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Notice Concerning Receipt of Written Notice of Reassessment Order from Nagoya-Naka Tax Office Directed at Subsidiary and Revisions to Earnings Forecasts

KATITAS Co., Ltd. (the “Company”) hereby provides notice of the following. The Company’s subsidiary REPRICE Co., Ltd. (“REPRICE”) was subject to a tax examination by Nagoya-Naka Tax Office (the “tax authorities”) in September 2022, and today (April 27, 2023), REPRICE received “Notice of Reassessment Order for Consumption Tax and Local Consumption Tax and Notice of Decision to Impose Additional Tax” (hereinafter the “Reassessment Order, etc.”) from the same office.

As a result of REPRICE receiving this Reassessment Order, etc., for its settlement of accounts of the fiscal year ended March 31, 2023, the Company has decided, as detailed below, to record ¥1,332 million in extraordinary losses as differences in consumption taxes, etc. for the five years corresponding to the period subject to the tax examination and ¥429 million for the refund of income taxes (reduction of income taxes; hereinafter, these losses are collectively referred to as “Recording of Extraordinary Losses, etc.”).

In line with the Recording of Extraordinary Losses, etc., the Company has revised, as detailed below, the consolidated earnings forecasts for the fiscal year ended March 31, 2023, which were announced on May 13, 2022.

The accounting and tax treatment practiced by REPRICE, which received this guidance from the tax authorities, is the same as the accounting and tax treatment adopted by the Company. Concerning the accounting and tax treatment adopted by the Company, the Company has filed a lawsuit seeking the revocation of a reassessment order, etc. from the tax authorities as outlined in “Notice Regarding Reassessment Receipt of Written Notice from the Kantoshinetsu Regional Taxation Bureau and Revision of Earnings Forecasts” announced on April 28, 2020 and “Update Regarding Measures in Response to Reassessment Receipt of Written Notice from the Kantoshinetsu Regional Taxation Bureau (April 28, 2020)” announced on March 23, 2021. The aforementioned lawsuit is awaiting the first instance verdict at the Tokyo District Court on May 25, 2023.

The KATITAS Group views the current Reassessment Order, etc. by the tax authorities to be unacceptable and plans to promptly file an appeal or take other necessary procedures against it.

1. Circumstances and details regarding the Reassessment Order, etc.

From September 2022, REPRICE was subject to a tax examination by the tax authorities targeting the five-year period from the fiscal year ended March 31, 2018 to the fiscal year ended March 31, 2022. The tax authorities asserted that, based on the results of their tax examination, in the method of calculating the amount of

consumption taxes that REPRICE adopts, which is described below, there is no way of making a distinguishing classification between consideration for non-taxable asset transfers and consideration for taxable asset transfers, and that falls under the “case where the value is not rationally separated” stipulated in Article 45, paragraph 3 of the Order for Enforcement of the Consumption Tax Act, and issued the Reassessment Order, etc.

1) Method adopted by REPRICE for calculating the amount of consumption tax

REPRICE concluded sales agreements with buyers that covered the land and buildings as a single unit and calculated the amount of consumption tax applicable to the buildings through a proportional division method using the assessed value of fixed assets tax for the land and buildings of the property delivered (“REPRICE’s Proportional Division Method”).

REPRICE’s Proportional Division Method was adopted based on the National Tax Agency’s Tax Answer “No. 6301 Tax Base Q&A: Building Price in the Event of a Lump Transfer of Building and Land,” which states that using the method of proportional division based on the assessed value of inheritance tax or the assessed value of fixed assets tax is deemed to be a rational method for separating the land and building portions.

The accounting and tax treatment adopted by REPRICE had been discussed in the tax examination regarding the accounting treatment for consumption tax, etc., targeting the fiscal years from the fiscal year ended May 31, 2012 to the fiscal year ended May 31, 2014, which was carried out recently. However, as that discussion did not result in REPRICE receiving special guidance, REPRICE continued to adopt the accounting and tax treatment method.

2) Reason for the Reassessment Order, etc. from the tax authorities

The tax authorities assert that “the amount of the transfer consideration of the taxable asset and the amount of the transfer consideration for the non-taxable asset” are “not rationally separated” in REPRICE’s accounting and tax treatment, citing the reason that “with the method that applies proportional division to the total sales amount using the assessed value of fixed assets tax, the added value relating to the renovation does not get reflected in the building’s price.”

3) Articulation of the problem

In principle, the amount that the Consumption Tax Act treats as the tax base is the amount of consideration that passes between the parties involved in the transfer, etc., of a taxable asset. Where a taxable asset and a non-taxable asset are transferred together, a rational method is required to separate the amount of consideration for transfer of the taxable assets and the amount of consideration for transfer of the non-taxable assets. To provide for cases where these assets are not rationally separated, an exceptional provision is established in the tax base for consumption tax pertaining to the transfer, etc. of the taxable asset, stipulating that the taxable amount be obtained by multiplying the amount of consideration for the transfer of assets by the percentage of the part of the consideration of the taxable asset existing in the total amount, comprising the consideration of the taxable asset and the consideration of the non-taxable asset at the time this asset is transferred (Article 45, paragraph 3 of the Order for Enforcement of the Consumption Tax Act).

The difference of opinion between the tax authorities and REPRICE is whether or not REPRICE’s Proportional Division Method falls under the exceptional provision of the “case where the value is not rationally separated” in Article 45, paragraph 3 of the Order for Enforcement of the Consumption Tax Act.

4) Summary of REPRICE's main assertions

- i. REPRICE's Proportional Division Method is a method for separating taxable assets from non-taxable assets based on an objective standard of the assessed value of fixed assets tax, and proportionally dividing the total sale payment amount by the assessed value of fixed assets tax is accepted by the National Tax Agency as being generally rational.
- ii. The sales activities of REPRICE, carried out as part of its handling of multiple properties, begin with advertising the property information and its listing price on REPRICE's website and real estate portal websites directly after the property is procured. Because of that, REPRICE needs to calculate the consumption tax of multiple properties directly after their procurement. Therefore, the method for calculating consumption tax that the tax authorities are insisting upon, which involves proportional division method that adds the actual cost price of renovation to the cost price of the building, is not a method that can be adopted under REPRICE's business flow. For that reason, REPRICE's Proportional Division Method is a rational method that matches REPRICE's business flow.
- iii. With regard to the tax authorities' assertion that the added value due to renovations is not reflected in the building price, the consumption tax base is originally the amount of consideration that passes between the parties involved, and added value due to renovations is not considered in the calculation of the amount of consideration that constitutes the tax base.
- iv. The "case where the value is not rationally separated" in the Order for Enforcement of the Consumption Tax Act is interpreted as referring to relatively limited scope of cases such as where the parties have decided the consideration arbitrarily between themselves, such as when the content of the agreement document and the facts do not agree, for example where the parties have colluded in a misrepresentation. When REPRICE concludes a sales agreement for land and buildings with the buyer, all of the agreement documents created by REPRICE with the buyer bear the consumption tax amount and are signed or stamped with registered seals of the seller (REPRICE) and the buyer based on the parties' intention, showing clearly that the documents are genuinely agreed in accordance with the free will of the parties. Since there was no condition of collusion in a misrepresentation between REPRICE and the buyer, the transfer payment for the buildings stated in the agreement document should be treated as the tax base under the Consumption Tax Act.

5) Amount of the effect from the Reassessment Order, etc.

For the consolidated earnings of the fiscal year ended March 31, 2023, the Company will record ¥1,332 million in extraordinary losses for differences in consumption taxes, etc. for the five years corresponding to the period subject to the tax examination and ¥429 million for the refund of income taxes (reduction of income taxes).

6) Future plan

The KATITAS Group has been in consultation with external experts from within the tax examination period, and as described above, it believes that there is no error in the KATITAS Group's existing accounting and tax treatment. Since the KATITAS Group is unable to completely agree with the Reassessment Order, etc. from the tax authorities, it intends to promptly undertake the necessary procedures, such as filing an appeal.

2. Revisions to earnings forecasts

1) Revisions to the consolidated earnings forecasts for the fiscal year ended March 31, 2023 (from April 1, 2022 to March 31, 2023)

	Net sales	Operating profit	Ordinary profit	Profit attributable to owners of parent	Basic earnings per share
	Millions of yen	Millions of yen	Millions of yen	Millions of yen	Yen
Previous forecast (A)	113,376	14,018	13,875	9,355	121.08
Revised forecast (B)	121,341	14,060	13,833	8,539	110.26
Changes (B-A)	7,965	41	(41)	(815)	
Changes (%)	7.0	0.3	(0.3)	(8.7)	
(Reference) Results of the fiscal year ended March 31, 2022	101,269	13,127	12,697	6,845	88.71

2) Reason for the revision

In the fiscal year ended March 31, 2023, families living in rental homes, in particular, have a strong desire to buy inexpensive, high-quality houses or to improve their living environments, and as a result of the number of such customer inquiries increasing, the number of properties sold is now expected to be 6,927 properties, which surpasses the initial plan of 6,845 properties. Moreover, by setting selling prices with a cost-pass-through approach that takes into account the impact of the rising prices of materials and other factors, the unit selling price has risen. As a result, net sales have been projected to exceed the plan.

On the other hand, although the gross profit per unit on properties sold was maintained at a high level, there has been a trend of the unit selling price significantly exceeding the plan, mainly in suburban areas, and the gross margin is expected to be 22.1%, which is below the plan. However, as a result of improving sales and purchasing productivity per sales person, we compensated for the drop in gross margin, and operating profit is expected to exceed the plan, taking into account our decision to pay end-of-year special bonuses of ¥305 million.

Please note that ordinary profit is expected to be lower than the plan because we recognized ¥48 million as non-operating expenses for the arrangement fees described in “Notice Regarding the Conclusion of a Changing Syndicated Loan Agreement (Increase Maximum Amount of the Commitment Line)” released on March 31, 2023.

Furthermore, as mentioned in section 1 above, profit attributable to owners of parent is expected to be below the forecast because the Company’s consolidated subsidiary REPRICE posted extraordinary losses as a result of the Reassessment Order, etc. for the period from the fiscal year ended March 31, 2018 to the fiscal year ended March 31, 2022.

Please note that together with the revision to the earnings forecasts, the Company has also revised the dividend forecast for the year-end dividend for the fiscal year ended March 31, 2023. For details, please refer to the “Notice of Upward Revision to Dividend Forecast for the Fiscal Year Ended March 31, 2023” released today.

(Note) The earnings forecasts have been prepared based on information currently available to the Company as of the date of this material’s release and actual results may differ from the forecasts due to various factors

going forward.

3. Impact from the ruling of the lawsuit filed by the Company

The first instance verdict for the lawsuit filed by the Company at the Tokyo District Court, as described above, is scheduled to be on May 25, 2023. Depending on the ruling, the consolidated earnings figures for the fiscal year ended March 31, 2023 may be affected. The effects will be as described below.

(1) If the Company wins the lawsuit

There will be no effect on the earnings figures.

(2) If the Company loses the lawsuit

(i) Accounting treatment for the fiscal year ended March 31, 2023

As the Company is continuing its existing accounting treatment for the previous fiscal years even after receiving the Reassessment Order, etc., a discrepancy with the calculation method advocated by the tax authorities has arisen for the fiscal year ended March 31, 2022 and the fiscal year ended March 31, 2023. Moreover, for REPRICE, as the fiscal year ended March 31, 2023 was outside the target period of the tax examination, a discrepancy with the calculation method advocated by the tax authorities has arisen for the fiscal year ended March 31, 2023.

Because of the above, the KATITAS Group plans to record the difference arising from the discrepancies between the accounting treatment of the Company and REPRICE and the calculation method advocated by the tax authorities as extraordinary losses for the fiscal year ended March 31, 2023.

The breakdown of the aforementioned is as follows.

Target period	Fiscal year ended March 31, 2022 portion	Fiscal year ended March 31, 2023 portion	Impact on earnings of the fiscal year ended March 31, 2023 if lawsuit is lost
Impacted company	KATITAS	KATITAS, REPRICE	
	Millions of yen	Millions of yen	Millions of yen
Differences in consumption taxes, etc.	1,361	2,141	3,503
Income taxes - current	-	(526)	(526)
Refund of income taxes	(368)	-	(368)
Impact on profit attributable to owners of parent	992	1,615	2,607

(3) Future schedule regarding the lawsuit

As mentioned above, the first instance verdict for the lawsuit filed by the Company is scheduled to be made at the Tokyo District Court on May 25, 2023.

Since the lawsuit filed by the Company is expected to proceed to the court of second instance and the court of final appellate instance, the Company expects a period of about three years from this point in time will be required before a final verdict is reached.