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## RESEARCH ARTICLE

# The Analysis of the Necessity and Impact of Property and Inheritance Taxes in China

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## ABSTRACT

The purpose of this paper is to explore the necessity and possible impact of the implementation of property tax and inheritance tax in China based on the Western tax system and the existing experience and background in China. After understanding the provisions of the Western tax system, the comments of Western people, and the results of relevant experiments in China, we found that China's existing economic structure may create a number of problems and the low level of asset mobility of a small number of high-net-worth individuals and their small contributions to social and economic consumption also require a new tax for social wealth redistribution. Property tax and inheritance tax would be the right solution to local debt and social equity problems.

## KEYWORDS

Property tax, inheritance tax, real estate market, social equity.

## ARTICLE INFORMATION

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## 1. Introduction

### 1.1 Research Background

In the past twenty years, common prosperity for all has received a lot of attention. The 10th meeting of the Financial and Economic Commission of the CPC Central Committee proposed that we should adhere to the people-centered development philosophy and promote common prosperity through high-quality development, handle the relation between efficiency and fairness properly, scale up the size of the middle-income group and narrow the gap between the rich and the poor. Taxation is an important means of wealth redistribution in the world and mitigates the problem of the large gap. China reformed its tax system in 1994, and the local government obtained land transfer fees by selling land. Rising house prices also push up land sales. Gradually, the government sold the land, and the firm sold the house, which became a circle.

### 1.2 Literature Review

According to Research on real inheritance tax reform under the background of land finance transformation, the growth trend of the land income is negative these days, and the removal cost is also rising to two thirds of the land income; as we can see, the problems of the land finance are obvious (Zhang, 2024). Cyclical problems quickly emerged, with some local governments experiencing financial turnover problems. Local governments urgently need a new type of tax to fill the financial gap, and property tax has received a lot of attention. Chinese property tax was introduced in the 1980s, which stipulates that houses which are only used to live are duty free (H. Zhang, 2021). But now, the houses have become investments, which is not in line with the original intention of the current housing taxes. The collection of property tax can increase investment costs, reduce speculative returns, reduce housing prices, reduce the pressure on low and middle income families to buy houses, and alleviate the local debt crisis.

China has built a moderately prosperous society in an all-round way. According to the Report on the Development of People's Livelihood in China released by the China Social Science Research Center of Peking University, the Gini coefficient of property in China was 0.45 in 1995, 0.55 in 2002, 0.73 in 2012 and 0.47 in 2002, all higher than the standard value 0.4 set by the United Nations. It shows that the inequality between the rich and the poor in China is very significant. In China, the first rich did not lead to the later rich, but the situation of the rich getting richer.

Rupert Hoogewerf published its wealth report on April 14, 2022. The report shows that wealthy families in China own more than 160 trillion yuan, which is 1.6 times China's GDP, and this figure represents a 9.6 percent increase over last year. Such an amount of assets is obviously too high, and it is not good for Chinese sustainable development (Zhang & Huang, 2023). Also, the contribution of Chinese final consumption expenditure to economic growth is only 32.8%, which is substantially lower than 59.5% in 2019, and it is also lower than 70% in developed countries. The data shows that public willingness to consume is low or their power of consumption is not good, which tells us that the wealth needs to be redistributed. Therefore, the role of inheritance tax in adjusting the rich and poor, improving economic mobility, and increasing government fiscal revenue needs to be implemented in China to ensure China's sustainable development prospects.

### **1.3 Problem Statement**

Although the finance circle has already operated for several decades, the land is limited, and the part of unsustainable shows that the main driving force for this cycle to continue is the rapid increase in urbanization brought about by the rapid development of the economy and a large number of young families need housing to meet their needs, the speed of urbanization and the rate of population growth. This article will further discuss the necessity and impact of property and inheritance taxes in China.

## **2. The Necessity of Property Tax and Inheritance Tax**

China has realized the rapid accumulation of wealth in China and completed the task of "let a group of people get rich first." However, the Chinese incomplete tax system and the drawbacks of its land finance caused their local government to have some problems with their finance, and it also widened the gap between the rich and the poor. For such reasons, we need to start with land finance and limit the transfer of huge wealth between generations to alleviate local finance problems and promote the rationalization of social wealth redistribution. Nowadays, China needs a more broadly targeted property tax, as well as property taxes and inheritance taxes, for China's growing number of high net worth individuals.

### **2.1 The Necessity for a Property Tax**

There are two important backgrounds for property tax collection. First, the property tax used now was published in the 1980s. The real estate and service industries were completely different then, and China has not changed the tax policy on non-profit private housing for a long time. Second, Chinese society is different from most other societies, influenced by traditional concepts and social customs; the vast majority of Chinese people have a strong sense of property ownership and even tend to buy more houses than basic needs. The housing developed in such a context gradually has a high added value, which brings very high housing prices. Many people have worked hard for decades just to buy a house. So, one of the necessities is: In this unique economic form, "housing" naturally becomes an investment product with speculative possibilities; hence, now it is hard to distinguish whether the house is bought for living, then it is difficult to apply China's current property tax policy. To tackle this problem. A tax is needed to distinguish between houses that meet basic housing needs and those that are used for investment profit. Therefore, the implementation of a certain area of property tax reduction can not only ensure that the basic housing benefits are not damaged but also increase the cost of housing investment. The second necessity is that the current high housing price is not a reasonable development state of real estate. China's first-tier cities are in urgent need of a large number of high-quality talents to develop the economy. However, the high housing prices in first-tier cities have undoubtedly become a barrier to the entry of some high-quality talents, which is not conducive to the development of youth and the future development of cities and is a huge hidden danger for China's economic development. One of the problems caused by this hidden danger is the lack of high-quality talent exposed by the talent wars that have broken out in various cities since 2022. In fact, the excessively high housing price brings about a process with a certain outcome. The excessively high housing price discourages many people from buying houses, and these people begin to save money to buy houses, but the continuously high housing price delays their consumption progress. With the rapid rise of land prices, real estate developers begin to stop buying land because their expectations do not match the actual income, resulting in problems for government finance. The social and economic operation needs capital flow, but the high housing price and the decline of market expectation at this time again reduce the enthusiasm of people's consumption, and the social capital flow slows down. At this time, if the real estate developers choose to maintain the high price, they will maintain the status quo of social and economic stagnation, a large number of idle properties will appear, the capital flow will encounter difficulties, and the real estate development will inevitably have problems. If the price drops rapidly, the real estate developers will lose money, the willingness to buy land will decline, the government's finances will continue to be tight, and the social economy will face difficulties. Therefore, no matter how one chooses, there will be a bad result; the key to solving this problem is to reduce

housing prices and promote housing no longer as an investment product, which is an effective method, so the implementation of property tax is necessary.

## **2.2 The Necessity of Inheritance Tax**

The precondition for the imposition of inheritance tax is that there are enough people with high net worth. Many developed countries in the world levy inheritance tax and mainly use it to adjust the gap between the rich and the poor. According to the 2023 Statistical Bulletin of the National Economic and Social Development, China currently has nearly 300 million migrant workers and a rapidly expanding group of people holding ultra-high assets, which has not formed a state of a small proportion of low-income and high-income people and a high proportion of middle-income people. It should be noted that although the total value of all industries in China has increased to a certain extent, the contribution rate of China's final consumption expenditure to China's economic growth in 2022 will decline significantly compared with that in 2021 and return to a high proportion of 85.3% again in 2023, indicating that China's consumption has full potential but lacks stability, and the consumption enthusiasm of a large number of people has changed significantly. Therefore, there are three main reasons for the need for an inheritance tax:

(1) To ensure the tax system can steadily improve the consumption enthusiasm of middle and low income people in the future and play a similar role of "pushing grace order" to disperse huge wealth so that more wealth can be in the hands of middle and low income people in China.

(2) China's current service industry has not reached the level of developed countries, and China's luxury industry has not developed rapidly. Therefore, a large part of the consumption of high net worth individuals has not participated in the domestic cycle strongly supported by China. Decentralization of more capital will promote domestic circulation and stabilize the Chinese economy.

(3) Due to the prevalence of the current media, a large number of rich people, the second generation of rich people, and even the "fake second generation of rich people" will shoot some faux rich stories, and the high entry barriers of some high-income industries make some young people have the negative psychology of "learning is not as good as being born," and then produce the hatred of the rich. It is difficult to reverse this trend only by propaganda guidance. A more reasonable approach would be to reduce the pass-through of wealth between generations without loss.

## **3. The Influence of Inheritance Tax and Property Tax**

### **3.1 Impact of Inheritance Tax on the Chinese Economy, Social Equity and Tax Revenue**

The introduction of inheritance tax has had two main impacts on China's economic environment.

(1) By imposing an inheritance tax on high net worth individuals may limit the intergenerational transfer of wealth to a certain extent, reduce the excessive concentration of wealth, and thus promote a more rational distribution of social resources (W. Zhang, 2021).

(2) On the other hand, the implementation of inheritance tax may trigger capital outflow and migration of talents, especially high net worth individuals who may avoid taxes by emigrating or transferring their assets, which may have a certain negative impact on economic development (Li, 2020). In addition, how to effectively levy inheritance tax while encouraging consumption and investment will be an important issue for policy makers to weigh (Wang, 2019).

Inheritance tax is regarded as an effective tool to reduce the gap between the rich and the poor and to promote social equity. Through the imposition of inheritance tax, part of the wealth of the affluent class can be transferred to the public coffers for social welfare expenditures, such as education, healthcare, and public services, thus improving the overall equity of the society (Liu, 2022). However, the implementation of inheritance tax may face the challenge of low social acceptance, especially in a society where culture traditionally focuses on the transmission of family wealth; inheritance tax may trigger social discontent and backlash (Chen, 2021). Therefore, when implementing inheritance tax, policy makers need to consider cultural factors and ensure the fairness and transparency of tax policies to win public support (Ding, 2020).

From a tax perspective, the introduction of an inheritance tax can provide the Chinese government with a new source of revenue and alleviate fiscal pressures, especially in the context of coping with an ageing society and increasing public expenditure. However, how to design an effective inheritance tax system to prevent tax evasion and reduce administrative costs will be an important challenge for China (Zhou, 2019). In addition, inheritance tax needs to be coordinated with the current tax system to ensure consistency and stability of tax policies (Yang, 2021).

### **3.2 The Impact of China's Property Tax**

Property tax, as a form of direct taxation, is regarded as a crucial tool for regulating the real estate market, increasing fiscal revenue, and promoting social equity. In recent years, China's economic growth has gradually slowed, the volatility of the real estate market has intensified, and the issue of income inequality has become more pronounced. Against this backdrop, the introduction of property tax has become a hot topic of discussion among government officials. Many scholars believe that the introduction of a property tax could effectively curb speculative behavior in the real estate market, stabilize housing prices, and provide local governments with a stable source of fiscal revenue. Additionally, property tax is viewed as a powerful means of wealth redistribution, capable of reducing wealth inequality and promoting social equity.

However, the implementation of property tax in China also faces numerous challenges. For instance, the real estate market accounts for a significant portion of China's economy, and its fluctuations have far-reaching impacts on the overall economy. Questions remain as to whether China's current legal framework and tax system can effectively support the implementation of property tax.

#### **3.2.1 The Impact of Property Tax on the Macroeconomy**

The introduction of a property tax primarily affects the supply and demand dynamics of the real estate market. According to the research by Zhang and Deng, property tax increases the holding cost, which suppresses speculative buying behavior, thereby helping to stabilize housing prices (Zhang & Xiao, 2022). The stabilization of housing prices has a positive effect on economic growth, as it reduces the risk of economic bubbles and provides a more solid foundation for the real economy. At the same time, property tax can also redistribute income, reduce income inequality, and optimize the overall consumption level and consumption structure of society.

The contribution of property tax to fiscal revenue is equally significant. Huang Yan pointed out in her research that property tax can provide local governments with a stable source of tax revenue, reducing their reliance on land transfer fees (Huang, 2020). This diversification of fiscal revenue helps local governments maintain fiscal stability during economic fluctuations, enhancing their ability to regulate the economy. Moreover, as the property tax is gradually promoted, the fiscal autonomy of local governments will be strengthened, enabling them to formulate more reasonable fiscal policies based on their actual situations.

However, property tax may also have a negative impact on economic growth. The research conducted by Liu Jianfeng and others indicates that the introduction of property tax may suppress real estate development investment, exerting pressure on economic growth in the short term (Liu, 2020). Property tax increases the cost of real estate development, which may lead developers to reduce investments, affecting the supply in the real estate market. In addition, the suppressive effect of property tax on housing prices may reduce household wealth in terms of real estate, thereby affecting household consumption capacity and consumer confidence.

The imposition of property tax needs to take into account the affordability of families in different regions and with different income levels, avoiding excessive increases in residents' tax burdens. Additionally, it is imperative to address the need to improve policies at the institutional and implementation levels to ensure the fairness and effectiveness of the tax.

The impact of property tax on China's economy is multifaceted. It can promote economic growth by stabilizing housing prices and optimizing the consumption structure, and it can provide local governments with a stable source of fiscal revenue. However, the implementation of property tax must carefully consider the actual conditions of the real estate market, the affordability of residents, and the improvement of the tax system to maximize its positive impact on the economy while minimizing potential negative effects.

#### **3.2.2 The Impact of Property Tax on the Real Estate Industry**

The impact of property tax on the real estate market is reflected in various aspects such as the housing price formation mechanism, supply-demand relationship, and real estate investment. Firstly, the effect of property tax on housing prices is complex and multifaceted. On one hand, property tax increases the holding cost for home buyers, which may reduce their willingness to purchase, particularly among speculative buyers, where higher tax burdens could suppress investment demand. However, a reduction in demand does not necessarily lead to a decrease in housing prices, as housing prices are formed through a complex balance of supply and demand. Yang Shaoyuan and Xu Xiaobo pointed out that "property tax, as a form of wealth tax, functions to adjust wealth distribution, enabling low-income earners to afford essential housing" (Yang & Xu, 2007). This suggests that one of the objectives of property tax is to influence housing prices by redistributing wealth, making them more reasonable.

The effect of property tax may vary significantly across different regions. Zheng Huanhuan and Qingyong Zhang noted in their study (Zheng & Qing, 2013) that since January 28, 2011, Shanghai and Chongqing have implemented property taxes aimed at curbing speculative demand and mitigating housing price increases. However, despite the implementation of property tax, housing

prices in these two cities continued to rise. Using the synthetic control method, the study found that by November 2012, the average housing price in Shanghai was approximately 2 127 RMB per square meter lower, or 13.4% lower, compared to what it would have been without property tax, and this difference was considered significant in placebo tests. However, in Chongqing, no significant impact of property tax on housing prices was found. This indicates that the effectiveness of property tax policy may be influenced by various factors, including economic conditions, market maturity, and policy enforcement.

On the other hand, the imposition of property tax increases the costs for real estate developers, which may lead them to scale down development projects or raise housing prices to pass on the costs. Additionally, the presence of property tax may also influence developers' strategies regarding the types of properties they develop, potentially leading them to focus on high-end properties to achieve higher returns, thus affecting the market supply structure. Lai Wenjie and others pointed out that "housing prices include land use costs and taxes, which are passed on to housing prices after developers pay them in a lump sum, resulting in higher housing prices" (Lai et al., 2023). This pass-through mechanism could lead to an increase in housing prices in the short term.

The impact of property tax on real estate investment is also significant. The presence of property tax raises the threshold and risks associated with real estate investment, which may deter some investors from entering the market. However, property tax also provides investors with an expectation that the government will regulate the real estate market through tax policies, which could influence their judgment of future market trends. The study by Zhang and Deng shows that "property tax has an overall positive effect on housing prices in China, and the change in housing prices has a significant positive wealth effect on consumption" (Ren, 2023). This suggests that the implementation of property tax policy may increase household wealth through higher housing prices, thereby stimulating consumption.

The design and implementation of property tax policy need to comprehensively consider the market's supply-demand situation, investor behavior, and the macroeconomic environment. Policymakers should use scientific tax design to reasonably set tax rates and tax bases to minimize excessive market intervention. Additionally, they should strengthen the monitoring and analysis of the real estate market and adjust policies promptly to adapt to market changes. Ren Qiang and others proposed that "a broad-based real inheritance tax helps weaken bubbles in the long term and should be established as a fundamental system" (Liu & Duan, 2023). This emphasizes the role of property tax in stabilizing the real estate market in the long term.

Given the differences in the development status of real estate markets and housing prices across regions, the formulation and adjustment of property tax policies should be tailored to local market environments. Moreover, the implementation of property tax policy should be coordinated with other real estate regulatory policies to create a synergistic effect that promotes the healthy development of the real estate market. During the implementation of property tax policy, the government should also strengthen the supervision and use of property tax revenue to ensure that tax revenue is used for public services and infrastructure construction, thereby enhancing tax transparency and credibility. This not only helps improve taxpayer satisfaction but also promotes social equity and sustainable economic development.

The impact of property tax on the real estate market is multifaceted, involving the housing price formation mechanism, supply-demand relationship, real estate investment, and more. A reasonable property tax policy can promote healthy market development while achieving fair wealth distribution. The formulation and implementation of such policies require detailed market analysis and prudent decision-making processes to ensure that the policy outcomes align with the intended goals.

### **3.2.3 The Impact on Property and Social Equity**

The imposition of property tax plays a crucial role in regulating income distribution and promoting social equity. Through the establishment of progressive tax rates, property tax can levy different proportions of taxes on property owners with varying property values, helping to achieve vertical equity in wealth distribution. Liu Xueliang and Duan Quanwei pointed out (Liu et al., 2012) that the issue of tax burden shifting cannot be ignored, particularly in the case of property rentals, where property tax may be passed on to tenants through higher rents, potentially weakening the role of property tax in adjusting income distribution. The fairness of property tax policy and the challenges of its implementation are also key issues. During the collection process, ensuring the equitable distribution of the tax burden and avoiding exacerbating social inequality due to improper tax design are challenges that must be addressed in property tax reform. Additionally, the research by Liu Hongyu and others suggests that the imposition of property tax needs to consider the actual conditions of different regions and income groups to achieve both vertical and horizontal equity in taxation (Guo et al., 2019).

A wealth of international experience shows that broadly taxing existing properties while providing exemptions for specific types of properties or particular groups is a common practice in property tax systems. In China, scholars such as Guo Zhe have proposed

property tax exemption schemes, such as exemptions based on the number of units, area, or value, aiming to achieve a progressive tax system, alleviate the burden on housing-strapped groups, and regulate the distribution of social wealth (Zhan & Li, 2015).

Although the redistributive function of property tax is limited, its implementation is still significant in the context of the current large income gap. An ideal property tax system should select an appropriate tax rate structure and exemption threshold against the backdrop of specific property and income distributions. The study by Zhan Peng and others indicates that the implementation of property tax has a positive impact on social equity. Despite the cautious approach in the property tax pilot programs in Chongqing and Shanghai, with average tax rates of less than 0.2%, the use of progressive tax rate structures has still managed to reduce income inequality.

#### **4. Conclusion**

We find that property tax will have a multidimensional impact on China's economy, real estate market, and social equity. It provides local governments with a stable source of revenue, helping to promote economic growth and infrastructure investment. Meanwhile, property tax influences household and corporate consumption and investment behavior by regulating the real estate market, helping to curb speculative behavior and stabilize housing prices. In terms of social equity, property tax promotes vertical equity in wealth distribution through progressive tax rates despite the potential issue of tax burden shifting.

The Inheritance tax has the potential to regulate China's economy, promote social equity, and increase fiscal revenue. We suggest that policymakers should consider how to effectively levy inheritance tax while encouraging consumption and investment. Since the research method of this paper is mainly a study of past domestic and foreign experiments and tax systems, the experiment inevitably has certain limitations. The future research direction is to further analyze the possible reactions of the public and feasible countermeasures after the implementation of the payroll tax.

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