuticals and medical devices imported by eligible entities shall be subject to customs supervision within the regulatory period. After such items are sold to

patients under valid prescriptions, customs will not conduct further post-sale supervision.

## **8. Patient Use Requirements**

Patients must use duty-free pharmaceuticals and medical devices obtained from medical institutions for personal use only within the Pilot Zone. Resale, removal, or mailing of these items outside the Pilot Zone is prohibited.

## **9. Transfers Due to Objective Reasons**

If an eligible entity needs to transfer duty-free pharmaceuticals or medical devices due to objective reasons, prior approval from relevant authorities in Hainan Province is required. For items within the customs regulatory period, import duties and VAT must be paid to customs before the transfer.

Violations, including unauthorized transfers or resale by patients, shall be rectified by the Pilot Zone Administration, with recovery measures implemented where possible. Domestic VAT shall apply to such transactions.

## **10. Management Measures**

The Hainan Provincial Government shall take primary responsibility for implementing this policy and, in consultation with relevant national authorities, issue detailed management measures. These measures shall specify eligibility determination procedures, usage requirements for duty-free items, and penalties for misuse or violations. The management regulations shall be issued and implemented simultaneously with this notice.

## **11. Monitoring and Reporting**

Hainan Province shall regularly review the import, sale, and use of duty-free pharmaceuticals and medical devices, strengthen the management and supervision of eligible entities in the use and disposal of duty-free pharmaceuticals and medical devices (including prescriptions or medical orders issued by the physicians of medical institutions), and promptly investigate any violations. Quarterly reports shall be submitted to the issuing authorities of this notice, including basic information of eligible entities, duty-free pharmaceuticals and medical devices imported and sold by each entity, and tax exemptions data.

Relevant departments of Hainan Province shall carry out necessary technical system upgrades to improve the functionality of traceability management platform. Meanwhile information interoperability shall be enhanced to share data of eligible entities, patients, duty-free pharmaceuticals and medical devices.

## 12. Supervision and Compliance

The Hainan Provincial Government shall strengthen supervision to prevent violations and report any incidents promptly.

## 13. Penalties for Violations

Violations involving resale, proxy purchase, or smuggling of duty-free items shall be dealt with by customs in accordance with regulations and incorporated into the credit record by the Pilot Zone Administration. Patients violating provisions will face a three-year prohibition on purchasing duty-free items. Criminal liability shall be pursued where applicable.

## 14. Violations by Entities or Physicians

Eligible entities and physicians misusing duty-free items shall be penalized according to regulations. Entities subject to criminal prosecution will lose eligibility for this policy, with relevant information communicated to Haikou Customs and Hainan Provincial Taxation Bureau.

## 15. Implementation Scope

This notice applies exclusively to the Hainan Boao Lecheng International Medical Tourism Pilot Zone and takes effect upon publication.

**Ministry of Finance, National Health Commission, General Administration of  
Customs, State Taxation Administration, National Medical Products Administration  
September 2024**

### **III. Announcement by the Customs Tariff Commission of the State Council on Granting Zero-Tariff Treatment for 100% of Tariff Lines from Least Developed Countries (Tax Commission Announcement No. 9 [2024])**

To promote unilateral openness toward least developed countries (LDCs) and achieve shared development, starting from **December 1, 2024**, China will apply a **zero-tariff preferential rate to 100% of tariff lines** for goods originating from LDCs that have established diplomatic relations with China. For tariff quota goods, only the **within-quota tariff rate** will be reduced to zero, while the **out-of-quota tariff rate** will remain unchanged.

**Customs Tariff Commission of the State Council  
September 11, 2024**

## **ForTran News**

1. In September 2024, Shanghai ForTran Law Firm, in collaboration with Wolters

Kluwer, launched the Guidelines for the Application of Derivative Financial Instruments and Compliance with Fiscal and Tax Regulations.

2. In September 2024, attorney Ivy Yang attended the Huangpu-Singapore International Legal Services Practice Workshop.
3. On September 26, 2024, Attorney Hann Wu delivered a lecture on International Tax Law at Shanghai University of Political Science and Law.