

The Construction Industry's Strategies in Responding to the "Transformation from Business Tax to VAT" Decision

Jian Lin

Fuzhou University of International Studies and Trade, Fuzhou City, Fujian Province, China

Keywords: "transformation from business tax to VAT" decision; construction industry; tax planning

Abstract: The "transformation from business tax to VAT" decision has been carried out in the construction industry in a new round of tax reform. Since then, the construction industry has been affected to a great degree. As an important industry of the national economy, the tax planning of the construction industry must be conducted effectively to ensure the tax expenditure and tax burden reducing, as well as to improve the development of the industry. Based on the analysis of the status quo of tax levy and management in the construction industry, this paper analyzes the specific impact of the "transformation from business tax to VAT" decision on construction companies' tax burden, and gives due suggestions to respond to the decision.

1. Status Quo of Tax Levy and Management in the Construction Industry

As a key industry in China, the business activities of the construction industry can directly affect the second and third industries. For a long term, the business tax has been adopted in the construction industry. However, this kind of tax based on revenue has led to questions as double taxation and the tax revenue couldn't be deducted. The tax burden was not balanced in such a model, and it has also affected the development of the industry, therefore, many construction companies have reduced their revenue. As a result, there were a large number of unqualified construction companies emerging in the construction market. After the implementation of the transformation, the construction industry can deduct the input tax amount to avoid double taxation, which is of positive significance to the development of the industry. The industrial characteristics of the construction industry determine the particularity of its tax levy. While the construction industry provides services to the market, it also sells goods. Generally speaking, goods sell is in the scope of VAT levy, and the majority of labor services provided belong to scope of business tax levy. If a construction company offers both services and goods sell, it should make clear if the operation belongs to mixed sales or sideline business. Business tax should be paid based on all the revenues of the mixed sales, while it needs to be accounted separately for sideline business. There are always some construction-funds arrears in the construction industry, and in this case, the construction party will advance the construction funds. Many people think that the accountant will not confirm the income and make tax declaration if they have not yet received the project funds, which will seriously affect the timely payment of tax revenues. In addition, the cash flow of the project is not always run smoothly, and when the company settles the project payment with the construction party, the construction party will offset the project payment with raw materials, real estate, automobile equipment, etc. Therefore, the construction party will always not count those parts as income tax, resulting in a lot of tax evasion problems.

2. The Adverse Effect of the "Transformation from Business Tax to VAT" Decision on the Construction Industry

2.1 The long period of equipment update leads to an increase in tax burden

While construction, a large amount of machinery and equipment are needed, and ways of financing leases or purchase can be adopted to meet equipment needs. The fixed assets such as

automobiles, real estate and equipment purchased by enterprises prior to the transformation decision own high value and will only be renewed after being put into use for a relatively long period of time. In the future, the purchase of fixed assets will be decreased, and the corresponding input tax will be relatively low. In the same time, when the amount of output tax minus the input tax amount, the amount of tax payable by enterprises will increase, which means an increase of the tax burden of construction companies.

2.2 Tax burden will increase due to the difficulty of obtaining VAT special invoices

In general, construction projects are complemented in a decentralized way because it is not easy to purchase all building materials together at once and start all the construction projects. In order to facilitate the construction of the project and reduce the expenditure, the construction company will autonomously purchase materials from where the project lies in. The basic materials such as cement, masonry, sand, and steel account for a large proportion and the majority of local operators selling such materials are small taxpayers. They generally issue ordinary invoices for VAT, while it is more difficult for construction companies to obtain special invoices, and therefore, companies cannot deduct VAT. If they want to obtain special invoices, they must be invoiced by the tax bureau. The special invoice tax rate is 3%, which is the same as input tax rate, and the simple tax levy method is adopted. However, it is 11% for the construction industry, and the tax rate difference of the purchasing materials is 8%, thus the tax cost of construction companies will increase by 8%. The labor cost of the construction company accounts for a large proportion of the project cost, about 20% to 30%, and some even as high as 60%. There is always no special invoice for VAT in terms of the labor cost, and if the invoice is required, it needs the construction labor service company to offer labor services through dispatching, and in this way, the construction industry can obtain a 6% deduction. The tax rate for purchasing steel deductibles is 17%, but the proportion of steel costs in project construction may be small, which does not make much sense to reduce the tax burden.

2.3 Increase financial pressure on construction companies

It always costs a long period of time to complete construction projects, and the project retain age may not be paid until the end of the project acceptance. Therefore, there is a time-lag between the withdrawal of construction funds and the tax payment. In the process of construction, the withdrawal of construction funds may sometimes be delayed or need a further negotiation between the parties. However, VAT must be paid monthly, if the amount of which is large, it may increase the cash expenditure pressure on the company.

3. Corresponding Suggestions to Respond to the Transformation Decision

3.1 To strengthen the financial management within the corporate

First of all, the accounting treatment of VAT is not consistent with the business tax. In the past, business tax was directly calculated based on the amount of revenue at 3%. For VAT, output tax and input tax should be considered, and the accounting requirements and the process are more complex. What's more, there are still problems in the conversion of the old and new tax systems during the complementation of the transformation decision. In order to deal with these problems, the company should organize relevant training to financial personnel, letting them better know about the basic knowledge of "transformation from business tax to VAT" decision and accounting treatment, so as to help them familiarize the tax treatment method of VAT in the construction industry. Secondly, the type of invoices changed after the transformation implementation, which requires companies to strengthen the management of VAT. The management of previous business tax invoices is relatively simple, while there are strict regulations and laws upon the use and invoicing of VAT. For small taxpayers, the input tax is not involved in the VAT, and the invoice management and accounting work of which are not yet complicated. For general taxpayers, only when special invoices that meet the requirements be obtained and certified can the accountants account it as input tax and declare the deduction.

3.2 To strengthen operation management and to adjust the supplier structure

With the transformation, enterprises need to consider whether they can obtain special invoices for VAT when purchasing the steel, cement and equipment needed for the project. The materials needed for construction account for a large proportion of the project cost, and enterprises need to figure out if different types of suppliers can directly affect the deduction of input tax. If the supplier is a general taxpayer, the company can use and issue a special value-added tax invoice, and then apply for deductible VAT, thereby reducing the amount of tax payable and reducing the corporate tax burden. For small taxpayers, special invoices are not available, because the tax rate is only 3% even invoiced by the tax bureau. Therefore, a construction company must establish a supplier information base to clearly know supplier's price, goods' quality, invoice provision, etc., and check whether there is a general taxpayer to verify and intensify the update and maintenance management.

3.3 To choose right type of taxpayers

VAT is divided into general taxpayers and small taxpayers. With the transformation, companies need to reasonably choose the type of taxpayers. If a general taxpayer is selected, it will be levied at an 11% rate for VAT, and the input tax can be deducted, meanwhile, the output tax should be calculated according to the VAT rate. If a small taxpayer is selected, it will be 3%, and the enterprise's input tax cannot be deducted. Therefore, construction companies should reasonably choose the taxpayer's type according to their own actual conditions.

3.4 To adjust quotation

Construction companies are required to adjust the scale fees and bid prices, and VAT should be involved in the quotation system and they can adopt a quoting model that does not include tax price nor tax fees. Of course, whether or not this model can be adopted depends on the ability of companies to negotiate prices and transfer tax burdens. For materials purchasing, construction companies should manage to obtain input invoices, if failed, developers must bear the liability for compensation resulting in the increased tax burden. The payment methods of deposit should be adjusted in the construction industry, and efforts should be made to reduce the withdrawal ratio of the deposit.

3.5 To enhance business model innovation

With the transformation, construction companies can set up several subsidiaries for materials, transportation and construction services, so that the production, transportation and labor services can be separately accounted for, and thereby the management and planning can be improved and strengthened and profits can be maximized. Through the operating mode of the group company, the external procurement and the supplier selection are no more needed. The invoices obtained at the same time are also VAT special invoices that meet the requirements and can be deducted directly. Subsidiaries can also provide relevant labor services to increase the cost as well as the VAT deduction amount, which will be more conducive to tax saving.

4. Conclusion

The construction industry is of great importance in China, which attracts many employees every year. It has the characteristics of large-scale production value, complex business processes, and wide-range influences. For a long time, the authority has imposed a business tax on the construction industry, while there are some problems while implementing the business tax levy, such as it cannot be deducted and it may be double levied. The transformation from business tax to VAT has been implemented in May 2016. Before the transformation, the construction business tax rate was 3%, while it becomes 11% for the VAT. Although the implementation of the transformation has resolved some problems and made up some disadvantages existing in the business tax levy process, the tax rate has also increased, which correspondingly brings an impact on the tax burden of the construction companies, making the tax burden increased for some companies. To rationally reduce the negative impact of this tax reform and make full use of it, enterprises should conduct research

and analysis on the content of the reform and actively implement tax planning according to their own conditions.

Acknowledgement

This research was financially supported by the Key construction course "Final Settlement Practice of Corporate Income Tax" at school-level (JF2017052) and Education Reform and Research Project "Reform and Practice of Auditing Practice Courses" School-level (JF2018051).

References

- [1] Lu Qinghua. Thinking on the Tax Planning in Responding to the "Transformation from Business Tax to VAT" Decision [J]. Journal of Taiyuan University (Social Science), 2016, (12): 12-11.
- [2] Wang Jianguo. Strategies for Coping with the "Transformation from Business Tax to VAT" Decision [J]. Tax Research, 2016, (1): 99-102.
- [3] Wang Zhiguo. The Influence of the "Transformation from Business Tax to VAT" Decision on the Tax Planning of Construction Companies [J]. Accounting Review, 2015, (18): 167.
- [4] Yang Liping. Reasons Analysis of Tax Burden Increased in the Construction Industry and Construction Corporates' Tax Planning with the Implementation of the "Transformation from Business Tax to VAT" Decision [J]. Journal of Huaihai Institute of Technology (Humanities and Social Science Edition), 2017, (01): 99-101.
- [5] Zhou Hongbin. Impact of the "Transformation from Business Tax to VAT" Decision on the Tax Burden of Construction Companies and the Countermeasure Analysis [J]. Accountant, 2015, (7): 24-25.