Paper 8: Immovable Property Tax Reform: Taxing the Income of Real Estate Transactions by Consolidating Housing and Land

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Taiwan's land tax is classified into land value tax (LVT), agricultural land tax, and land value increment tax (LVIT). The LVIT, which is essentially an income tax on gains from land transactions, plays an important role in financing local government expenditures. The tax base of LVIT is determined by the government-assessed present value of land (GAPV), instead of the actual transaction value. No tax burden occurs on transactions during the period between consecutive annual adjustments of GAPV. There is thus a considerable gap between this system and fair, equitable taxation. The defect LVIT system is thought as a factor to surging real estate prices in Taiwan over recent decades. The public appealed to the government for tax reform of income from real estate transactions. The Income Tax Act was amended in 2015 to tax actual gains from real estate transactions combining house and land on a consolidated basis, and has taken effect since 2016. The LVIT remains unchanged by the implementation of income tax reform. The tax base of the real estate transaction income tax is the actual value of the properties reduced by related costs, expenses, and the increase in GAPV for LVIT purposes to avoid double taxation. This chapter aims at providing a background for different aspects related to tax levied on income from real estate transactions. In addition to introduction focusing on LVIT and the income tax reform in 2016, problems and issues of LVIT and the tax reform are addressed. Taiwan's land and tax policies in the 1950s represented a successful experience for developing countries, but also resulted in high real estate prices and wealth distribution inequality over recent decades. The income tax reform had been implemented for just two years, whether a success or failure case is still worth investigating. However, it is definitely a precious experience to developing countries, both academically and empirically.

Keyword: Property Tax, Land Value Increment Tax, Real Estate Transaction Income Tax

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Income Tax Reform: Taxing the Income from Real Estate Transactions by Consolidating Housing and Land

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OUTLINES

- How the Real Estate Transaction Income Taxed in Taiwan
- An Overview of the Land Value Increment Tax (LVIT) and Its Practice
- The 2016 Income Tax Reform and Its Concerns
- Recommendations for the future

How the Real Estate Transaction Income Taxed in Taiwan

- Taiwan's land tax system is classified into **LVT**, **agricultural land tax**, and **LVIT**.
- **LVT**: levied on the ownership of land, which tax base is the declared land value.
- **Agricultural land tax**: suspended since 1985.
- **LVIT**: essentially an income tax on gains from land transactions.

How the Real Estate Transaction Income Taxed in Taiwan

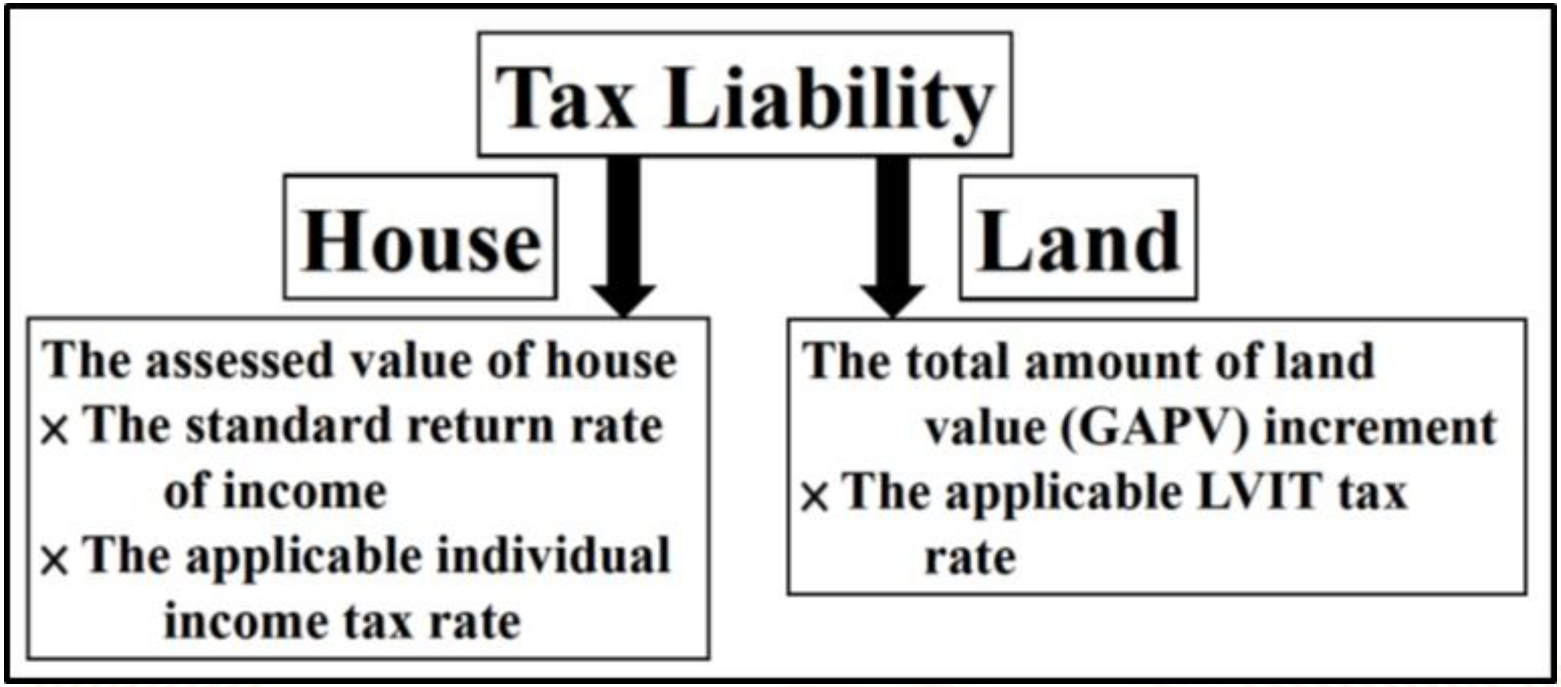

Figure 1 The Tax Liability of Incomes from Real Estate Transactions before the Implementation of the 2016 Income Tax Reform

An Overview of LVIT and Its Practice

Total amount of land value increment
= The present value of land at the time of transfer
− (The present value of land at the penultimate transfer or the value of land originally assessed) × CPI/100
− (Land improvement cost + Construction benefit fee paid + Land rezoning fee + Claimed current value of donated land)

Figure 2 The calculation of land value increment

An Overview of LVIT and Its Practice

Table 1 The LVIT tax rate structure

Bracket	Increment Multiple	Marginal Tax Rate[1]
Level 1	Total amount of GAPV increment is not in excess of 100%	20%
Level 2	Total amount of GAPV increment is in excess of 100% but less than 200%	30%[2]
Level 3	Total amount of GAPV increment is in excess of 200%	40%[2]

1. **The LVIT tax liability is collected at a special privileged rate of 10% for the sale of owner-occupied residential land.**
2. **The relief provided for long term ownership gives a 20% reduction to the increment beyond the minimal tax rate (20%) for land ownership between 20 and 30 years, 30% reduction to the increment beyond the minimal tax rate for land ownership between 30 and 40 years, and 40% reduction to the increment beyond the minimal tax rate for a duration longer than 40 years.**

An Overview of LVIT and Its Practice

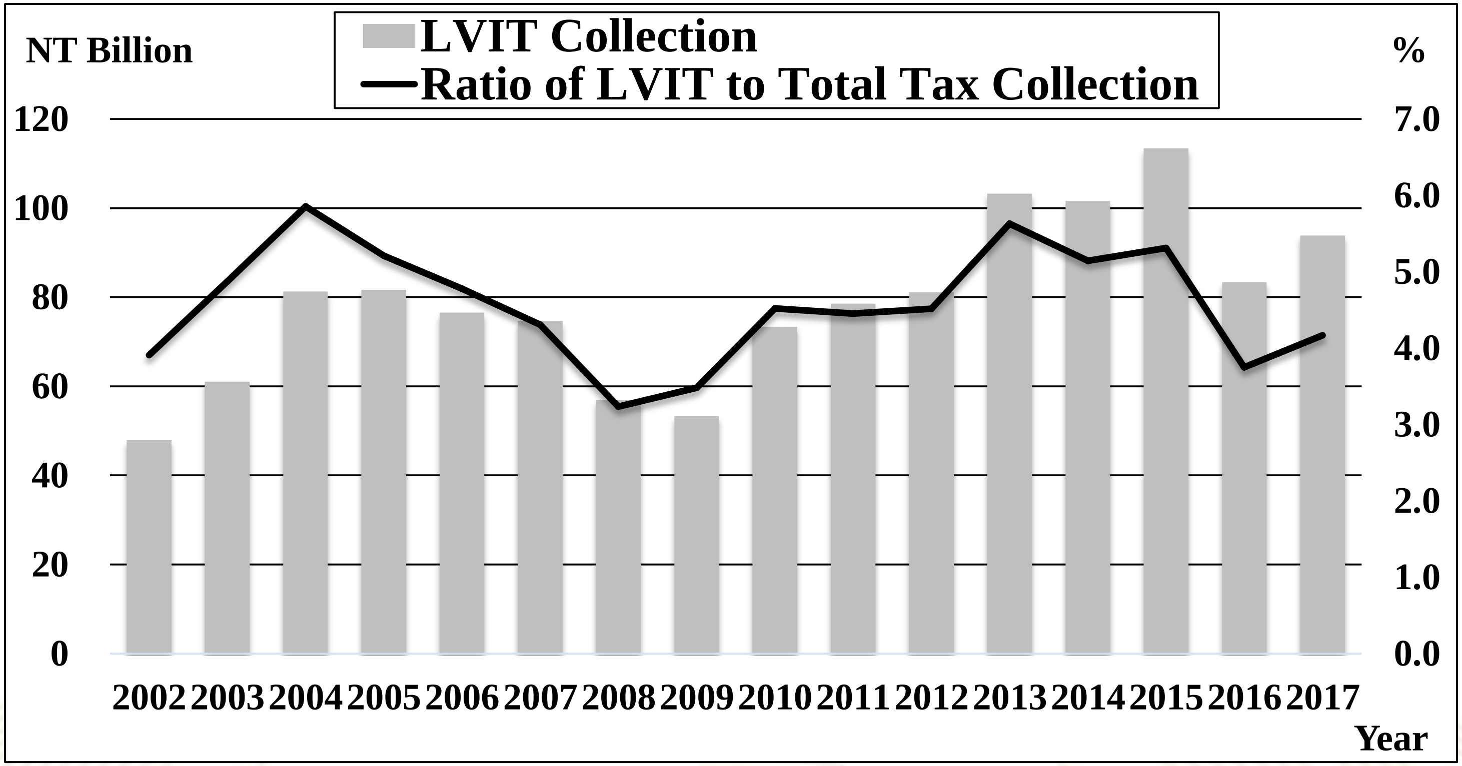

Figure 3 The LVIT tax collections and its ratio to total tax revenues, 2002-2017

An Overview of LVIT and Its Practice

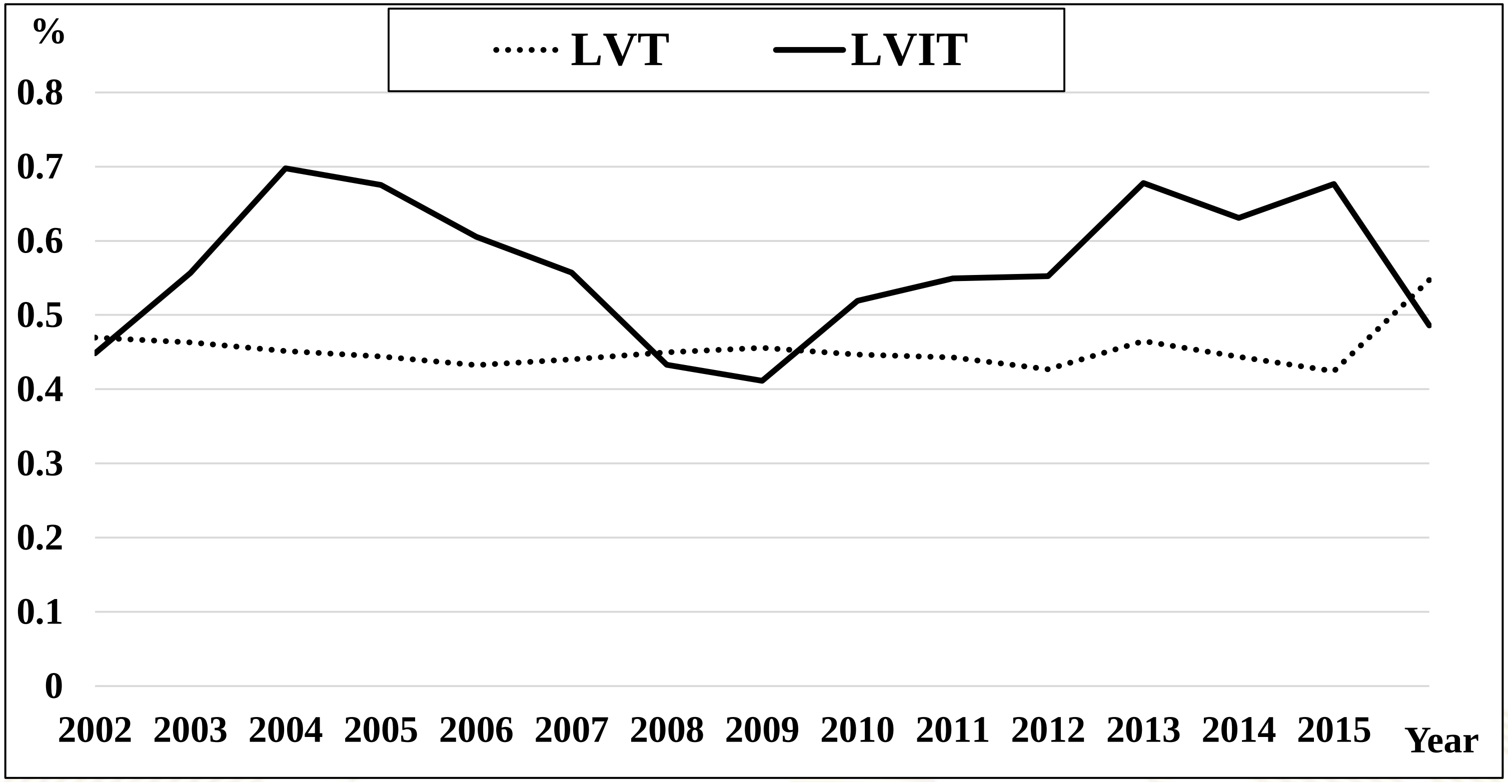

Figure 4 The ratios of LVT and LVIT tax collections to GDP, 2002-2016

An Overview of LVIT and Its Practice

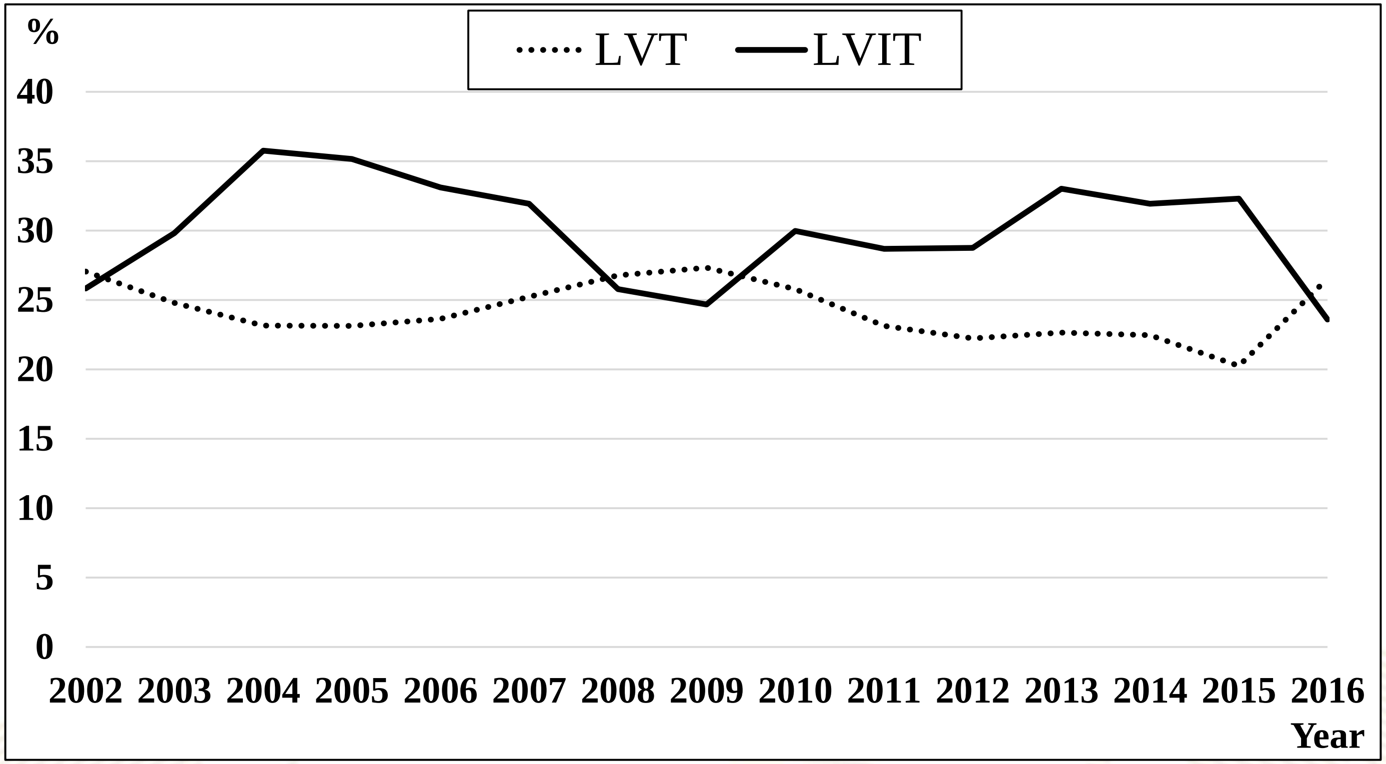

Figure 5 The ratios of LVT and LVIT tax collections to local government self-financing tax revenues, 2002-2016

An Overview of LVIT and Its Practice

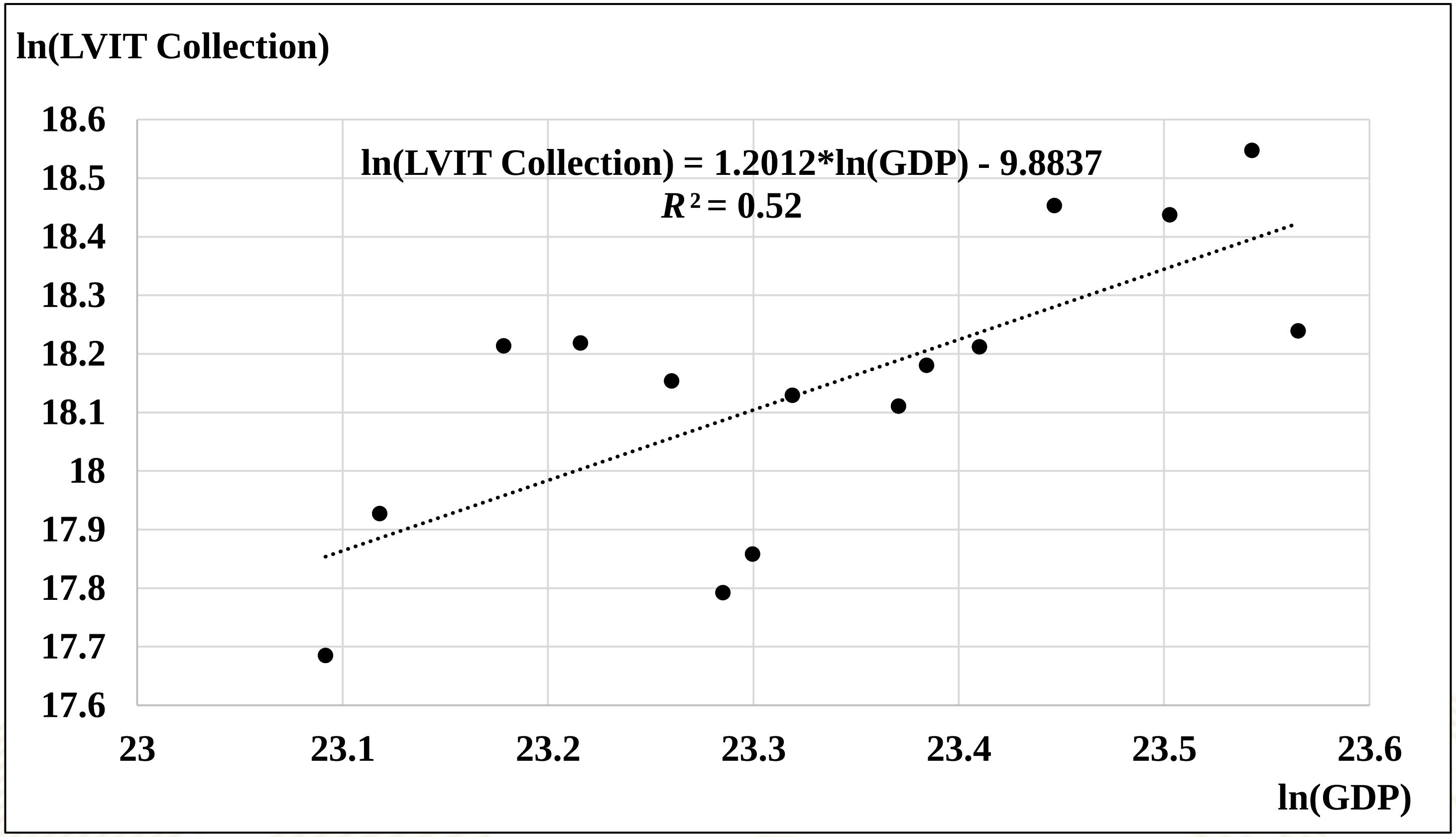

Figure 6 The scatter plot of LVIT collection and GDP, 2002-2016

An Overview of LVIT and Its Practice

- The GAPV of land is a lagged price, based on land transactions during the past one year.
- Tax holidays.
- The progressive tax rate structure results in the lock-in effect.
- The LVIT is distributed progressively related to family income, but far from being a horizontally equitable tax.

An Overview of LVIT and Its Practice

- Cons of LVIT:
  - A more comprehensive capital gains tax should be implemented for equally treating different types of capital gains.
  - The progressive tax structure penalizes long-term land holding and encourages short-term land speculation.
  - The GAPV of land is far below the market level.

An Overview of LVIT and Its Practice

- Pros of LVIT:
  - The tax administration and collection cost of LVIT is relatively low.
  - Even if the land value increment is incorporated in individual income, the lock-in effect still exists.
  - Local public finance.
  - The legislative issue.

The 2016 Income Tax Reform and Its Concerns

Taxable gains
= Sales price of real estate
  – Purchase cost
  – Relevant expenses
  – Total increment in GAPV and land

Figure 7 The taxable gains of the 2016 real estate transaction income tax reform

The 2016 Income Tax Reform and Its Concerns

Table 2 The tax rate structure of the 2016 real estate transaction income tax reform

The Length of Ownership	Tax Rate*
Less than one year	45%
More than one year but less than two years	35%
More than two years but less than ten years	20%
More than ten years	15%

* **The exemptions of a sale of owner-occupied residential land is NT$ 4 million. Any portion in excess is collected at a special privileged and flat rate of 10%.**

The 2016 Income Tax Reform and Its Concerns

- Concerns:
  - The inequity treatment problem.
  - Double-incentive for holding agricultural lands.
  - Tax competition between central and local tax authorities

Recommendations for the future

- The provision of double-incentive for agricultural lands should be revised or removed.
- A capital gains tax should be used to replace this long-practiced LVIT taxation.
- A well-designed intergovernmental fiscal transfer mechanism should be implemented.

THANK YOU!

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