

# TAX PLANNING IN MERGERS AND ACQUISITIONS

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## Abstract

M&A is an important method for an enterprise to realize the expansion of business scale, increase of market shares and become a multinational company, while taxes account for a large proportion of the total cost of M&A activities. Tax planning in the M&A process can not only reduce the taxes and charges of both parties, but also help to promote scientific management of enterprises.

**[Keywords]** Tax Preferential; Tax Planning; High-tech Enterprise

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## 1. Research Background

Taxation is an important link in the development and implementation of merger and reorganization business. M&A gains and losses incurred by the M&A enterprise in the M&A process shall be subject to income tax; Investing in inventory is subject to VAT; The equity transfer income generated by the target enterprise during the M&A process is subject to income tax, etc. There are many types of taxes involved, covering all aspects of corporate mergers and acquisitions. Since the applicable tax rates vary widely from asset to asset, dividends are distributed and interest is paid. Business income and capital gains also have different applicable tax rates<sup>1</sup>. Therefore, different tax arrangements and designs will have different tax implications during the M&A process. Under the premise of legality, using the flexibility of taxation to reduce the tax pressure of enterprises in the process of mergers and acquisitions, so as to obtain greater merger and acquisition benefits, is a very crucial part of enterprise operation and financial management, and is also an objective need for enterprises to occupy advantages in the fierce competition in domestic and foreign markets. In 2006, our country's 《Accounting Standard for Business Enterprises No. 20—Business combinations》 Promulgated and implemented, the business of business combination is divided into business combination under common control, business combination with business combination under not common control, the accounting treatment of business combination under the same control adopts the equity combination method, consolidated net assets are recorded at book value, and the profit or loss of the consolidated is not recognized; Mergers not under common control are accounted for using the purchase method, and consolidated net assets are recorded at fair value to recognize consolidated gains and losses. Due to the different treatment of accounting and tax laws, it is more difficult for the parties to the merger to treat taxes, but it provides space for corporate tax planning in the process of merger. Selecting M&A targets is a key strategic decision in the M&A process, and the target company's industry needs to be considered. The operating conditions of the region and the target company. The company's own strategic goals and other aspects. In the process of analyzing and researching the income tax planning in the business of enterprise mergers and acquisitions, it can help enterprises improve their concept of tax payment, make their mergers and acquisitions more scientific and effective, and promote the

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1 李 Flat. individual 所 Tax-collectedinternational 经验[N]国 Financial 报, 2018-07-31 (006) .

mutual promotion and development of their own interests and government revenue.

## 2. Feasibility Analysis Of Tax Planning In M&A

### 2.1 Differences in Tax Code Provisions

Tax costs vary from region to region. In order to carry out macro-control, the state adopts differentiated tax policies for regions with uneven economic development level and uneven resource distribution. For example, China's current tax law stipulates that the local authorities of ethnic autonomous regions shall decide whether or not to reduce or reduce the part of enterprise income tax that belongs to the locality; In order to further promote the large-scale development of the western region, companies engaged in state-encouraged industries in the western region will be reduced by a preferential income tax rate of 15%; In addition, the state also implements preferential tax policies for high-tech enterprises in special economic zones, exempting them from income tax for the first two years, and halving the tax rate of 25% for the next three to five years. This geographical tax difference can encourage enterprises to carry out tax planning. For example, a company can acquire a business within a SEZ, transfer part of the group's operations to the SEZ, or transfer profits from other regions to the SEZ to reduce taxes.

The tax burden of enterprises in different industries is different. The tax gap between industries is reflected in each type of tax. For example, business tax payers in different industries are subject to different business tax rates; Tax rates for various consumer goods also differ; Enterprises providing processing, repairing and repairing services pay value-added tax, while enterprises providing other types of labor pay business tax; The state implements preferential tax policies for certain special industries. For example, environmental protection enterprises are exempt from corporate income tax for the first three years, and corporate income tax is halved in the fourth to sixth years<sup>1</sup>. This sectoral tax differential allows taxpayers to reap tax savings by restructuring their investments.

The tax burden of different sizes of enterprises is different. For example, VAT taxpayers are divided into general taxpayers and small-scale taxpayers. The tax burden

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1 Shi Jian , Liu Rong , Fei Maoqing. individual 所 Taxation 费用 deductinstitutionalinternationalComparative research[J].internationalTaxation, 2018(7): 11-16.

of the two is markedly different. General taxpayers can use special VAT invoices to deduct input tax in the process of handling economic business; Small-scale taxpayers adopt a simple collection and management method, and cannot deduct input tax; Small and small profits Enterprises are subject to corporate income tax at a rate of 20%. This difference in tax burden enables enterprises to choose the appropriate scale of operation according to their specific economic operations and the characteristics of their tax burden.

## 2.2 Flexibility of tax laws

Although tax laws and regulations are mandatory for taxpayers, they also have their flexible side. First of all, from the taxpayer's point of view, for example, the tax law stipulates that small-scale taxpayers should collect value-added tax according to the simplified method, but under certain conditions, small-scale taxpayers can also apply to become ordinary taxpayers. This shows that the tax law is flexible in practice. Secondly, from the perspective of the scope of taxation, the object of taxation of some taxes is not clear, and the scope of taxation is difficult to define. For example, VAT and sales tax are not easy to define in practice for taxpayers who mix sales and concurrent sales; For another example, an enterprise's income tax is calculated by the product of its taxable income and its applicable tax rate, and the taxable income is calculated by subtracting the amount of each deduction from the total income of the enterprise. However, there is no clear definition of the tax law on deductible items, which allows enterprises to transfer non-deductible items or parts to similar expenses that can be deducted, or transform items with high taxes into items with low taxes, so as to achieve the purpose of tax saving. Third, from the aspect of tax calculation basis, when the tax rate is fixed, the smaller the tax base, the smaller the tax payable; Conversely, the larger the tax base, the greater the tax payable. For example, when an enterprise accounts for inventory, it can use a variety of valuation methods, and the cost of sales in the current period is also very different due to different methods; In terms of depreciation of fixed assets, different depreciation methods can also be adopted according to the actual situation of the enterprise. These different accounting

### **3. Tax Planning Analysis For M&A Target Selection**

#### **3.1 The industry in which the target of the merger is located**

##### **3.1.1 Horizontal mergers and acquisitions**

Tax planning analysis for horizontal M&A. Horizontal mergers and acquisitions are the mergers and acquisitions of enterprises in the same industry or with the same business. Enterprises can use horizontal mergers and acquisitions to obtain economic and financial synergies, increase market share, and expand scale. Horizontal mergers and acquisitions will not have too much impact on the original production and operation scope of the enterprise. Therefore, the tax types of enterprises have hardly changed much, and relatively speaking, the content of tax planning analysis will be relatively small. However, if the acquirer was originally a small-scale taxpayer, it may become a general taxpayer after the completion of the merger. The change in size leads to a change in the applicable tax rate, which will lead to a change in the overall tax burden.<sup>1</sup> In addition, if an enterprise chooses to acquire a loss-making enterprise, it can use the loss of the target enterprise to offset the profit of the acquiring enterprise, thereby reducing the overall profit, thereby reducing the income tax payable in the current period. Of course, this loss covering is conditional. This also deals with the impact of different M&A payment methods on corporate income tax, which will be discussed later.

##### **3.1.2 Vertical mergers and acquisitions**

Tax planning analysis for vertical mergers and acquisitions. Vertical mergers and acquisitions are mergers and acquisitions of upstream and downstream enterprises, through which enterprises can reduce or eliminate vertical transaction costs, realize the integration of supply, production and marketing, and produce scope economy. From the perspective of tax payment, the original purchase or sale behavior of enterprises implementing vertical mergers and acquisitions is transformed into the transfer of assets within the group, thereby reducing the tax burden. Since the original sales between enterprises are no longer purchase and sale business, there is no need to pay VAT in the current period of asset transfer. Although the total amount of VAT

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1 whisper 新华. personal tax "Deductions" Should be quoted 入通胀 Adjustment mechanism [N] 国税报, 2015-07-08 (B04) .

paid does not change when the product eventually leaves the enterprise (assuming the selling price does not change), the enterprise can still reap the benefits of deferring tax payment. If both parties to the merger and acquisition are consumption tax payers, the consumption tax in the intermediate link can be deferred until the final consumer goods are sold, especially when the consumption tax rate in the later link is lower, the tax burden can be reduced. For example, tobacco and cigarettes are both excise taxable consumer goods, and if a tobacco manufacturer acquires a cigarette manufacturer in the same region, the tobacco is not required to be paid when it is sold, but only the cigarette is subject to excise tax.

Case: A Enterprise and B The enterprise is two wineries, and A For the production of liquor, the applicable consumption tax rate is 25%; B For enterprises producing medicinal wine, the applicable consumption tax rate is 8%. And B The raw materials used in the medicinal liquor produced by the enterprise are: A Liquor produced by enterprises. hypothesis A Businesses sell annually to B The liquor of the enterprise is 5000 million, then, if the two enterprises merge, tax benefits can be generated: A 向 B VAT on the sale of liquor 850 million yuan ( $5000 \times 17\%$ ) can be postponed until B The enterprise pays when it sells medicinal wine, so that it obtains the time value of the money; In addition, taxpayers who produce consumer goods for their own use are not taxed if they are used for the continuous production of taxable consumer goods. such A The consumption tax originally accrued for the sale of liquor by enterprises 1250 million yuan ( $5000 \times 25\%$ ) Nor does it Payment required. In addition, vertical M&A can also use the losses of the acquired party for effective planning under certain conditions. However, due to the increase in the economic business of enterprises due to vertical mergers and acquisitions, the types of taxes will change greatly. This makes tax pooling more difficult.

### 3.1.3 Hybrid M&A

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Tax planning analysis for hybrid M&A. Hybrid M&A is aimed at different industry sectors. Mergers and acquisitions by companies in different markets are not the company's competitors, nor its upstream and downstream companies. Hybrid M&A enables companies to diversify risks and discover new profit growth points through diversification strategies. Due to the inconsistent tax rates of different industries, a hybrid M&A can transfer assets from a high-tax industry to a low-tax industry. Hybrid mergers and acquisitions may lead to concurrent operations and mixed sales. For mixed sales behavior, if the enterprise is engaged in the production of goods, VAT is payable on wholesale or retail operations where the taxable income of VAT exceeds more than half of the gross income; The rest of the businesses pay business tax. Companies can plan for a more beneficial business by comparing the VAT and sales tax amounts of their mixed sales. If the business tax rate of the enterprise is lower, it can increase the business in taxable labor services; Conversely, if the VAT rate is lower, then the production and sales operations should be increased. Of course, in addition to tax planning, it is also necessary to consider the profit level and market demand of different business operations and even corporate strategies. Safeguard the interests of the enterprise in general.

For concurrent operations, if the tax rates of the concurrent business of the enterprise are different, it is required to account for their respective income in accordance with the provisions of the tax law; Otherwise, it needs to be calculated at a higher tax rate. Therefore, enterprises should objectively register their account books and calculate business income separately as much as possible, so as to make it the basis for paying taxes, so as to avoid the increase of enterprise tax burden due to unclear accounting of low-tax businesses. If the business of the enterprise is a non-VAT taxable item, it is also necessary to separate the income of the different items; Where concurrent operations are not accounted for separately, VAT is required to be levied on all occasions. Therefore, enterprises can compare the VAT and business tax burden of concurrent operations, and if the VAT is lower, it can not be assessed separately. However, after the amendment of the Rules, this planning method is no longer valid. Because the competent tax authority will choose the basis for the division in its favor in order to increase tax revenue, if the VAT revenue is higher, then the tax authority can appropriately increase the sales in this regard. This is a loss for businesses. Therefore, in order to avoid this risk, enterprises should try to account for

concurrent business activities separately to prevent excessive taxation.<sup>1</sup>

Under normal circumstances, the decision of whether to acquire an enterprise in the same industry, acquire an upstream and downstream enterprise, or conduct a hybrid merger and acquisition occurs before tax planning. Companies will not abandon plans for horizontal M&A because vertical M&A can save more taxes. Therefore, the discussion in this part does not mean that the tax planning plan of the enterprise can affect the choice of the target enterprise by the acquirer, but provides tax planning ideas for different types of mergers and acquisitions. Make mergers and acquisitions smoother. For example, after an enterprise decides to carry out horizontal M&A, it can reduce the cost of M&A by choosing a loss-making enterprise to complete the M&A<sup>2</sup>, Realize greater M&A benefits.

### 3. 2. The region where the target of the merger is located

#### 3.1.1 Tax Jurisdiction

It is the right to tax that a country exercises in accordance with its own tax laws. In order to safeguard its own tax interests, sovereign states will expand the scope of their taxation as much as possible and determine the tax jurisdiction that best suits their own interests, without interference from other countries. Of course, a country cannot impose unlimited taxes, and its tax jurisdiction is formulated according to certain principles. Tax jurisdiction includes territorial, resident and civil jurisdiction. The sovereign States exercising single territorial jurisdiction are France, the Netherlands, Brazil, Ecuador, Nicaragua and Panama, Venezuela, etc.; Most countries exercise both territorial and resident jurisdiction in order to increase their tax revenues; In addition to territorial and resident jurisdiction, the United States also exercises civil jurisdiction. Exercising two or more tax jurisdictions is bound to result in businesses paying taxes in different countries. In tax planning, multinational corporations should try to eliminate all kinds of links with the tax jurisdiction of the host country, minimize the establishment of permanent establishments in countries exercising two tax jurisdictions, and avoid bearing excessive tax burdens.

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1 Hu Zhengyan and Wu Jinbo: "A Comprehensive Review of Tax Planning Literature in Enterprise Mergers and Acquisitions," Contemporary Economy 2013 Year No 21 Time limit.

2 Fan Xianting: "Tax Planning of Payment Methods for Enterprise M&A", Finance and Taxation Research 2013 Year No 3 Time limit.

### **3.1.2 Tax Policy**

Taxes, tax rates, and tax incentives vary greatly from country to country. For example, Afghanistan implements national treatment for foreign investors, and both overseas and local enterprises can enjoy the same tax policy; Turkish tax law stipulates that all activities in its free zone enjoy tax exemption, do not have to pay taxes according to the collection policy of other parts of the country, there are no restrictions or restrictions on foreign investment in the region, and enjoy the same preferential policies as domestic enterprises. Singapore's GST rate is only 5%, which is one of the lowest GST rates in the world. Ireland's corporate income tax rate is only 12.5%, which is much lower than the tax rate in most European countries, making it very attractive for multinational companies. If a Chinese enterprise establishes a number of subsidiaries in Germany, it can establish a consolidated tax relationship between these subsidiaries, each subsidiary first separately accounts for its own income, and then summarizes the accounting in the remittance company, and the net income after all profits and losses are offset as the tax basis, and each subsidiary is no longer taxed separately. For a subsidiary in Germany, if profits are transferred to the Chinese parent company, capital gains tax is not required, while the branch office is not. When Chinese enterprises invest overseas, they should comprehensively consider the tax policies of the two countries and the "taxation treaty" that may be signed between the two countries to obtain more tax benefits.

### **3.1.3 Tax collection and management system**

Different countries have different ways of implementing their tax administration systems, some of which are relatively lenient and some of which are relatively severe, which will affect the tax burden of enterprises and the time of tax payment. When enterprises invest in mergers and acquisitions, they should choose countries and regions with a weak degree of tax collection and administration to invest on the premise of not affecting the development strategy.

## **4. Identification Of The Nature Of "Famous Stock Real Debt" In The Bankruptcy Scenario**

### **4.1 Tax planning analysis of financing link**

There are two methods of internal financing and external financing. Internal financing does not require interest and dividends, and it is relatively simple and quick to obtain, but the company's capital is limited, and almost no company relies solely on

cash to complete the acquisition of another company. Therefore, the realization of corporate mergers and acquisitions requires a large amount of external financing. External financing mainly includes debt financing and equity financing, and enterprises can make decisions on financing ratios from the perspective of taxation.

#### **4.1.1 Internal Financing**

The use of an enterprise's own funds does not have to pay borrowing interest and other expenses, does not increase the financial risk of the enterprise, and does not expose shareholders to the risk of equity dilution. However, from the perspective of taxation, if the internal funds of enterprises cannot be paid before tax, enterprises will bear a large tax burden and will also face the risk of double taxation.

#### **4.1.2 Equity financing**

That is, the acquiring enterprise uses the issuance of shares to raise funds. Since there is no fixed maturity date for common shares and no pressure to pay fees on a regular basis, the company does not need to repay the investment amount and does not need to spend a lot of cash, but it may lead to dilution of the shareholding. From a tax point of view, dividends issued by enterprises are not allowed to be deducted before tax, so the tax burden of enterprises is relatively high.

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That is, the acquisition enterprise uses the way of increasing debt to raise funds, mainly including bank borrowing and bond issuance. Loan interest expense can be deducted before tax, so it can reduce corporate income tax and reduce the tax burden of enterprises; Issuing bonds not only covers interest expense before tax, but also is more flexible than borrowing; When an enterprise uses convertible bonds for financing, the effect of interest tax deduction can be generated in the early stage, and if the enterprise is operating well in the later stage and creditors are willing to convert the bonds into ordinary shares, the enterprise does not have to repay the cost of the bonds, reducing the pressure of repayment.

Example: Suppose Company M plans to acquire Company P for 800 million yuan, and all the funds need to be raised externally. Before the merger, Company M's asset-

liability ratio was 50%, the total assets were 1 billion yuan, the original share capital was 100 million shares, the after-tax profit was 150 million yuan, and the after-tax profit after the completion of the acquisition would reach 200 million yuan, and the borrowing interest rate was 8%. Due to the financial position and good standing of Company M, the 800 million yuan can be obtained in full through bank loans. If Company M is financed through a bank loan, the financing cost is lower than that of an equity acquisition. However, after the acquisition, the asset-liability ratio of Company M increased to 72.22%, which greatly increased the financial risk of Company M; EPS increased from 1.5 ( $15000 \div 10000$ ) to 1.52 [ $(20000-4800) \div 10000$ ]. If Company M borrows 400 million yuan from the bank and issues 40 million ordinary shares at 10 yuan per share, then the asset-liability ratio of Company M will remain unchanged after the merger; However, the increase in equity capital led to a change in earnings per share. EPS decreased from 1.5 to 1.26 [ $(20000-2400) \div (10000+4000)$ ], and at the same time, Company M will also face the risk of dilution of equity.

When enterprises carry out financing, they often adopt a combination of multiple financings. Taxation is only one aspect of the various costs and risks that need to be considered when financing a business. If only from the perspective of tax reduction, bond financing is undoubtedly the best choice, but the increase in debt will increase the financial leverage of the enterprise, thereby increasing the financial risk of the enterprise, resulting in the cost of debt capital of the enterprise exceeding the cost of equity capital; If enterprises have difficulties in operation, they will face tremendous debt pressure. In addition, if the company originally has idle funds but uses debt financing, it will lead to a decrease in the efficiency of the use of the company's funds, so that Reduced shareholder compensation. When the rate of return on EBIT investment of an enterprise is higher than the debt financing cost of the enterprise, the use of debt financing can reduce the overall capital cost of the enterprise and increase the return on investment of shareholders, and vice versa, it will reduce the return to shareholders. Therefore, M&A enterprises should consider cash in a comprehensive manner. Equity. Financing options with different proportions of debt, and choose financing strategies that can maximize the value of the company.

#### 4.2 Tax planning analysis of the payment process

Enterprise mergers and reorganizations can complete the acquisition of target enterprises through various payment methods, such as cash, stocks, bonds, and asset replacement. Different payment methods will incur a very different tax burden.

#### 4.2.1 Cash Payments

The acquisition of the target enterprise by the enterprise through cash can save the acquirer from the risk of equity dilution, but the acquirer not only needs to bear a lot of financial pressure, but also difficult to obtain tax-saving benefits. The acquired enterprise also faces a lot of taxes, and the room for tax planning is relatively small, and it cannot obtain the tax deduction effect of other payment methods (such as borrowing interest). Of course, cash payments may result in more favorable transaction prices, and when the difference between this transaction price and other payment methods can make up for the tax losses that the business has not earned, then cash payments are advantageous.

#### 4.2.2 Stock Payments

The M&A enterprise issues ordinary shares to the target enterprise to achieve the merger. This payment method can effectively reduce the tax of the parties to the merger and acquisition Pressure take-off. Under certain conditions, the acquirer can offset the losses of the acquired party Minus its current profit. When the corporate merger and reorganization business meets the requirements of special tax treatment, and The proportion of equity purchased by the acquirer of the target enterprise shall not be less than that 75%, the proportion of equity payment to the total transaction amount is not less 85%, then either acquisition Both the party and the acquired party are treated according to the book value of the equity of the target enterprise. In addition, if an enterprise that meets the special restructuring requirements conducts mergers and acquisitions, the proportion of equity paid by the acquirer to the total transaction amount shall not be less than that 85%, and under the same control merged For mergers and acquisitions that do not require payment of consideration, they can be based on the accounts of the equity of the acquired party Face value is treated and can be offset by the losses of the acquired party 税。 Relative to the national tax issue (2000) 118 The provisions of the fiscal and tax (2009) 59 Pair The threshold for tax-free restructuring has been raised, but still allows enterprises to pass the reconciliation each The proportion of the payment method and the space for tax planning.

#### 4.2.3 Assume the debt of the target enterprise

It refers to the acquirer to assume the target enterprise Debt as a condition to realize the acquisition of the target company. This method of M&A is usually used when the acquiree is insolvent, and the acquiree's ownership equity is close

to zero or even negative。 《Circular of the State Administration of Taxation on income tax issues related to business mergers and divisions》 (Guo Shui Fa [2000] 119, abolished) requires the acquirer's acquisition costs to be determined by the net book value of the target enterprise's assets。 Guo Shui Fa [2000] 119 After the lapse, it was replaced by fiscal and taxation[2009]59 There is no specific provision for debt-bearing M&A。 The method of consolidating the debts of the target enterprise is not included in the scope of special treatment, so it can only be treated as a general business combination, that is, it is calculated based on the fair value of the assets and liabilities of the acquired party, and cannot use the losses of the acquired party for tax deduction, and the acquired enterprise needs to calculate the income from the transfer of assets。 However, the acquirer can still benefit from pre-tax payment of tax interest expense, so this payment method can obtain the effect of interest deduction。

#### 4. 2. 4 Integrated payment methods

It refers to the acquisition of target enterprises by using cash, stocks, asset replacement, bonds and other methods to achieve mergers and acquisitions of target enterprises. Diversified payment methods can give businesses more flexibility in tax planning. Enterprises can invest in acquired parties through fixed assets, inventory, etc. as consideration, so as to optimize the asset structure. Of course, investing in inventory and fixed assets is subject to VAT. By reasonably arranging the proportion of equity and debt investment, an enterprise can not only obtain the tax deduction effect of interest, but also use the special restructuring clause to use the losses of the acquired party to deduct the tax. In addition, when selecting the payment ratio of equity and debt, an enterprise should adopt a scientific calculation method to determine the proportion of payment that maximizes tax benefits.

Example: Suppose Company K uses a private placement to issue 50 million ordinary shares of RMB 5 per share to Company Z and acquire 60% of the shares of Company Z. Company Z's registered capital is 250 million yuan. Since the special tax treatment requirements are not met, accounting can only be carried out according to general principles。 Therefore, Company Z needs to calculate the income from equity transfer:  $5 \times 5000 - 25000 \times 60\% = 100$  million yuan, its income tax (assuming a tax rate of 10%) is:  $10000 \times 10\% = 10$  million yuan, and the tax basis of Company K's investment in Company Z is:  $5 \times 5000 = 250$  million yuan; If

Company K chooses to acquire 75% of the equity of Company Z, it meets the conditions for special restructuring (assuming that the other conditions for special tax treatment in the Circular are met), then Company Z does not need to recognize the income from the equity transfer of 100 million yuan, and the tax basis of Company K's investment is:  $250 \text{ million} \times 60\% = 150 \text{ million yuan}$ . This deferred the current income tax of \$100 million.

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