



Grant Thornton

An instinct for growth™

# Doing business in Japan

If you are planning on doing business in Japan, knowledge of the investment environment and information on legal, accounting, taxation and human resource frameworks are essential to keeping you on the right track.





Grant Thornton

An instinct for growth™

**“Trust is fundamental to building business. In Japan, a strong trusting relationship, not only with your team but also with your business partners, will take your business halfway to success”.**

**Yoichi Ishizuka, Managing Partner  
Grant Thornton Taiyo Tax Corporation**

# Contents

Foreword .....	3
Country Profile .....	4
Business Entities .....	6
Branch versus Corporate entity .....	10
Partnerships .....	13
Accounting and reporting requirements .....	17
Corporate taxation .....	20
Consumption tax .....	27
Individual taxation (*) .....	37
Social Security (*) .....	53
International Social Security Agreements (*) .....	59
Inheritance Tax and Gift Tax .....	56
Other Taxes .....	64
Employment Regulations and Industrial Relations .....	73
Manufacturing and Other Trade Regulations .....	76
Contact details .....	78

\* Information updated as for 2020

---

# Foreword

---

“Grant Thornton Japan” represents a collaboration of independent professional firms including Grant Thornton Taiyo LLC, Grant Thornton Taiyo Tax Corporation, Grant Thornton Taiyo Inc., Grant Thornton Taiyo Advisors Co., Ltd, Grant Thornton Taiyo Human Capital Corporation and Grant Thornton Taiyo Accounting Service Inc.. We are the Japan member of Grant Thornton International Ltd.

Grant Thornton is one of the world’s leading organisations of independent assurance, tax and advisory firms. These firms help dynamic organisations unlock their potential for growth by providing meaningful, forward looking advice. Proactive teams, led by approachable partners in these firms, use insights, experience and instinct to understand complex issues for privately owned, publicly listed and public sector clients and help them to find solutions. More than 53,000 Grant Thornton people, across over 135 countries, are focused on making a difference to clients, colleagues and the communities in which we live and work.

If you require any further information, please do not hesitate to contact your nearest Grant Thornton member firm.

This guide has been prepared for the assistance of those interested in doing business in Japan. It does not cover the subject exhaustively but is intended to answer some of the important, broad questions that may arise. When specific problems occur in practice, it will often be necessary to refer to the laws and regulations of Japan and to obtain appropriate accounting and legal advice. This guide contains only brief notes and includes legislation in force as of 30 September 2019.

“Grant Thornton” refers to the brand under which the Grant Thornton member firms provide assurance, tax, human capital and advisory services to their clients and/or refers to one or more member firms, as the context requires. Grant Thornton International Ltd (GTIL) and the member firms are not a worldwide partnership. GTIL and each member firm is a separate legal entity. Services are delivered by the member firms. GTIL does not provide services to clients. GTIL and its member firms are not agents of, and do not obligate, one another and are not liable for one another’s acts or omissions.



# Country Profile

## Overview

Japan is a democratic island country that is located in north-eastern Asia. The capital city is Tokyo. Most of the population speaks Japanese as their first language. The terrain is mostly mountainous with about 70% forest. The climate is full of seasonal changes.

Japan has the population of about 126 million, which is the eleventh largest in the world. Its GDP is about 5.17 trillion, ranked the third largest in the world, after the United States and China as of 2019. Manufacturing industry is strong and is often ranked the one of most innovative country. In addition, a huge highly developed domestic market exists in Japan on the back of large population.

The population is aging due to a decrease in birth rates so that serious labour shortage will be expected in the near future. In response to this significant problem, the government encourages to make the country more open and attract foreign businesses.

## Economy

Since in late 2012, Japanese government announced that a comprehensive policy package to revive the Japanese economy from two decade of deflation, the aging of society and shrinking of the population, which is called “Abenomics”. Abenomics is based on “three arrows” of monetary easing, fiscal stimulus and structural reforms to improve its investment environment.

As a part of these measures, the government carried out lowering tax, deregulation and structural reform in the sector of agriculture, medical care and energy. The effective corporate tax rate has reduced from 38% to 29% for the past ten years, and set up tax credits to promote capital investment and a pay increase. As a result, the economy is recovering from deflation and continues to boom.

Furthermore, Japan sees the greatest issue of the aging society and shrinking of the population as an opportunity, because this challenge will soon be shared by most developed countries. Japan is committed to achieving a pioneer in the establishment of a new social model, taking the following solutions; Productive individual and society, smart regulations and laws, attractive international opportunities, and more competitive business.

2020 Tokyo Olympic games have been postponed 2021.

## Business infrastructure

Japan has great convenient transportation infrastructure, which consists of airports and high-speed rail way lines (Shinkansen). The safety and precision are appreciated very highly. Furthermore, infrastructure fees, such as transportation fees, high speed internet fees and real estate cost are reasonable, compared to the other developed countries.

## Living

Japan is ranked the one of the most safe and peaceful countries, based on items including crime rate and terrorism. Some of the cities are ranked as the most liveable cities in the world. The cost of living in the major cities such as Tokyo and Osaka, is about the same as other large cities. The cost of living in Tokyo is about 10% higher than for the rest of the country. If you are moving to a small town, your rent and food expenses will likely be much lower.

Japan has excellent healthcare systems. Everyone can receive the same medical services anytime all over Japan. Japan is also known as a gastronomic country, with the most Michelin starred cities in the world. In addition, Japanese cuisine is recognized by UNESCO as an intangible cultural heritage.



# Business Entities

There are a number of entities available to the foreign investor doing business in Japan. Naturally the nature of the investor's activities in Japan largely determine the entity chosen. The most common entities used include:

Representative Office

Japan Branch Office

Corporate-type entity, such as:

- Kabushiki Kaisha ("KK": a limited stock corporation)
- Godo Kaisha ("GK": a limited liability corporation)

Partnership-type arrangements, such as:

- Nini Kumiai (partnership)

## Representative Office of a foreign company

Foreign companies looking to expand into Japan may initially conduct market research and other "non-commercial transactions" through an unregistered Representative Office. A Representative Office is not required to comply with government reporting or corporate registration requirements, except where the foreign company is a financial institution.

As the Representative Office is not carrying on sale-type activities in Japan, and therefore not generating any income through its activities, it need not file a tax return. However, the employees of the Representative Office will be liable for Japanese income taxation if they receive compensation for the rendering of personal services in Japan.

As a Representative Office is unable to engage in customer negotiations, or solicit sales, and the individual representative is held jointly and severally liable with the foreign company for any transactions, claims, or other liabilities in Japan, the entity is used primarily on a temporary basis by foreign companies that intend to establish a registered branch office or Japanese subsidiary in the near future

## Japan Branch Office

Foreign companies looking to do more than marketing or other Representative Office type activities may incorporate a branch office, as a branch office is generally able to perform sales activities without restriction. As a branch office is regarded as being the same entity as its foreign head office from a Japanese legal and tax viewpoint, its Japan source income will be subject to Japanese taxation.

While a branch is subject to Japanese corporate tax, there are some potential benefits in establishing a branch as opposed to a corporate entity such as a KK or GK. These, along with some disadvantages are discussed in more detail in on page 14.

### Establishment

The establishment of a branch requires the appointment of a representative who is a resident of Japan (no nationality requirement), and registration as a foreign company under the Corporate Law, before it can commence its business activities. It typically takes about four weeks to set up a Japan branch.

## Corporate type entities

There are four types of incorporated companies available under Japan's Commercial Code:

- Kabushiki Kaisha (limited stock corporation which is organized only by limited shareholder(s).);
- Godo Kaisha (limited liability corporation which is organized only by member(s) with limited liability);
- Gomei Kaisha (general partnership corporation which is organized only by member(s) with unlimited liability); and
- Goshi Kaisha (limited partnership corporation which is organized by members with unlimited liability and limited liability).



## Kabushiki Kaisha

The most common form of corporate entity used in Japan by foreign investors is the Kabushiki Kaisha (“KK”). The KK is a limited stock corporation, meaning its shareholders are protected from liability claims made by third parties (up to their capital contribution). The minimum capital requirement to set up a KK is as low as JPY 1.

The KK has a higher level of prestige in Japan than other corporate forms and further, under Japanese law, certain regulated activities (such as pharmaceutical, securities, or telecommunications) in some cases may only be performed by a KK.

- **Formation**

The formation of a KK requires at least one director, who is not required to be a Japanese resident, and also requires at least one shareholder (who can also be the director). Articles of Incorporation and other registration documents are prepared and filed with the Legal Affairs Bureau. Once the registration has been processed, the KK may open a bank account, execute contracts, and engage in other activities as a legal entity. Capital contributions made by shareholders may be in the form of either assets or cash. Non-cash contributions for a KK require a court supervised appraisal unless one of the following applies: (i) the number of shares issued to persons who make a non-cash contribution is not more than 10% of the value of the outstanding shares, (ii) The value of the non-cash contribution is JPY5 million or less, (iii) the non-cash contribution is in the form of marketable securities, (iv) a qualified person such as lawyer, CPA or licensed Tax Accountant issues an appraisal report.

It typically takes about four weeks to set up KK.

- **Internal Structure**

The Companies Act in Japan outlines the requirements for establishing a KK, which has created a number of categories of KK, based on whether it is large or small, open or closed, listed or non-listed. The corporate governance and management structure for KKs will vary depending on whether or not the KK is open or closed, and large or small.

All KKs need at least one director. In cases where three or more directors are appointed, a board of directors and a statutory auditor need to be appointed.

- **Statutory Filings**

Once the KK has been organised in accordance with the relevant corporation law requirements, the following reports need to be filed:

Tax filing report to the relevant district tax office, and the relevant metropolitan or prefecture tax office

Social Insurance report to the Social Insurance Office, the Labour Standards Inspection Office, and the Employment Security Bureau.

A report must also be submitted to the Minister of Finance and other Ministers having jurisdiction over the company's business activities through the Bank of Japan.

Subject to a shareholders' resolution, the KK is allowed to pay dividends, within the Distributable Amount defined in the Companies acts, at any time during the year or any number of times.

## Godo Kaisha

A Godo Kaisha (“GK”) is a corporate entity loosely based on the U.S. LLC in that the liability of the investors in the GK is limited to their capital contribution. However, unlike the U.S. LLC for US tax purposes, it is not a pass through entity for Japanese tax purposes.

- **Formation**

Unlike the KK, in which those who invest are known as shareholders, investors in a GK are referred to as “members”; with each member signing the GK’s Articles of Incorporation. When there are no individual members, a management person, responsible for managing the company on the members’ behalf, needs to be appointed. Articles of Incorporation must be prepared and filed. Once capital contributions have been made and the registration has been processed, the company may open a bank account, execute contracts, and engage in other activities as a legal entity. Capital contributions made by members may be in the form of either assets or cash (unlike KKs, non-cash contributions do not require an inspection by a court appointed inspector). It typically takes two to three weeks to establish a GK.

- **Statutory Filings**

The statutory filings for the GK are the same as for the KK, listed above.

- **Internal Structure**

The legal duties of GK managers are similar to the legal duties of KK directors. GK members may sue managers in the same way that KK shareholders may sue directors on the company's behalf.

Unlike certain types of KK, a GK is not required to establish a board of directors or hold members' meetings to manage the GK's affairs. Each member is responsible for managing the affairs of and representing the GK, however there is scope for this role to be narrowed under the GK's articles.

- **U.S. Tax Entity Classification**

Whether a GK will be treated as a separately taxed (corporate) or as a pass-through entity will depend on the tax laws of the applicable jurisdiction. For U.S. tax purposes, a GK can be treated as a default corporation that can elect to be treated as a pass-through (either disregarded or as a partnership).

- **Partnership Companies**

In addition to KK and GK, Japan's commercial law provides two partnership company forms, the gomei kaisha and the goshi kaisha.

## Gomei Kaisha

A gomei kaisha is a company with unlimited liability members who are jointly and severally liable for the company's liabilities.

## Goshi Kaisha

A goshi kaisha is generally similar to a gomei kaisha, except that there are members with both unlimited and limited liability.



**Corporate entity**

Generally, there are no major differences between the branch of a foreign company and a Japanese company from a tax perspective. However, different legal definitions as well as some small differences in terms of taxation exist.

Additionally, the following needs to be considered on a practical level:

## The advantages of a branch relative to a subsidiary are:

- There is no requirement to appoint directors and statutory auditors for it, however the Branch Manager must be a resident of Japan
- Loss of branch business can be added to the financial figures of the head office.
- No Japanese withholding income tax is applicable to the remittance of branch profits to its head office. In the case of a company, dividends remitted overseas (including liquidation dividends) are subject to Japanese withholding tax at 20.42% or reduced tax treaty rates.
- Additional tax on undistributed profits of a family company (see page .35) is not applicable to a Japan branch of a foreign company.

## The disadvantages of a branch relative to a subsidiary are:

- In addition to the financial statements of the Japanese branch office, the financial statements of the foreign company's head office need to be submitted to the tax office.
- Per capita inhabitant tax is assessed based on the share capital of the head office, leading to generally higher assessments than for a Japanese subsidiary company.
- Business scale taxation is determined based on the capital stock of the head office. Therefore, if a branch has a head office with a big amount of capital, the branch is subject to business scale taxation leading to generally higher tax..
- Company entities (in particular KJs) have greater prestige than a branch office in the eye of Japanese customers, clients and other stakeholders.

## Permanent Establishment (PE)

Under the 2018 tax reform, the AOA (Authorised OECD Approach) rule was applied to the taxation of a Permanent Establishment (PE) and applicable for fiscal years beginning on or after 1 January 2019. As a result, the taxation of foreign corporations depends on whether they own PE or not. A branch should be treated as a typical PE. The definition of PE is the following:

- Branch Permanent establishments

A branch permanent establishment includes the following facilities:

1. A place of management, a branch, an office, a factory or a workshop,
2. A mine, an oil or gas well, a quarry or any other place of extraction of natural resources

- Construction activity permanent establishment

A building site or construction site or installation project or similar work or services in the supervision of such projects in Japan, which is carried on for a period of more than 1 year.

- Agency permanent establishment

A person who is acting in a contracting state on behalf a foreign company and habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts that are routinely conclude without material modification by a foreign company.

**Change of source rule**

The source rule covers the separation of Japan source income and foreign source income. Previously, a foreign corporation operating in Japan through a PE was liable to corporate income tax on the Japan source income of the PE. Therefore, any foreign source income that was attributable to the PE was out of the scope of corporate income tax. Under the AOA, any sourced income through a PE in Japan for business income purposes is considered income attributable to the PE. A foreign tax credit is available for the PE under this reform.

**Intra-company transactions**

The intra-company transactions such as intra-company licences, intra-company loans etc, need to be recognized, because a PE is deemed a separate enterprise conducting business independently from the foreign corporation. Therefore, transfer pricing rules apply to transactions between PEs and head offices. In addition, a PE is required to prepare and maintain documents relating to both intra-company transactions and its transactions with third parties.



**Partnerships**

Partnerships in Japan are not recognized as separate legal entities for Japanese tax purposes. Therefore, partners (kumiai-in) in a partnership (kumiai) are taxed on the basis of the profits or losses allocated to them under such an agreement.

Partnerships fall under one of two categories: the Nin'i Kumiai ("NK") type partnership and the Tokumei Kumiai ("TK") partnership. NK-type partnerships are governed by the Japanese Civil Code while TKs are governed by Japan's Commercial Code.

## NK-type Partnerships

NK-type partnerships are formed by an agreement among parties (kumiai-in) whereby each partner makes an investment in the partnership and carries on a business jointly with the other partners. Such partnerships typically involve arrangements where partners jointly carry on business and together own the assets (and liabilities) of the partnership. A description of the three NK-type partnerships available in Japan follows.

### Nini Kumiai (NK)

The NK is the most commonly used NK-type partnership used in Japan, with all partners jointly owning the assets within the partnership and jointly and severally liable for the partnership's liabilities. Advantages to using the NK are the partnership is not required to be registered and the NK is not limited in the kind of business it can perform.

## Investment Limited Partnership (Toshi Jigyo Yugen Sekinin Kumiai or ILPS)

This partnership type is provided for under the Investment LPS Act which governs ILPSs conducting investment business. The typical ILPS consists of general partners who have unlimited liability and limited partners whose liability is limited to their capital investment. General partners are responsible for managing the partnership's business. Such partnerships need to be registered with the Legal Affairs Bureau.

## Limited Liability Partnership (Yugen Sekinin Jigyo Kumiai or LLP)

The Limited Liability Partnership ("LLP") Act which came into effect in 2005, governs limited liability partnerships. The key feature of the LLP is all partners' liability is limited to their capital investment. In addition, each partner is required to be active in the management of the partnership, however unlike NKs, some restrictions are placed on an LLP's activities. Two further requirements of the LLP are it needs to submit registration with the Legal Affairs Bureau and at least one of the partners must reside in Japan (either an individual or a Japanese company).

## Taxation of Partners

The taxation of a partner in NK-type partnerships will depend on whether the partner is a resident or non-resident of Japan. In the case of non-residents, their tax position will change if they have a permanent establishment in Japan. The nature of the income earned by partners will also determine how it is taxed.

## Japan Resident Partners

Japan resident partners are required to declare any income/loss generated from their partnership arrangements in their Japanese tax return, regardless of whether any actual distribution is made. The nature of the income generated by the partnership's activities will generally be retained in the hands of the individual partner, and taxed accordingly. It should be noted the introduction of a number of laws since 2005 has restricted the utilization of losses generated from partnerships.

## Foreign partners without a Permanent Establishment in Japan

Profit distributions made to a foreign partner in an NK-type arrangement will not be subject to Japan tax if the resident partners are not deemed to be a permanent establishment of the non-resident partner. It should be noted, given the nature of the relationship between the partners in an NK-type arrangement, the risk of the tax authorities deeming the resident partners to be a permanent establishment is significant.

## Foreign partners with a Permanent Establishment in Japan

In such cases, the foreign partner will be required to file a Japan tax return and pay tax at the applicable marginal rate presuming the partner is an individual. Any withholding tax paid on distributions is creditable on their tax return.

## Permanent Establishment

There is no clear guidance under Japanese tax law as to whether the activities of a Japan resident partner of an NK-type partnership create a permanent establishment for non-resident partners in such partnerships. As the determination of a permanent establishment is based on facts and circumstances, each case needs to be analyzed on its own merits.

## Tokumei Kumiai (TK)

A TK is provided for under Japan's Commercial Code. It consists of a TK operator and one or more "silent" or TK investors. A TK is not a legal entity for Japanese tax purposes, but rather an agreement between the TK investor and the TK operator under which the TK operator agrees to operate the business on behalf of itself and the investor. The TK investor makes a contribution to the TK operator in exchange for a percentage of the TK operator's profits or losses. Critically, the TK investor must not have any control in the management of the TK operator.

## Taxation of the TK operator

The TK operator is subject to normal Japanese corporate/income tax as a taxable entity doing business in Japan, however the TK operator is able to claim any income distributions made to the TK investor as a deductible expense. The TK operator will report net income in the case net losses are distributed.

## Taxation of TK investors

The Japanese tax implications of a TK investor may vary, depending on whether the TK investor is a resident of Japan, and in the case where the TK investor is a non-resident of Japan (i) whether it has a PE in Japan, or (ii) the jurisdiction in which the TK investor is a resident.



## Japan resident partners

The Tokumei Kumiai profit/loss allocation is treated as normal taxable income/loss of the TK investor for the particular period in which the income/loss is received. 20.42% withholding tax will be levied on such distributions. Profit/loss distributions received by the investor will be aggregated with the taxpayer's other income and taxed at the applicable marginal rate. With respect to a TK arrangement in which the investment is real estate, an active individual TK investor may be able to offset losses against other income, however a passive TK investor is prohibited from doing so. An active TK investor is one who plays an active role in the business decisions of the Japan TK operator.

## Foreign partners having a permanent establishment in Japan

The profit/loss allocation from the TK to a TK investor deemed to have a PE in Japan is treated as normal taxable income/loss of the TK investor for the period in which the accounting period end date of the TK operator falls. The TK investor is required to file a tax return and pay income tax at the applicable marginal rate. The distributions from a TK to foreign partners are subject to 20.42% withholding tax, which is creditable for the TK investors when declaring such income in their Japanese tax returns.

## Foreign partners not having a permanent establishment in Japan

A TK investor who does not have a PE in Japan is taxed 20.42% withholding on the actual distributions of the TK's profit allocations. There are no further Japanese tax obligations in respect of the TK allocations and no requirements to file a tax return in Japan. It should be noted that non-resident TK partners residing in certain jurisdictions may be able to claim a tax exemption by virtue of that jurisdiction's Double Tax Agreement ("DTA") with Japan containing an "Other income" article which provides such income is only taxable in the country in which the investor resides, meaning such TK distributions are not taxed in Japan. One example is the Ireland-Japan DTA. While Japan's DTAs with other jurisdictions such as the US and the Netherlands also contain an "Other income" provision, protocols to these agreements give Japan the right to impose Japan domestic withholding tax rates on such income, resulting in the 20.42% rate being levied.



# Accounting and reporting requirements

All companies that are incorporated as profit organizations conform to the “Companies Act”, which plays a role in coordinating the interests of creditors and shareholders. In addition, listed companies shall be governed by the “Financial Instruments and Exchange Act” which lays down the rules for the protection of investors. The preparation of financial statements is also established by these laws.

## Contents of financial statements

The Companies Act requires companies to prepare financial statements for each fiscal year. The period of a fiscal year may not exceed one year. Additionally, listed companies of domestic exchanges are required to disclose financial statements on a quarterly basis and annual audited financial statements in accordance with the Financial Instruments and Exchange Act.

The Companies Act requires every company to prepare the followings:

- Balance Sheet
- Income Statement
- Statement of Changes in Net Assets
- Annotations for the above statements
- Supporting schedules

In addition to the above, listed companies are required to prepare a cash flow statement in accordance with the Financial Instruments and Exchange Act.

## Accounting Principles

The financial statements must be prepared in accordance with accounting principles generally accepted in Japan, called J-GAAP. In certain circumstances, the consolidated financial statements are allowed to be prepared in accordance with other accounting standards including International Financial Reporting Standards (IFRS).

## Comparison of J-GAAP and IFRS

The accounting, auditing and disclosure systems in Japan have been substantially revised and have essentially become equivalent to and consistent with internationally recognized systems for several years. As a result, the committee from the EU evaluated that J-GAAP is not identical to IFRS but equivalent to IFRS in the view point of the investors. Through a long-lived process, current differences between them have been reduced to a minimum. The following outlines some of the major current differences between J-GAAP and IFRS:

- **Other comprehensive income not reclassified to profit or loss**  
Under J-GAAP, all of the items recognized in other comprehensive income will be eventually reclassified (recycled) to profit or loss, while IFRS requires some ‘non-reclassifying’ items.
- **Goodwill**  
Under J-GAAP, goodwill must be amortized over not more than 20 years using either the straight line method or any other rational method. If there is an indicator that goodwill has been impaired, the realization of an impairment loss must be considered. Under IFRS, goodwill is not amortized, however an impairment test must be carried out annually and whenever there is an indicator that impairment may have occurred.
- **Research and development costs**  
Under J-GAAP, all expenditure on research and development cost shall be recognized as expenses when incurred. Under IFRS, only research expenditures are generally recognized as expenses. Development expenditures, however, are only considered to be intangible assets if certain requirements are met, such as the asset either being intended to be used or sold later on.

- **Reversal of impairment losses**

Under J-GAAP, reversals of impairment loss are prohibited. Under IFRS, only reversals of impairment losses relating to goodwill are generally prohibited. Regarding other assets, impairments can be reversed if there is an indication that such treatment may be necessary.

- **Fair value model**

Under J-GAAP, neither the revaluation model for property, plant and equipment, nor the fair value model for investment property is allowed.

## Voluntary adoption of IFRS

The Japanese government has eased the required conditions to promote greater use of IFRS on a basis of voluntary adoption. As a result, the number of voluntary adoption is increasing so far. All listed companies and unlisted companies are allowed to use IFRS for consolidated financial statements as of 2019, if they meet some criteria. IFRS is not permitted to be used in statutory financial statements in Japan.

## Statutory audit

“Large companies, as defined by the Companies Act, and listed companies need to receive audit from a CPA. According to the Companies Act, a “large Company” is any Stock Company which satisfies any of the following requirements:

- (a) The amount of stated capital in the balance sheet as of the end of its most recent Business Year is JPY 500 million or more; or
- (b) The total sum of liabilities in the balance sheet at the end of its most recent Business Year is JPY 20 billion or more.

## Retention of accounting documents

Retention period of accounting documents are determined by the Companies Act and the Corporation Tax law. In the main place, the Companies Act requires companies to keep and maintain proper accounting records (financial statements, general ledgers, sub-ledgers, journals, etc.) and important operational and financial documents including minutes or agreements for ten years. Accounting records can be maintained electrically subject to approval by the tax office. Regarding language, no legal regulation specify the official language, however using Japanese is considered appropriate. For foreign companies, using English may be applicable.

## Accounting and reporting requirements applicable to branches

- (1) A foreign company, which has a branch in Japan, must attach the financial statements of the Japan branch as well as those of the company as a whole to the Japanese corporate tax return to be filed each fiscal year.
- (2) A foreign company which conducts banking, insurance, or other regulated business must prepare financial statements for the Government in compliance with the relevant laws governing such industries. There are no accounting and reporting requirements applicable to a branch that conducts non-regulated businesses.

Tax authorities (and regulated authorities in the case of regulated businesses) may examine the branch's business records.

## Currency

Accounting record and statutory financial statements must be presented in Japanese Yen.



# Corporate taxation

The amount of taxable income is computed as the net of gross revenue less costs, expenses and losses on the realisation basis in accordance with J-GAAP and tax adjustments in accordance with the requirement of the corporate tax law. This chapter deals with some of the most important rules of corporate taxation with a special regard to those that are of importance to companies from overseas.

## Administrative overview

### Place of payment of taxes

The place of payment of taxes for a domestic Japanese corporation is usually the place where its head office or principal office is located. The corporation must notify the tax office with jurisdiction within two months of incorporating and before moving from the jurisdiction to another jurisdiction.

### Tax year

The tax year of a corporation is the year specified in its Articles of Incorporation or in laws or regulations. If the tax year is not so specified, the corporation may elect a tax year by notifying the tax office within two months of the date of incorporation. Once established, the tax year may be changed by notifying the tax office.

### Tax returns

Corporate tax returns are due two months after the last day of the corporate taxpayer's fiscal year, however, generally a one month extension can be obtained from the tax authorities. Therefore, a company with a fiscal year of 1 January to 31 December needs to file its corporate tax return on or before 28 February in the following year (31 March if an extension has been granted).

If corporations meet the accounting requirements, corporations receive permission to file interim and final blue tax returns. In this case, corporations obtain some privileges as follows:

- (1) Exclusion from the restriction on use of carried-forward losses
- (2) Ability to claim tax refunds by carrying back losses
- (3) Availability of various tax credit systems

Also, corporate taxpayers are required to file an interim tax returns if the tax for the prior year on a six month basis was more than JPY100,000. A corporation should file an interim tax return within two months from the end of the sixth month of the tax year.

### Payments and fines

Tax reported on interim and final tax returns is required to be paid by the due date for filing tax returns. Late payments of tax carry a penalty at a rate of 14.6% per annum (7.3% for the first two months when the payment is overdue).

## Tax rates

Japanese corporate taxes consist of corporation tax (national tax), local corporation tax (national tax), inhabitant tax (prefectures and municipalities), enterprise tax (prefectures) and special corporate enterprise tax (prefectures).

### (1) Corporation tax

Company with capital of:	Annual taxable income bracket	Applicable rates for fiscal years beginning before March 31, 2019 (%)	Applicable rates for fiscal years beginning before March 31, 2020 (%)	Applicable rates for fiscal years beginning on or after April 1, 2020 (%)
Small or Medium-Sized Enterprises	JPY0 to 8 million	15%	15%	19%
	Over JPY8 million	23.20%	23.20%	23.20%
Ordinary Enterprises	All income	23.20%	23.20%	23.20%

A Small or Medium-Sized Enterprise (SMEs) is a company with share capital of JPY100 million or less. However, a company may not be treated as a SME, if 100% of the shares of the company is directly or indirectly owned by a large sized company whose capital is JPY 500 million or more. In the case, the definition of a large sized company is including not only Japanese parent company but also foreign parent company.

### (2) Local corporation tax

Local corporation tax was introduced along with the reduction in the inhabitant tax rate in the 2014 tax reforms. It is calculated as 4.4% of national corporation tax. The tax applies to fiscal years beginning on or after 1 October 2014. The tax rate will increase from 4.4% to 10.3% for fiscal years beginning on or after 1 October 2019.

### (3) Inhabitant tax

Inhabitant taxes are computed as a percentage of corporation tax within the ranges shown below.

Type	Applicable rates for fiscal years beginning before March 31, 2020 (%)	Applicable rates for fiscal years beginning on or after April 1, 2020 (%)
Prefecture	3.2 to 4.2	1.0 to 2.0
Municipality	9.7 to 12.1	6.0 to 8.4
Total	12.9 to 16.3	7.0 to 10.4

In addition to the above income-based tax, the following per capita taxes are assessed as part of Inhabitant tax.

(Based on a taxpayer in Tokyo Metropolitan Area)

Sum of share capital and capital reserve (JPY '000,000s)	Prefecture (JPY '000s)	Municipality	
		Companies with 50 or fewer employees (JPY '000s)	Companies with more than 50 employees (JPY '000s)
0 to 10	20	50	120
Over 10 to 100	50	130	150
Over 100 to 1,000	130	160	400
Over 1,000 to 5,000	540	410	1,750
Over 5,000	800	410	3,000

#### (4) Enterprise tax

Enterprise tax is computed as a percentage of taxable income at the following rates.

Some types of tax in Japan are levied on a company's share capital amount. Size based business tax is a component of enterprise tax and is levied on a company's business scale, not on the scale of its profits. The taxation applies to corporate tax payers with share capital of more than JPY100 million at the end of a fiscal year.

The tax basis of size-based business tax consists of 3 factors, taxable income, value added based tax and capital based tax

#### Value added-based tax

Base amount of Value added-based tax is calculated according to the following formula;

Taxable income or loss for the year	+	Profit distributed (employee compensation + net interest expense + net rent payments)
-------------------------------------	---	---

#### Capital based tax

Base amount of the capital-based tax is calculated according to the following formula;

Paid in capital	+	Capital surplus for tax purposes
-----------------	---	----------------------------------



## Enterprise tax rate

Component			
		Share capital of over JPY100 million	Share capital less than or including JPY100 million
Income Levy	0 to JPY4 million	0.4%	3.5%
	Over 4 to 8 million	0.7%	5.3%
	Over 8 million	1.0%	7.0%
Value added based tax		1.26%	N/A
Paid in capital levy		0.525%	N/A

## (2) Effective tax rate

The effective tax rate is calculated with the following formula. Applicable rates for a fiscal year beginning on or after October 1, 2019.  $\{(A) \times [1 + (B) + (C)] + (D) \times [1 + (E)]\} / [1 + (D) \times [1 + (E)]]$

Furthermore, there are some size-based taxes, not based on corporate income. These taxes slightly increase the actual tax rate. The following table shows how the effective tax rate can be calculated for a tax year beginning on or after October 1, 2019

Tax	Companies with capital of less than JPY100 million and annual income of JPY8 million or more	Companies with capital of more than JPY100 million
(A) Corporation tax	23.20%	23.20%
(B) Local corporation tax	10.30%	10.30%
(C) Inhabitants tax	7.00%	7.00%
(D) Enterprise tax (Standard rate)	7.00%	1%
(E) Special corporate enterprise tax	N/A	N/A
Effective tax rate	33.58%	29.74%

## Additional taxes on undistributed profits of family companies

A domestic “family company”, which is a domestic company, with more than 50% of its total issued shares directly or indirectly owned by one shareholder together with its relatives (excluding any corporate shareholders who themselves are not family companies), is subject to an additional surtax at the following rates on undistributed income calculated for cash accounting period in excess of a designated amount (minimum JPY20 million):

Annual undistributed profit bracket (JPY '000s)	Applicable tax rate (%)
0 to 30,000	10
30,000 to 100,000	15
Over 100,000	20

The above surtax is suspended for family companies with share capital of JPY100 million or less. However this suspension is revoked if the company is directly or indirectly 100% controlled by a large company (companies with share capital of JPY500 million or more).

## Tax incentives

### Research and Development Tax Credit

The tax credit for research and development (R&D) is applicable to a company filing a blue tax return. In the case of companies other than SMEs, The amount of the tax credit is basically from 6% to 14% of R&D expenditure, which is basically capped at 25% of a taxpayer's national corporate tax liability for a fiscal year. If a company satisfies certain conditions, the maximum creditable amount increases to 40% of the corporation tax liability. SMEs which satisfies certain condition may enjoy from 12% to 17% of R&D expenditures. The maximum creditable amount is 25% of the corporation tax liability for a fiscal year. Additionally, a special R&D tax credit with a cap of up to 10% of national corporate tax liability is applicable to special experiment and research expenses.

### SME investment promotion tax system

When a SME filing a blue tax return makes investments on certain facilities to improve productivity a special depreciation of 30% in addition to regular depreciation or a 7% tax credit will be permitted. The credit is capped at 20% of a company's corporation tax liability.

Additionally if specific infrastructure used to aid the introduction of 5G systems, is both acquired and put into use, a special depreciation of 30% in addition to regular depreciation or a 15% tax credit will be permitted. The credit is capped at 20% of a company's corporation tax liability.

### Salary Increase Incentive

If a company filing a blue tax return that satisfies the requirements related to increase in salary, education cost and acquisition cost, this tax credit is available. The creditable amount is 15% to 20% of increase in salary payments over the previous year. The amount of the tax credit is capped at 20% of the corporation tax liability.

## Deduction of expenses

### Limitation on deductibility of interest expenses

#### (1) Thin capitalization rules

The thin capitalisation rules are designed to prevent Japanese corporations and foreign corporations doing business in Japan from using excessive interest payments to foreign-related persons to reduce their Japan Corporation Tax.

Interest paid by a Japanese corporation on debt to controlling foreign stockholders is disallowed to the extent the average balance of debt on which the interest is paid is more than three times the equity of the controlling foreign shareholders in net assets of the interest paying corporation in that year.

## (2) Earnings Stripping Rules

If a company's net interest payments to related parties are greater than 50% of its adjusted taxable income, the portion in excess of 50% will not be deductible for corporation tax purposes. Net interest payments to related parties do not include payments on which the recipient pays corporation tax in Japan. The interest limitation will not apply in years where the net interest payments are less than JPY10 million or where less than 50% of the total interest payments are made to related parties.

Under the 2019 tax reform, the earnings stripping rule has been amended to be more in line with BEPS Action 4 Interest Deduction and will be applied for fiscal year beginning on or after 1 April 2020. Interest expenses paid to third parties will be included when considering the restriction on interest expense deductibility. Prior to the reform, only interest paid to related parties was subject to restriction. The deductible limit will be reduced to 20% of adjusted income, compared to 50% under the old rule. Additionally, the amount of net interest expense that is exempt from the rule will be increased from JPY 10 million to JPY 20 million.

## Director's remuneration

Remuneration paid to directors of Japanese companies is subject to rules different from the salaries paid to other employees. Directors of Japanese corporations include auditors and liquidators. The following remuneration paid to directors is deductible by corporations:

- (1) Fixed monthly payments
- (2) Fixed payments in accordance with an advance notice to the tax office
- (3) Performance bonuses paid in proportion to the company's earnings to directors who engage in the operation of the company's business. (only in case a company satisfies certain conditions).

## Entertainment expenses

Entertainment expenses are expenses for entertaining customers, suppliers, and other persons associated with the business of the corporation for purposes of furthering the corporation's business interests. For companies whose fiscal years begin on or before March 31, 2020, 50% of meal expenses may be deducted. These expenses exclude meals for employees/directors. SMEs may elect to deduct the larger of 50% of meal/drink expenses or JPY8 million. As for companies whose fiscal years begin between April 1, 2020 and March 31, 2022, these laws stay mostly the same, except that companies whose stated capital exceeds JPY10 billion no longer have to adhere to the deductible limit of 50% of meal expenses.

## Treatment of losses carried forward

### Carried forward losses

Currently tax losses can be carried forward for 10 years and offset against up to 60% of each year's taxable income for a blue tax return filer. The credit limit will be reduced the table as below. SMEs can offset carried forward tax losses against 100% of current year taxable income. An SME is a corporation whose stated capital is JPY 100 million or less, unless 100% owned directly or indirectly by a corporation of which stated capital is JPY 500 million or more.

	<b>Fiscal year beginning between April 1, 2015 and March 31, 2016</b>	<b>Fiscal year beginning between April 1, 2016 and March 31, 2017</b>	<b>Fiscal year beginning between April 1, 2017 and March 31, 2018</b>	<b>Fiscal year beginning on or after April 1, 2018</b>
Credit limit	65% of taxable income	60% of taxable income	55% of taxable income	50% of taxable income

## Double taxation relief

### Dividends received exclusion

Dividends received by a Japanese company from another Japanese company are excluded from taxable income. The exclusion rate varies depending on the ownership rates as follows:

% ownership of related company	Dividend exclusion %
5% or less	20%
More than 5% but not more than 1/3	50%
More than 1/3 but less than 100%	100% less the amount of the recipient's interest expense allocated to the dividends
100%	100%

### Foreign Dividend Exclusion

95% of dividends received by a Japanese company from foreign subsidiaries are excluded from taxable income, provided that the investor company owns 25% or more (or reduced tax treaty rates if available and applicable) of the shares of the company paying the dividend for more than six months.

### Foreign tax credit

A Japanese company may either deduct foreign income taxes or claim a foreign tax credit against corporation income tax. However, a withholding tax on foreign dividend applied to the Foreign Dividend Exclusion is not applied to deduction foreign income taxes and claim a foreign tax credit. Unused foreign tax credits may be carried forward for three years. Furthermore, a foreign tax credit is available for the branch of a foreign company.

### Others

### Withholding tax on interest, dividend and royalty

#### (1) Withholding tax on interest

Interest on loans paid within Japan to a non-resident is subject to withholding tax at the rate of 20.42% (20% national tax, and subject to a 2.1% surtax).

Interest on deposits paid within Japan to a non-resident is subject to withholding tax at the rate of 15.315% (15% national tax, and subject to a 2.1% surtax).

If applicable, a reduced rate under a tax treaty will apply.

## (2) Withholding tax on dividends

Dividends on unlisted shares, paid within Japan by a domestic corporation to a non-resident shareholder, are subject to withholding tax at the rate of 20.42% (20% national tax, and subject to a 2.1% surtax).

Where the Japanese payer of the dividend is a listed company, the rate is 15.315% (15% national tax, and subject to a 2.1% surtax). Where a non-resident shareholder owns more than 3% of the shares in a listed company, the withholding regime for unlisted shares applies.

If applicable, a reduced rate under a tax treaty will apply.

## (3) Withholding tax on royalties

Japanese tax law provides that royalties paid within Japan to a non-resident are subject to 20.42% (20% national tax, and subject to a 2.1% surtax). If applicable, a reduced rate under a tax treaty will apply.

# Foreign exchange conversion

Regarding receivables and payables in foreign currency, a company may select the either method: the method of conversion based on the exchange rate at the time receivables and payables were occurred, or the method of conversion based on the exchange rate at the end of a fiscal year.

# Other taxes

There are other taxes levied on a company in addition to income taxes. Please refer to page 68 for more details.

# Group taxation regime

A 100%-controlled group is formed by a direct or indirect parent-subsidary relationship and a direct or indirect brother-sister relationship. Where a 100%-controlled group does not file a consolidated tax return, there are a few special rules on transactions between domestic members.

Under the group taxation regime each corporation files tax returns and makes tax payments, but special treatments are available, including:

- (1) Dividends received from a 100% subsidiary are exempt from corporate tax.
- (2) No gains/losses are recognized on asset transfers within a 100% group.
- (3) A donor must recognize a non-deductible donation, but a donee is not required to recognize a taxable gift gain.

Capital gains/losses from in-kind distributions within a 100% group are deferred.

# Special Tax Treatment regarding COVID-19

In light of the Coronavirus pandemic in 2020, various tax relief measures were introduced and clarifications regarding existing regulations were made in order to provide support to taxpayers who have been adversely impacted by COVID-19. The following covers the most important pieces of information released by the National Tax Authority:

## Filing and payment extension

Though no general filing extension for corporate tax returns has been issued, companies can opt to file an application for an extension in the case that they are experiencing difficulties in making payments or preparing/filing the corporate tax return on time because of COVID-19. This extension will be granted upon application if certain requirements are satisfied. Taxpayers who file and pay tax under the extension will not be subject to any late filing/payment penalties or interest. When applying for the extension, taxpayers will be required to include specific facts and explain why they are unable to file and pay on time.

## Process to apply for an extension

Taxpayers are required to submit the Application for Extension of Due Date for Filing of Return form. It should be submitted within 1 month after the date on which the extraordinary measure ends (for example the date on which your office was closed because of COVID-19). The filing deadline will be extended by 2 months from the day when the extraordinary measure ends.

## Tax treatment of salary paid to directors

In Japan, payments made to registered directors are treated as non-deductible expenses, unless all payments are the same amount and made at fixed intervals (e.g. monthly).

The amount of the payment may only be changed once a year and must be changed within 3 months of the start of the fiscal year. However, in exceptional cases the amount of the payment can be changed for the reasons stated below, after an extraordinary shareholder's meeting has been held.

- Salary change based on significant changes in the status or duty of a director; or
- Salary decrease in response to significant performance issues.

In light of COVID-19, if salary decreases have occurred because of a significant decrease in sales or if future business conditions are expected to deteriorate significantly, these salary changes can also be treated as exceptional reasons. This means that a company's payments to registered directors may still be treated as deductible, provided the other conditions are satisfied.

## Waiver of accounts receivable from business partners in the event of a disaster

The amount of losses arising from a corporation's waiving of accounts receivable, outstanding contracts, loans, or any other claims equivalent thereto, in whole or in part, within a reasonable period of time after a disaster occurs, for the purpose of supporting the recovery of customers and business partners who have suffered a disaster, does not fall under the category of donations and entertainment expenses.

In addition, in cases where the previous terms and conditions of a contract are changed (such as an extension of payment terms or an exemption of all or some lease premiums, loan interests, instalment payments, etc.), corresponding expenses as well as instalment payments that companies no longer owe will not be treated as donations or entertainment expenses either.

Expenses and losses related to waivers of accounts receivable or changes in contract terms as support for business partners who have difficulty paying their accounts payable due to a decline in sales because of COVID-19 events (e.g. cases where sales decrease or companies become unable to pay because of their limited movement due to the government's request for people to stay home or due to restrictions regarding the entering and leaving of the country) will be treated the same.

## Low-interest or non-interest-bearing loans to customers and suppliers in the event of a disaster

In the event that a company provides a low-interest or interest-free loan to a disaster-affected business partner, and that loan was provided within a reasonable period of time after the occurrence of the disaster for the purpose of supporting the recovery of that business partner, that loan will be deemed to fall under the normal business terms and conditions.

This treatment is also applied to low-interest or non-interest bearing loans, which are provided to business partners who have difficulty paying their accounts payable.

#### **Condolence money, etc. for business partners**

Expenses incurred by a corporation for the purpose of maintaining or restoring a business relationship that had already existed prior to COVID-19 for the purpose of paying condolence money or providing business assets or services to its business partners (for example in cases where the office is closed due to COVID-19) within a reasonable period of time after the disaster occurred are not deemed entertainment expenses.

#### **Expenses incurred for employees of subcontracting enterprises**

If a company, who has both its own employees and those of a third party working at its place of work e.g. a factory or construction site, incurs expenses in order to pay condolence money or provide goods to its own employees and those of the third party, these expenses will not be treated as entertainment expenses. However, if the company pays condolence money or provides goods to its employees only, these expenses will be treated as entertainment expenses.



**Consumption tax**



Consumption Tax is a multi-step, broad-based tax on most transactions in assets and services in Japan and the receipt of foreign goods from bonded areas in Japan. The tax is assessed at each state of the manufacturing, wholesale, and retail processes. Deductions for consumption taxes paid at previous stages by businesses result in the consumer bearing the full burden of Consumption Tax.

## Consumption Tax rate

From October 1, 2019, the consumption tax rate increased from 8% to 10%. A reduced rate of 8% applies to food and beverages (except for dining out and alcoholic beverages) and newspapers issued twice weekly or more under a periodical subscription.

Where food and other items are provided together, the reduced tax rate is applicable to the entire amount if the amount of food and beverages represents more than 2/3 of the amount and the total amount is JPY 10,000 or less.

## Taxpayers

For the purposes of Consumption Tax, taxpayers are either (i) an enterprise, including both sole proprietorships and corporations, which transfers assets or provides services in Japan, or (ii) an enterprise or any person who removes foreign goods from a bonded area.

The threshold for mandatory payment of consumption tax is having taxable sales of more than JPY10 million during the base period (the fiscal year two years prior to the current fiscal year) and in the first 6 months of the previous fiscal year.

It is not necessary for a taxpayer to have a residence or domicile in Japan in order to be subject to Consumption Tax. In this case, a taxpayer who has no residence or domicile in Japan needs to appoint a Tax Agent in Japan to prepare the taxpayer's filing obligations.

## Exempt enterprises

An exemption from the obligation to pay Consumption Tax is available for small businesses whose taxable sales are not more than JPY10 million during the base period and in the first 6 months of the previous fiscal year.

## Election to be a taxable enterprise

An exempt enterprise may elect to be a taxable enterprise by submitting a notification to the District Director of the Tax Office with jurisdiction over their place for tax payment. In principal, the notification must be submitted by the day proceeding the first day of the Taxable Period for which a business intends to elect to be a taxable enterprise.

The election may be revoked upon notice to the tax office, but the notice of revocation may not be filed before the beginning of the second tax period following the period of the election.

## Newly established

A newly established sole proprietorship without a base period, or with sales less than JPY10 million during first 6 months of the previous year or the base period is exempt from Consumption Tax for its first two years.

Newly established corporations without a base period, or with sales less than JPY10 million during first 6 months of the previous year or the base period may be exempt only if their capital is less than JPY10 million at the start of their first two fiscal years. However, a new company may choose to file a consumption tax return as mentioned above if it anticipates a refund.

## Tax periods

For sole proprietorships, the consumption tax period is the calendar year. For corporations, the tax period is the company's fiscal year for corporate tax purposes.

## Special tax periods

Enterprises may elect to use special tax periods of three months/one month if the tax office is notified. The notification must be submitted by the day preceding the first day of the applicable taxable period.

An enterprise may discontinue the use of special tax periods upon notification to the tax office. However, the notification to discontinue use may not be filed within two years of the notification to use the special tax periods.

## Taxable transactions

The scope of Consumption Tax includes (i) the transfer (either by sale or lease) of assets or the provision of services in Japan by an enterprise in return for payment, and (ii) the removal of foreign goods upon their release from a bonded area.

## Non-taxable transactions

Transfers of certain designated types of assets and services are non-taxable either because the asset is not of the type contemplated for Consumption Tax or for reasons based on social policy concerns.

- Sales and leases of land and rights to land
- Transfers of securities
- Financial transactions
- Sales of postage stamps and document stamps
- Merchandise and service cards
- Government fees
- International money orders and foreign exchange
- Medical services
- Nursing care services
- Social welfare services

## Exempt Transactions

Consumption Tax is based on the principle of taxing assets and services in the place where they are consumed. Exemptions therefore are provided for assets for export and international communications and transport activities. Records need to be kept, such as export authorizations, in order to apply for the export exemption. Examples of exempt transactions include:

- International transportation of passengers, freight, and international communications, including shipment and communication occurring in Japan
- Transfer of intellectual property to non-residents
- Most services for non-residents, excluding (i) the transport or safekeeping of property in Japan, (ii) the provision of food or loading in Japan, or (iii) services provided in Japan which are similar to (i) and (ii).

# Taxation of cross-border electronic services

## Cross-border telecommunicated services

Books, music, advertising etc. distributed through telecommunication lines (collectively telecommunicated services) will be deemed to be provided in the location of the purchaser. This change came into force on October 1, 2015. Cross-border telecommunicated services provided by foreign enterprises fall into two categories, “B2B” transactions and “B2C” transactions.

B2B transactions are cross-border service transactions established through telecommunication lines such as internet or telephone lines where the recipients of the services are identified as enterprises with reference to the nature of service or trading terms etc. The recipients of B2B services from foreign enterprises will need to pay consumption tax on behalf of the foreign enterprises through a reverse charge mechanism.

B2C transactions are cross-border service transactions provided both inside and outside of the country through telecommunication lines such as internet or telephone lines, which do not fall under the definition of the B2B transaction. Foreign service providers providing B2C transactions are required to file a tax return and pay taxes in Japan.

### Treatment of providers of the service (Foreign enterprises etc.)

#### A) Recognition as taxable sales

Foreign enterprises which provide cross-border telecommunicated services will need to issue an invoice showing consumption tax added to the service price. If the invoice does not include the consumption tax separately, the price will be deemed tax inclusive thus reducing the net receipt to the enterprise. Foreign enterprises engaging in B2C transactions will be required to file a consumption tax return and pay consumption tax to the government.

#### B) Duty of notification

Foreign enterprises engaging in B2B transactions will need to make it clear to domestic enterprises (recipients of the service) that the purchase of the services is subject to consumption tax.

#### C) Registration of the ‘Foreign enterprises’

In the case of B2C transactions, the recipients will not be allowed to take a credit for the consumption tax on the transactions unless the foreign enterprises are registered. If this is the case, the services are categorized as B2C transactions from a registered foreign enterprise and the recipients will be able to take a credit for the consumption tax paid under certain conditions. According to the national tax authorities, the name of registered foreign enterprises will be published on the internet.

### Treatment of recipients of B2B services (Domestic enterprises etc.)

#### A) Reverse charge mechanism

The recipients of B2B services from foreign enterprises will need to pay consumption tax on behalf of the foreign enterprises through a reverse charge mechanism.

Under the reverse charge mechanism, recipients of the services will be required to report a “reverse charge” output tax in their consumption tax return. For most enterprises this output tax will be equal to the input tax paid by the enterprise for the service provided if it is related to business expenses.

#### B) Exception

If the proportion of taxable sales of the recipients of the services is 95% or more, the purchase of the telecommunicated services is ignored for the time being. This means that the recipients of the service do not need to recognize both consumption tax received and suspense consumption tax paid.

Regardless of whether the proportion of taxable sales is more than 95% or not, the transactions which are subject to reverse charge mechanism affect the recipient’s consumption tax return filing. Therefore we recommend classifying these transactions separately from other transactions when they are booked.

## Credit for taxable purchases

Because the Japan Consumption Tax is a multi-step tax assessed at all levels of the commercial process, a system is needed to prevent imposition of multiple layers of tax summing to more than the tax based on the price charged to the final consumer. Consumption tax can be reduced by deducting taxes on purchases against taxes on sales. The taxpayer files a tax return at the time specified above with the consumption tax reduced to reflect the refund received for taxable purchases.

## Simplified System

A simplified method of calculating the amount of Consumption Tax on taxable purchases is provided to relieve small businesses from administrative burden. If a taxpayer has taxable sales of JPY50,000,000 or less during its base period, the taxpayer may elect to use the simplified system to calculate the amount of creditable Consumption Tax by submitting a notification to the authorities.

Under this simplified system, the cost of purchases is estimated as a percentage of the sales price using a “deemed purchase ratio” which varies depending on the type of enterprise.

Type of business		Deemed purchase ratio (%)
Type 1	Wholesalers	90
Type 2	Retailers	80
Type 3	Farming, forestry, fishing, mining, construction, manufacturing( including manufactures who sell manufactured inventory to retailers), electricity, gas, heat or water suppliers	70
Type 4	All business other than Type 1, 2, 3 and 5(e.g. restaurant industry )	60
Type 5	Transportation and communication, service industry, finance and insurance companies (except the restaurant industry)	50
Type 6	Real estate	40

Once the taxpayer elects to use the simplified method, it cannot use the regular method for the two following years.

## Overseas Businesses Importing goods

Imported goods are taxed when they are released from a bonded area. The tax base on imported goods is the sum of the Cost, Insurance and Freight (CIF) price, custom duties and excise taxes. The taxpayer who withdraws foreign goods from a bonded area must pay the consumption tax before being able to receive those goods.

## Consumption Tax returns

The final Consumption Tax return and associated payment are generally due two months after the end of the tax period. However, for sole proprietorships the due date is the end of March of the following year. If a company files an application to extend the due date of their final corporation tax return, they can, however, also submit an application for a filing extension of their consumption tax return, which would then allow them to submit both returns one month later. This applies to tax periods ending on or after March 31, 2021.

## Interim Consumption Tax payments

Depending on the amount of consumption tax in the prior period return, interim consumption tax return(s) and payment(s) may apply to the taxpayer. Interim return(s) and payment(s) are generally due two months following the end of applicable interim period.

Final Consumption Tax for the prior tax period	Interim tax payments due
Over JPY48,000,000	11 interim (monthly) payments due each equal to 1/12 of the prior period consumption tax liability
Over JPY4,000,000 but less than JPY48,000,000	3 interim payments each equal to 1/4 of the prior period consumption tax liability
Over JPY480,000 but less than JPY4,000,000	1 interim payment equal to 1/2 of the prior period consumption tax liability
JPY480,000 or less	N/A

## Refund of excess tax on purchases

If the amount of Consumption tax on taxable purchases exceeds the Consumption tax on the tax base, the excess tax is refundable to the tax payer. To receive the refund, the tax payer needs to file the consumption tax return within two months after the end of the tax period (three months in case the request for extension has been filed and granted).



# Individual taxation

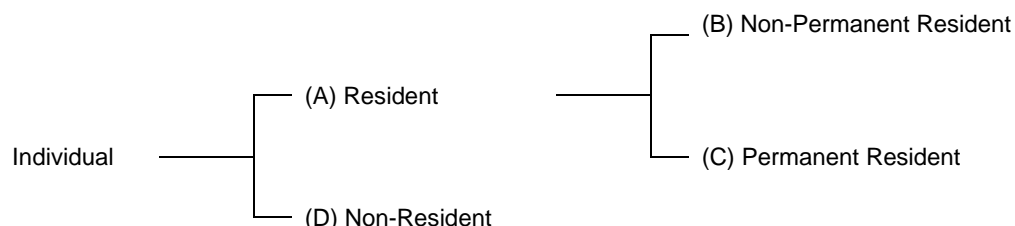
There are two levels of direct income taxes for individuals in Japan – national income tax (hereinafter referred to as “income tax”) and local inhabitant income tax (hereinafter referred to as “inhabitant tax”).

Income tax is a direct tax on the income of individuals during a calendar year and is assessed by the National Tax Office. How an individual is assessed income tax will depend on their residency status, source of income and nature of income among other factors.

Inhabitant tax is also a direct tax on the income of individuals during a calendar year but is assessed by municipal governments on individuals who reside or have domicile in Japan as of 1 January of the following year.

## Residency status

As in many countries, an individual's exposure to Japanese income tax is based on that individual's residency status. An individual for Japanese income tax purposes is categorized as either a (A) resident or (D) non-resident of Japan. A resident is further classified as either a (B) non-permanent resident or (C) permanent resident.



### (A) Resident

A resident is an individual (1) whose domicile is in Japan, (2) who has resided in Japan continuously for one year or more or (3) who is in Japan with the intention to stay for more than one year.

Under administrative rulings, there is a general presumption that an individual in Japan has a domicile in Japan if the following conditions are met.

- Has employment in Japan that normally require presence in Japan for a period of 12 months or more
- Holds Japanese nationality, maintains dependents in Japan and has sufficient employment and economic ties to Japan as would be expected for an individual with a Japanese domicile

A resident is further classified into (B) a non-permanent resident and (C) a permanent resident.

### (B) Non-Permanent Resident

A non-permanent resident of Japan is a resident individual who does not have Japanese citizenship and who has maintained a domicile or has resided in Japan for 5 years or fewer during the preceding 10 years.

Until December 31, 2016 non-permanent residents were subject to Japanese income tax and inhabitant tax on their (1) Japan source income regardless of where it is paid, (2) foreign source income paid in Japan and (3) foreign source income not paid in Japan but remitted to or effectively remitted to Japan.

Under new domestic rules effective January 1, 2017, non-permanent residents are taxed on all income except foreign source income that is not paid in, remitted, or effectively remitted to Japan. Effective April 1, 2017, capital gains arising from the sale of foreign publicly traded securities acquired by non-permanent residents post April 1, 2017 will be included in taxable income. Capital gains arising from the sales of foreign publicly traded securities acquired by a non-permanent resident prior to March 31, 2017 will also be included in taxable income if sold between January 1 and March 31, 2017.

A permanent resident of Japan is a resident other than a non-permanent resident - any individual who is either a Japanese national or a foreign national who has maintained a domicile or has resided in Japan for more than 5 years during the preceding 10 years - is treated as a permanent resident.

A permanent resident is subject to Japanese income tax and inhabitant tax on their worldwide income.

It is important for expatriates who have been on more than one assignment to Japan, even for different employers, to check when they become a permanent resident due to the ten-year look back rule.

#### (D) Non-Resident

A non-resident of Japan is an individual other than a resident – any individual who has not had a domicile in Japan or has not resided in Japan for a continuous period of 1 year or more.

A non-resident is generally subject to Japanese income tax and inhabitant tax only on their Japan source income at a flat rate of 20.42% on a gross basis. Generally, no deductions are available.

An expatriate on assignment to Japan will become a non-resident from the day following their permanent departure from Japan.

## Domicile

The term “address” is defined by the Japanese Civil Code as the individual's principal place of abode. Whether or not an individual has his or her address in Japan is determined on objective facts such as the individual's employment, household or place of business in Japan. In view of the nature of an address, an individual can never be treated as having more than one address at the same moment.

In general, if an individual, regardless of nationality, has taken residence in Japan to engage in a trade, business or employment, the individual is presumed to have an address in Japan unless contrary evidences direct otherwise - that the period of the individual's stay in Japan is not 1 year or more. Type or length of visa under which a foreign national has been permitted to enter Japan is not directly relevant.

## Source Income

The definition of Japan source income has been amended effective 1 January 2017 as follows:

- Where a non-resident person conducts business through a permanent establishment, income attributable to a permanent establishment through which a non-resident individual conducts business. Income attribution is determined based on functions, assets used, dealings between the permanent establishment and non-resident's place of businesses and other factors of the permanent establishment on the basis that the permanent establishment operates independently from the non-resident.
- Income from the management or holding of assets located in Japan;
- Income from the sale of assets located in Japan;
- Distribution of profit from business in Japan under certain partnership agreement where such business is conducted through a permanent establishment in Japan;
- Consideration received from the sale of land, any right on land, building, etc. located in Japan;
- Consideration received by persons engaging in businesses whose primary purpose is the provision of personal services within Japan;
- Consideration received for the leasing of real estate located in Japan, any right on real estate located in Japan or a right of certain quarrying, the establishment of a certain mining lease or the leasing of a vessel or aircraft to a resident or domestic corporation;
- (1 ) Interest on Japanese national government bonds, Japanese local government bonds or bonds issued by a domestic corporation, (2) interest on bonds issued by a foreign corporation attributable to business conducted in Japan through its permanent establishment, (3) interest on savings deposited with branches and offices located in Japan, or (4) distribution of profit from a jointly managed money trust, bond investment trust or publicly offered bond investment trust managed by an office located in Japan.



- (1) Certain dividend of retained earnings from a domestic corporation, dividend of profit, distribution of retained earnings, distribution of cash or interest on funds or (2) distribution of earnings from an investment trust or a specified trust issuing a beneficiary certificate managed by an office located in Japan;
- Interest on a loan made to a person conducting business in Japan and attributable to such business;
- Royalties or considerations received from a person conducting business in Japan attributable to such business including (1) royalty for or consideration received for the transfer of industrial property right or any other right concerning technology, a production method involving special technology or any other equivalent right or method, (2) royalty for or consideration received for the transfer of a copyright (including right of publication, neighbouring right and any other equivalent right) or (3) royalty for machinery, equipment or other certain tools;
- Salary, compensation and pension including (1) remuneration, salary, wage, annual allowance, bonus and any other payment or remuneration similar in nature as being compensation for provision of personal services corresponding to those performed in Japan, (2) certain public pensions or (3) certain retirement allowances arising from work or provision of personal services performed by an entitled person while such person was a resident of Japan;
- Certain awards for advertisement of a business conducted in Japan;
- Certain pension received under a contract for life insurance, casualty insurance or any other annuity contract entered into with a business office located or through a person acting as a contracting agent in Japan;
- Monetary compensation, interest, profit or margin gain attributable to business office located in Japan;
- Distribution of earnings received under certain silent partnership contract with respect to capital contributions to a person conducting business in Japan;
- Certain other income sourced in Japan.

## Short-Term Visitors

Under tax treaties between Japan and various other countries, a non-resident individual visiting Japan on a short-term basis may be exempt from Japan income tax on compensation from employment. While the provisions in each tax treaty are not identical, the following conditions are typical of the requirements which need to be satisfied:

- The individual is in Japan for not more than 183 days in any twelve-month period commencing or ending in the fiscal year concerned;
- The individual's compensation is paid by a non-resident employer; and
- Compensation paid to the individual is not charged to or otherwise treated as a deductible expense by a permanent establishment in Japan.

## Assessable Income

An individual's taxable income is defined as assessable income less allowable deductions. Japan's tax codes provide the following ten categories of assessable income:

- interest income
- dividend income
- real estate income
- business income
- employment income
- retirement income
- forestry income
- capital gains
- occasional income
- miscellaneous income

Typically, the most important element when considering tax positions of an expatriate on assignment to Japan is employment income. Employment income includes salaries and wages, commissions and bonuses, shares and options received in respect of employment, benefits in kind and various allowances received in exchange for services rendered. Commonly included allowances include, but not limited, to the follows:

- cost of living allowance (COLA)
- housing allowance
- allowance related to tax equalization
- utility allowance
- allowance for language lessons
- children's tuition allowance
- medical allowance
- home leave allowance
- commuter allowance
- stock options and other stock-based compensation

An expatriate may continue to be covered by pension and/or profit sharing plans maintained by the head offices, where the head office will continue to make contributions to the expatriate's individual account even while on assignment to Japan. These types of benefits are generally treated as assessable income for Japanese tax purposes.

## Benefits in kind

Assessable income from employment is not limited to employment income but also include payments in kind and economic benefits unless specifically exempted from tax under tax codes, regulations and administrative rulings. Below are Japanese tax implications of some of the popular benefits in kind offered to expatriates on assignment to Japan.

### (a) Company provided housing

Rent paid by the employer to the landlord for housing leased under the company name and made available to an employee is included in assessable employment income. Under certain conditions, however, rent paid by an employer to a landlord may be excluded from employment income.

"Legal rent," as it is often referred to, is an arrangement whereby if an employee incurs at least the basic rent each month, rent paid by an employer for an employee may be excluded from employment income. Basic rent is calculated as the total of the following three computations.

- (i) 2% of the basis of the building for the purposes of Fixed Assets Tax
- (ii) JPY 12 x (total floor space of the building in square meters / 3.3 square meters)
- (iii) Taxable basis of the ground site of the building for the purposes of Fixed Assets Tax x 0.22%

For simplicity purposes, however, many employers use a range between 5 to 10 percent of the actual monthly rent to be incurred by an employee as the result of the above calculations generally falling within this range. For an officer, at least 50 percent of the actual monthly rent needs to be incurred unless the premise is used partly for business purposes, in which case the amount may be reduced to 35 percent of the actual monthly rent.

### (b) Children's tuition allowance

Children's school tuition paid by an employer is generally included in assessable employment income.

If the employer, however, makes a donation to an international school under an eligible scholarship plan and in recognition of such donation, children of employees of that employer are exempted tuition payments for attending the school, an employee may not be taxed on such tuition-free benefits made available by the donation.

### (c) Moving expenses

Reasonable moving expenses are not included in assessable income provided they are in nature reimbursement of necessary business costs to relocate an employee on international assignment.

(d) Home leave transportation

Reimbursement provided to an employee on international assignment for the purpose of temporarily visiting his or her home country once a year is typically not included in assessable income, subject to certain conditions.

(e) Tax reimbursements

Tax payments made by an employer on behalf of an employee to cover that employee's personal tax liabilities are included in assessable employment income to the employee. Under gross-up tax arrangements, where incremental increase in tax liabilities occur as a result of the tax-on-tax effect of paying taxes of an employee, assessable income will increase dramatically.

It is important to take into account the effect of inhabitant tax for its deferred tax assessment timing. Incomplete gross-up tax arrangements will often result in an expatriate's assessable income and employer's salaries and wages expenses to snowball to an astonishing sum.

(f) Stock options

An employee on international assignment to a Japanese subsidiary or branch may often receive stock based compensation such as stock options of its foreign parent company or head office during their assignment in Japan. Tax treatment of stock options will generally depend on whether the options are qualified or non-qualified. Foreign stocks are non-qualified stock options.

Generally, there are no withholding requirements on such earnings but the individual is required to declare the income on his/her individual income tax return. Japanese subsidiary or branch of foreign parent companies are required to report the details of all stock compensation recognized by employees during the calendar year by March 31 the following year.

When a foreign parent company or head office provides equity compensation to directors and employees of the Japanese subsidiary or branch and such persons recognize economic benefits through exercise, vesting, etc. of such equity compensation, the Japanese subsidiary or branch is required to prepare and file an informational return to disclose details of the benefits recognized by directors and employees. The scope of individuals who receive economic benefits subject to this reporting requirement has been expanded to include non-resident individuals and terminated directors and employees of the Japanese subsidiary or branch who received equity compensation.

(i) Qualified stock options

Qualified stock options are subject to Japanese income tax and inhabitant tax at the time the shares are sold. Capital gain equivalent to sales price less exercise price is taxed at a flat 20.42% separately from other types of income.

Stock options granted under the Japanese Company Law may be qualified if the following conditions are satisfied:

- Holder of the stock options is a director, officer or an employee of the issuing company or of a company whose voting stock is 50 percent or more owned directly or indirectly by the issuing company;
- Stock options are granted by resolution at a shareholders' meeting where vesting period of the stock option is 2 years or more and life of stock option 10 years or less after the date of such resolution, respectively;
- Exercise price of the option must equal to or be higher than the fair market value of the underlying shares on the date of grant;
- Total exercise price of all options exercised in a year must not exceed JPY12 million;
- Option rights cannot be transferred; and
- Issued share certificates must be kept in a trust and under custody of either a securities company or a trust company in accordance with a prearranged agreement made between the company and the trust company.

(ii) Non-Qualified Stock Options

Non-qualified stock options are subject to income tax and inhabitant tax upon both exercise and sale. At the time of exercise, the difference between the fair market value and the exercise price is taxed as employment income. Subsequently, upon sale of the share, the difference between sales price and fair market value at exercise is subject to capital gains tax.

## Exemptions and Concessions

There are a number of benefits granted to employees which may specifically be excluded from assessable income.

Commuter allowance provided by an employer may be excluded from assessable income up to the following limits:

- Train or bus expense – Allowances or tickets for use on trains or buses are tax free to an employee up to a maximum of JPY150,000 per month. The commute must be by the most direct and economical route.
- Use of personal vehicle – Allowances for use of personal automobile or motor bicycles are limited based on the one-way distance of the daily commute as follows:

Commuting distance	Monthly limit
Less than 2km	Fully taxable
2 km or more, but less than 10 km	JPY4,200
10 km or more, but less than 15 km	JPY7,100
15 km or more, but less than 25 km	JPY12,900
25 km or more, but less than 35 km	JPY18,700
35 km or more, but less than 45 km	JPY24,400
45 km or more, but less than 55 km	JPY28,000
55 km or more	JPY31,600

- Reasonable gifts or awards made to an officer or an employee in recognition of long-term service with the employer.
- Gifts awarded to directors or employees in connection with the commemoration of anniversaries, etc. where such goods are suitable for the occasion and the estimated disposal value does not exceed JPY10,000.
- Discount sales of merchandises where the sales price is 70 percent or more of the ordinary selling price and the quantity of the discounted goods sold to an employee is reasonable for use by the household of the officer or employee.
- Cost of recreation, such as outings, etc. up to a reasonable amount.
- Life insurance or casualty insurance premiums borne by the employer on behalf of directors and employees provided that the insurance proceeds are to be made to the employer upon expiration of the insurance term.
- Insurance premiums paid by the employer on behalf of the employee provided the amount borne by the employer does not exceed JPY3,000 a month.
- Compensation for damage paid to a third party and legal fees in connection therewith where such damage was caused by an officer or employee while on duty and not due to their fault.
- Golf club or social club membership fees, etc. provided that they are connected with the business of the employer.
- Dividends and capital gains from listed shares held in an individual's savings account, in which an individual can make investments in listed shares up to JPY 1,200,000 per year from 2014 to 2023 (with maximum tax exempt balance being JPY 6,000,000) and hold them for a maximum of 5 years. Junior

## Allowable Deductions

A number of deductions may be made from a resident taxpayer's assessed income.

### Standard deduction

- Employment income

Amount of compensation	Standard deduction
Up to JPY 1,625,000	JPY 550,000
JPY 1,625,000 – JPY 1,800,000	40% of compensation
JPY 1,800,000 – JPY 3,600,000	30% of compensation + JPY 80,000
JPY 3,600,000 – JPY 6,600,000	20% of compensation + JPY 540,000
JPY 6,600,000 – JPY 8,500,000	10% of compensation + JPY1,200,000
JPY 8,500,000 or more	JPY 2,200,000

- Retirement income

Circumstances	Standard deduction
Up to 20 years of service	JPY 400,000 per year of service
For each year of service over 20 years	JPY 700,000 per year of service
Minimum deduction	JPY 800,000
Special deduction for those retiring due to physical hardship	Amount of the above deduction + JPY 1,000,000

Taxable retirement income is calculated as 50% of retirement income after the standard deduction and taxed at the ordinary tax rate separately from ordinary income. The 50% reduction does not apply to retirement allowances for a director whose service period is 5 years or less.

### Specific Deductions

- Casualty losses. A deduction is available for losses from disaster or theft on taxpayer's assets or on those of family members living in the same household. The deductible amount is the greater of (1) the amount of loss not covered by insurance proceeds less 10% of assessable income or (2) the amount of expenditures related to such loss less JPY50,000. Unused losses may be carried forward for 3 years.
- Medical expenses. A deduction is available for medical expenses of the taxpayer and family members living in the same household. Deductible amount is equivalent to medical expenses not covered by insurance proceeds less the lesser of 5 percent of assessable income or JPY100,000. Deduction is capped at JPY2,000,000.

- Between January 1, 2017 and December 31, 2021, the “switch OCT medicine deduction” will be introduced as a special tax deduction to promote over-the-counter (OTC) medicine over prescribed medicine. Taxpayers who take specific self-health management steps, such as routine medical check-ups and prevention/immunization, will be eligible to deduct expenditures which exceed JPY 12,000, up to a limit of JPY 88,000, used to purchase specified “switch OCT medicine” not covered by insurance. Taxpayers who claim this deduction will not be able to claim the medical expense deduction.
- Social insurance premiums. A deduction is available for social insurance premiums withheld from an employee’s payroll or paid outside of payroll for an employee or family members living in the same household in accordance with Japanese social insurance programs.
- Life insurance premiums. Deduction is available for (1) life insurance premiums, (2) qualified contributions to private pension plans and (3) nursing care insurance premiums paid to Japanese insurance companies or to foreign insurance companies authorized by the Ministry of Finance. The deductible amounts for each are shown in the tables below. The combined maximum amount deductible is JPY120,000 for income tax and JPY70,000 for inhabitant tax.

(1) Life insurance premiums

Total premiums paid during the year	Amount deductible
Up to JPY 20,000	Full amount
Excess over JPY 20,000 Up to JPY 40,000	50% of premiums paid + JPY 10,000
Excess over JPY 40,000 Up to JPY 80,000	25% of premiums paid + JPY 20,000
Excess over JPY 80,000	JPY 40,000

Qualified contributions to private pension plans executed before 31 December 2011.

Total premiums paid during the year	Amount deductible
Up to JPY 25,000	Full amount
Excess over JPY 25,000 Up to JPY 50,000	50% of premiums paid + JPY 12,500
Excess over JPY 50,000 Up to JPY 100,000	25% of premiums paid + JPY 25,000
Excess over JPY 100,000	JPY 50,000

(1) Qualified contributions to private pension plans executed after 1 January 2012

Total premiums paid during the year	Amount deductible
Up to JPY 20,000	Full amount
Excess over JPY 20,000 Up to JPY 40,000	50% of premiums paid + JPY 10,000
Excess over JPY 40,000 Up to JPY 80,000	25% of premiums paid + JPY 20,000
Excess over JPY 80,000	JPY 40,000

Qualified contributions to private pension plans executed before 31 December 2011.

Total premiums paid during the year	Amount deductible
Up to JPY 25,000	Full amount
Excess over JPY 25,000 Up to JPY 50,000	50% of premiums paid + JPY 12,500
Excess over JPY 50,000 Up to JPY 100,000	25% of premiums paid + JPY 25,000
Excess over JPY 100,000	JPY 50,000

(3) Nursing care insurance premiums

Total premiums paid during the year	Amount deductible
Up to JPY 20,000	Full amount
Excess over JPY 20,000 Up to JPY 40,000	50% of premiums paid + JPY 10,000
Excess over JPY 40,000 Up to JPY 80,000	25% of premiums paid + JPY 20,000
Excess over JPY 80,000	JPY 40,000

- Earthquake insurance premiums. A deduction is available for (1) earthquake insurance premiums and/or (2) certain long-term casualty insurance premiums paid to Japanese insurance companies or foreign insurance companies authorized by the Ministry of Finance. The deductible amounts for each are shown in the tables below. The combined maximum amount deductible is JPY50,000 for income tax and JPY25,000 for inhabitant tax.

(1) Earthquake insurance premiums

Total premiums paid during the year	Amount deductible
Up to JPY 50,000	Full amount
Excess over JPY 50,000	JPY 50,000

(2) Certain long-term casualty insurance premiums

Total premiums paid during the year	Amount deductible
Up to JPY 10,000	Full amount
Excess over JPY 10,000 Up to JPY 20,000	50% of premiums paid + JPY5,000
Excess over JPY 20,000	JPY15,000

- Charitable contributions. Deduction is available for qualified charitable contributions in excess of JPY2,000 made each year. To qualify, contributions must be made to the Japanese government, municipalities or designated non-profit organizations.

The deductible amount is the lesser of 40% of the taxpayer's total income or the amount contributed less JPY2,000.

For inhabitant tax purposes, a deduction is available for contributions made to prefectural community chest of the Japan Red Cross. The deductible amount is the lesser of 30% of the taxpayer's total income or the amount contributed less JPY5,000.

## Personal and dependent exemptions

- A resident taxpayer may claim exemptions for the taxpayer's self and qualified dependents as shown below. Children aged 15 and under cannot be claimed as a dependent, however, may be eligible for disability exemption. Furthermore, beginning 2023, dependents aged between 30 and 69, who are currently living overseas, can also not be claimed as dependents, unless they are studying abroad and have therefore become a non-resident in Japan, they have a disability or they receive an allowance from the taxpayer during the applicable tax year of JPY380,000 or more. In all of these cases, supporting documents must be submitted as proof.
- <https://www2.deloitte.com/jp/en/pages/tax/articles/bt/japan-inbound-tax-legal-december-2019-no49.html> p.15 7)

Effective January 1, 2016, taxpayers with dependent family members who are non-residents of Japan are required to submit documents to prove verification of family and remittances in order to claim dependent deduction, spouse deduction, special spouse deduction or disability deduction.



A non-resident taxpayer is only entitled to the basic deduction.

Exemption	Amount deductible for income tax	Amount deductible for inhabitant tax
Basic deduction for taxpayer	JPY380,000	JPY330,000
Spouse under age 70	JPY380,000	JPY330,000
Spouse age 70 or older	JPY480,000	JPY380,000
Dependent age 16-18	JPY380,000	JPY330,000
Dependent age 19-22	JPY630,000	JPY450,000
Dependent age 23-69	JPY380,000	JPY330,000
Dependent age 70 or older and living with taxpayer	JPY580,000	JPY450,000
Dependent age 70 or older and not living with taxpayer	JPY480,000	JPY380,000

Additional exemptions are available for spouse and dependents under certain cases as follows.

Additional exemption	Amount deductible for income tax	Amount deductible for inhabitant tax
Dependent with physical handicap	JPY270,000	JPY260,000
Dependent with severe physical handicap	JPY400,000	JPY300,000
Dependent with severe physically handicapped living with taxpayer	JPY750,000	JPY530,000
Widow (or widower), divorcee, never-married single parent or working student	JPY270,000	JPY260,000

<https://www.eytax.jp/tax-library/newsletters-en/pdf/japan-tax-alert-18-dec-2019-01-en.pdf> p.3 1)

## Tax Credits

The following tax credits can, where applicable, be claimed by a resident taxpayer filing a final tax return. A non-resident taxpayer subject to progressive tax rates is also entitled to credits for withholding income tax and donations.

### Dividends received credit

This credit is applicable to domestic dividend receipts only. While the amount of the credit is generally calculated as follows, complex tax credit arrangements are also available for certain other types of distributions.

A taxpayer electing to not report dividends received from Japanese public companies and instead suffer final withholding cannot claim the dividend received credit.

Taxpayer's total income	Type	Income tax	Inhabitant tax
Up to JPY10,000,000	Dividends from shares	10%	2.8%
	Distribution from stock investment trusts	5%	1.4%
Over JPY10,000,000	Dividends from shares	5%	1.4%
	Distribution from stock investment trusts	2.5%	0.7%

### Credit for withholding income tax

Income tax withheld from employment income, from dividends not subject to separate taxation and from other income reportable in a final return is creditable against income tax due on the final tax return. Special reconstruction income tax imposed on such withholding tax is also creditable against special reconstruction income tax due on the final tax return.

### Foreign tax credit

A foreign tax credit is designed to provide relief where a taxpayer is taxed twice on the same income within Japan and outside of Japan. To be eligible for a credit, taxpayer must have foreign source income.

The foreign tax credit is equal to the lesser of:

- The amount of foreign tax paid during the taxable year, or
- The amount of foreign tax credit limitation computed as follows

$(\text{Japanese income tax for the year}) \times (\text{Foreign source income for the year} / \text{Total income taxable in Japan for the year})$

If the amount of foreign taxes paid during the taxable year exceeds the amount of the credit limitation, the excess may be carried forward three years.

### Credit for donations

- Income tax

If a taxpayer pays donations to the following organizations, the taxpayer may elect to claim a tax credit instead of taking an income deduction.

Creditable amount = (a) + (b)	
(a) Tax credit for donations to political parties (the lesser of (i) or (ii))	(i) (Donations to political parties – JPY2,000) x 30%
	(ii) Income tax before tax credits x 25%
(b) Tax credit for donations to authorized NPOs and public interest entities (the lesser of (iii) or (iv))	(iii) Total of the following: - (Donations to designated NPOs – JPY2,000) x 40% - (Donations to certain public interest entities – JPY2,000) x 40%
	(iv) Income tax before tax credit x 25%

In principle, the total of the creditable donations and deductible donations is subject to a ceiling of 40% of total assessable income.

– Inhabitant tax

For inhabitant tax purposes, the following tax credits are available:

<b>Creditable amount = (a) + (b)</b>	
(a) Basic tax credit	(Total amount of eligible donations – JPY2,000) x 10%
(b) Additional tax credit (the lesser of (i) or (ii))	(i) (Total amount of donations to local governments – JPY2,000) x (90% - marginal income tax rate for the individual x 102.1%)
	(ii) Inhabitant tax before tax credits x 10%

## Tax rate

### Income tax

Taxable Income	Tax Rate	Standard Deduction
Up to JPY1,950,000	5.105%	JPY 0
JPY1,950,000 - JPY3,300,000	10.210%	JPY99,548
JPY3,300,000 - JPY6,950,000	20.420%	JPY436,478
JPY6,950,000 - JPY9,000,000	23.483%	JPY649,356
JPY9,000,000 - JPY18,000,000	33.693%	JPY1,568,256
JPY18,000,000 - JPY40,000,000	40.840%	JPY2,854,716
JPY40,000,000 or more	45.95%	JPY4,896,716

### Inhabitant tax

Taxable Income	Tax Rate	Standard Deduction
Flat rate	10%	0

# Filing tax returns and making tax payments

## Income tax return and tax payments

The tax year for individuals is the calendar year and a final income tax return must be filed by 15 March of the following year or the next business day if 15 March falls on a weekend or a holiday. Extensions of the filing deadline are not available in Japan unless granted by the National Tax Office in regions affected by natural disasters and other events. Final tax due need to be paid by the same day which may be extended for approximately one month if automatic bank transfer system is elected. Credit cards will be accepted for national tax payments made from 4 January 2017 and the credit card transaction date will be considered as the tax payment date.

If remuneration subject to withholding tax (paid within in Japan and not offshore) is less than JPY20 million and the amount of other income is less than JPY200,000, filing of an income tax return is not required since tax liabilities are settled through year-end adjustment of income tax on salaries and wages made by the employer and other income is deemed insignificant. If such individual has claimable deductions such as casualty losses, medical expenses and donations not deductible through year-end adjustment, a final tax return may be filed to declare such deductions.

## Estimated tax payments

An individual having filed a tax return in the previous year will be required to make estimated tax payments for the current year in July and November if the final tax payment on the previous year's tax return was more than JPY150,000. Estimated tax payments are generally equal to one-third of the net of income tax less withholding tax on the previous year's tax return.

## Inhabitant tax return and tax payments

An inhabitant tax return is generally not required to be filed since information necessary for assessment of inhabitant tax is either submitted by employers or included in income tax return filed with the National Tax Office.

If remuneration is paid through an employer in Japan, inhabitant tax on such income is paid to municipal tax office by the employer through monthly payroll. Inhabitant tax on other income, including remuneration paid outside of Japan in the previous year, is generally paid directly by the taxpayer in four instalments – on or before June 30, August 31 and October 31 of the current year and January 31 of the following year.

# Assets and liabilities reporting

Effective 1 January 2016, taxpayers filing a tax return reporting total income in excess of JPY 20 million and whose total value of assets as of the end of the calendar year is JPY 300 million or more or total value of eligible assets for exit tax purposes as of the end of the calendar year is JPY 100 million more must file a "Assets/Liabilities Report" together with their tax return to disclose details of assets and liabilities as of the end of the calendar year.

# Overseas asset reporting

Permanent residents with overseas assets valued at over JPY50 million as of the end of a calendar year must submit a "Overseas Assets Report" to disclose their overseas assets by 15 March of the following year. Appropriate disclosure of overseas assets may result in reduced penalties when understatements of tax are found in a tax audit whereas improper disclosure may result in additional penalties.

# Exit tax regime

In an effort by the Japanese government to prevent individuals from escaping tax by moving out of Japan, an exit tax regime to impose income tax on unrealized capital gains on financial assets at the time of departure has been introduced and became applicable from 1 July 2015.

In order to eliminate the potential for double-taxation previously created by the exit tax, effective from tax year 2016, stock options and other similar rights, where all or a portion of the income from exercising the right is considered as Japan source income, will be excluded from the scope of the exit tax.

Excess capital losses from listed securities due to the exit tax can be carried forward for up to three years.

Exit tax is applicable to a resident individual terminating domicile or residency in Japan and who satisfies the following conditions:

- Total value of financial assets is JPY100 million or more.
- Resident individual has lived in Japan for more than 5 years within the last 10 years before terminating domicile or residency.

For the purpose of the 5 out of 10 years test above, the period of stay in Japan with a residency status of working visas such as intra-company transferee and specialist in humanities and international services will be excluded. The period of stay in Japan with a residency status of personal status visas such as permanent resident and spouse or children of Japanese national will be included, however due to transitional measures, will not be subject to the exit tax until 1 July 2020.

Exit tax will not apply to foreign expatriate employees staying in Japan with working visas such as intra-company transferee or engineer/specialist in humanities/international services.

## Compensation structuring for expatriates

An expatriate coming to Japan on assignment will generally enter Japan as a non-permanent resident for Japanese tax purposes, unless they have resided in Japan for at least five years in the preceding 10 years. Non-permanent residents are liable for Japanese income tax and inhabitant tax only on Japan source income plus any foreign source income deemed to be paid in Japan or remitted to Japan.

Where payroll is paid overseas, the portion of the expatriate's employment income corresponding to the number of days spent outside of Japan on business during the year may be treated as non-Japan source income. Such income will not be taxable in Japan, provided no part of the relevant amount is remitted to Japan. For these purposes, remittance includes drawings from the offices in Japan of an employer company, foreign currency brought into Japan, borrowings in Japan to be repaid outside Japan, etc. An overseas compensation package may therefore offer a tax-planning opportunity particularly for expatriates with business travel outside of Japan. Salaries and wages paid to a non-permanent resident within Japan are taxable in Japan regardless of where the activities are performed.

Where an overseas payroll arrangement is utilized, it is necessary for the relevant employee to maintain a record of remittances made to Japan.

This benefit is available for an expatriate employee with a non-permanent resident status in Japan. If an expatriate employee has resided in Japan for more than 5 years in the last 10 years, the expatriate employee will become a permanent resident for tax purposes and will be taxed in Japan on worldwide income.

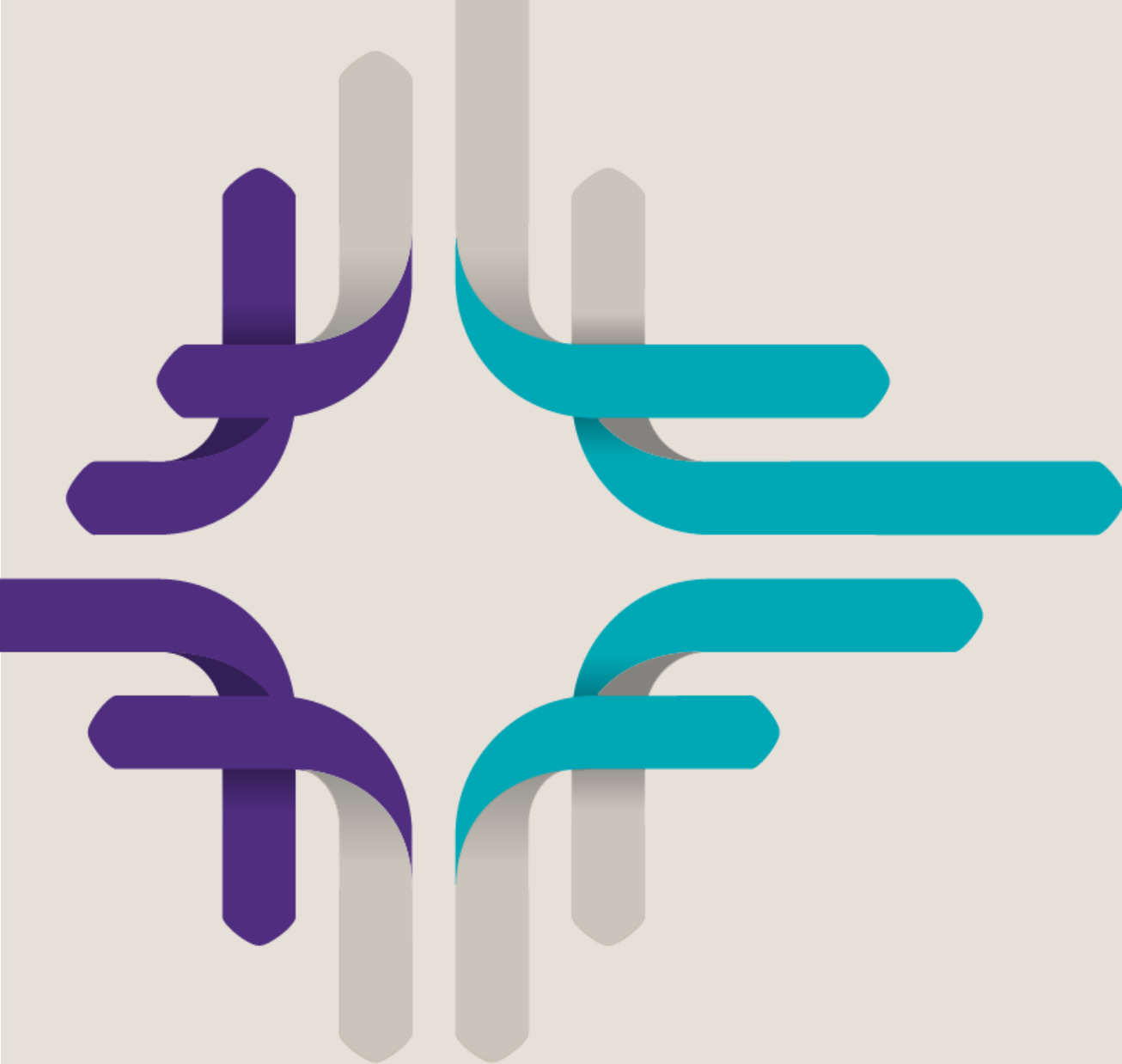
## Special Tax Treatment regarding COVID-19

In the case that the construction, acquisition or reconstruction of residential houses, which have been financed using a housing loan, has to be delayed due to the effects of COVID-19 and the houses therefore cannot be occupied before the end of December 2020, affected taxpayers are eligible for a deduction on the housing loan with an extended deduction period of 13 years in their income tax for 2021 and the years after if the following requirements are met:

- (1) Due to the effects of COVID-19, the new residential houses cannot be occupied by the time they were originally supposed to.
- (2) The date of completion as stipulated in the contract must be before the end of September 2020 (in the case of new construction) or before the end of November 2020 (in the case of acquisition or reconstruction of residential houses).
- (3) The buildings mentioned in (2) must be occupied by the end of December 2021.

Even if more than six months have passed since the date of the acquisition of a pre-owned residential house that was acquired using a housing loan, taxpayers can still take a deduction on the housing loan in their income tax for 2021 and the years after if the following requirements are met:

- (1) Due to the effects of COVID-19, pre-owned houses, for which extension or reconstruction was carried out after acquisition, cannot be occupied by the time they were supposed to.
- (2) Contracts for extension and renovation of the houses mentioned in (1) are set in place within five months after the date of acquisition of those houses or two months after the date of enforcement of the Special Law.
- (3) The applicant must occupy the dwelling within six months after the completion of the extension and renovation.



**Social Security**

The underlying concept of Japan's social security may have been most eloquently expressed by the Advisory Committee on Social Security, an advisory council to the prime minister, in 1949.

“Measures shall be taken to open the way to extend economic protection to such cases as those which were caused by sickness, injury, childbirth, death, aging, unemployment, many family children, and other causes of destitution either through the means of insurance or the direct means based on public expense. National treasury assistance shall guarantee those who are in destitute the minimum standards of living, while attempts shall be made to improve public health and social welfare so that all Japanese citizens are able to have a life worthy of being members of a civilized society.”

The spirit still holds true even after more than half a century except that the benefits of improved public health and social welfare today are extended to non-Japanese citizens and all residents of Japan irrespective of nationality are valuable members and foundation of this civilized society.

The key features of Japan's social security are (1) the system targets risks that cause social instability and require involvement of the entire public; (2) it is based on the principle of compulsory participation; and (3) insurers that manage the programs are the Japanese government, local municipalities and public or quasi-public agencies or organizations. Most of Japan's social security programs are managed not only by contributions in the form of insurance premiums but also by public funds and taxes.

With few exceptions, therefore, all residents of Japan regardless of nationality are obliged to participate in the nation's social security programs. There are six frameworks of social security programs for employees in Japan categorized into “Social Insurance” (Health Insurance, Nursing Care Insurance, Welfare Pension Insurance and Childcare Allowance Contribution) and “Labour Insurance” (Workers' Accident Compensation Insurance and Employment Insurance).

## Health Insurance

All residents of Japan, regardless of nationality, participate in one of a variety of public health care insurance and are issued credit card sized health insurance certificate cards.

The type corporate employees participate is often referred to as Employees' Health Insurance or simply Health Insurance and is managed and operated either by the Japanese government or by health insurance associations formed by large corporations and their group companies or by a group of separate companies within the same or similar industry or sector. Registration with Health Insurance is administered by the employer usually by their human resource department or outsourced service provider.

Often times, however, employees on international assignment to Japan or their employers do not recognize the benefit of registering in Health Insurance because their dependent family members and themselves are covered by global private health insurance policies offered by their direct employer as part of their assignment or secondment package. Certain bilateral social security agreements such as those between Japan and the U.S. may, under such circumstance, offer exemptions from participating in Health Insurance. It should, however, be recognized that participation exemption under bilateral social security agreements are limited and in most cases employees on international assignment to Japan and their dependent family members do not escape participation requirements.

In the rare event employees on international assignment to Japan escape participation in Health Insurance not due to the application of bilateral social security agreement but due to the nature of their service performance in Japan and other specific facts and circumstances, they are required to participate in the National Health Insurance managed and operated by local municipalities with jurisdiction over the assignees' registered address for residency card purposes. National Health Insurance is a health insurance for non-employees and participants include workers in agriculture, forestry and fisheries industries along with shop owners, self-employed workers and those unemployed and their dependent family members. Registration with National Health Insurance requires the individual to complete necessary application forms at the national health insurance division within local municipal offices with jurisdiction over their registered address.

### Benefits

Health Insurance allows affordable medical and dental care, hospitalization, prescribed medicines and various other benefits to covered employees and their dependent family members for non-work related injuries and sickness. While these benefits in kind constitute the core of the system, there are also cash benefits that include sickness/injury allowances, maternity allowances and cost compensation for childbirth, funerals, and others.

#### Benefits in kind

Insured employees and their dependent family members are eligible to receive outpatient and inpatient medical and dental care at hospitals, clinics, dentists and other medical institutions at 30 percent of its full cost by presenting their health insurance card at service counters. Medical services for beauty and other purposes that do not serve to cure injuries or sicknesses are often not subject to reduced cost.

Sometimes insured employees and their dependent family members may undergo costly medical examinations or surgeries at the same medical institution within the same month or over time and find their medical bills even at 30 percent of full cost to be prohibitively expensive. Such high medical costs in excess of the following amounts predetermined based on income levels of the insured may be claimed back or are reimbursable.

- (1) Those with monthly standard remuneration of JPY830,000 and above: JPY252,600 + (medical costs – JPY842,000) x 1% or JPY140,100 in case of multiple eligibility
- (2) Those with monthly standard remuneration between JPY530,000 and JPY790,000: JPY167,400 + (medical costs – JPY558,000) x 1% or JPY93,000 in case of multiple eligibility
- (3) Those with monthly standard remuneration between JPY280,000 and JPY500,000: JPY80,100 + (medical costs – JPY267,000) x 1% or JPY44,400 in case of multiple eligibility
- (4) Those with monthly standard remuneration of less than JPY260,000: JPY57,600 or JPY44,400 in case of multiple eligibility
- (5) Those exempted from inhabitant tax: JPY35,400 or JPY24,600 in case of multiple eligibility

It is important to note that medical expenses claimed as a deduction on tax returns need to be reduced for the amounts claimed back or reimbursed through health insurance.

#### Cash benefits

Health Insurance also offers various cash benefits to covered employees and their dependent family members for non-work related injuries and sickness. Common cash benefits include the following:

- (1) Sickness/injury allowance is paid to insured employees to compensate lost wages, in whole or in part, during medical leave from work. Insured employees gain eligibility beginning the fourth day of leave from work to a year and half thereafter. Allowance is equivalent to two-thirds (approximately 66.67 percent) of daily standard remuneration for each day of unpaid or partial leave from work.
- (2) Maternity allowance is paid to insured female employees to compensate lost wages, in whole or in part, during maternity leave from work. Insured female employees are eligible beginning 42 days before the expected delivery date to 56 days after the date of delivery, which may be before or after the expected delivery date. Allowance is equivalent to two-thirds (approximately 66.67 percent) of daily standard remuneration for each day of unpaid or partially paid leave from work.
- (3) Childbirth grant is paid to insured employees to compensate costs associated with giving birth. This grant is available when the insured employee gives birth or when the dependent spouse or a family member of the insured employee gives birth. The amount is generally JPY390,000 per birth. Delivery at qualified hospitals is eligible for a JPY420,000 grant.



## Insurance contributions

Contributions to Health Insurance are shared equally by employee and employer. Employees' share of contribution is determined by their monthly standard remuneration multiplied by the contribution rate and is deducted from salaries and bonuses.

For employees whose employer is based in Tokyo, the applicable contribution rate is 9.91% of standard monthly salary and bonuses and is capped at JPY137,749 on monthly salaries of JPY1,390,000 or more and at JPY521,430 on annual bonuses of JPY5,730,000 or more. Contributions are shared equally between employer and employee. The contribution rate varies across prefectures.

### Standard remuneration

Standard Monthly Remuneration (SMR) is a key concept of social security in Japan. Insured employees' SMR at the time of the insured event will determine the amount of eligible cash benefits such as for sickness/illness allowance and maternity allowance. Insured employees' SMR also determines the amounts of Health Insurance contribution to be deducted from employees' salaries and bonuses along with the employers' matching contribution.

SMR is calculated at the time of hire and generally remains in effect until the following September. SMR is calculated by summing the amounts of monthly base salary, monthly commuting allowance, monthly housing allowance, monthly child tuition allowance, monthly social security allowance and any other allowances fixed and determinable at the time of hire, regardless of given name or title, paid as compensation for services rendered. The monthly sum is then referenced to the Standard Monthly Remuneration Table and plotted within the range of monthly remuneration in an applicable grade.

Each year, the sum of monthly remunerations in April, May and June are averaged, with certain applicable adjustments, and reported to the authorities. The averaged remuneration is referenced to the Standard Monthly Remuneration Table and plotted within the range of monthly remuneration in the applicable grade which generally becomes the new SMR effective September of the same year to August of the following year.

Standard Daily Remuneration (SDR) is equivalent to SMR divided by 30, which becomes the basis for cash benefits for sickness/illness allowance and maternity allowance.

Standard Bonus Remuneration (SBR) is the amount of the actual bonus received rounded down to the nearest thousand. The health insurance contribution rate in effect is then applied to SBR to derive the amount of contributions deducted from the bonus and matched by the employer.

## Nursing Care Insurance

The flip side of having the longest average life span in the world is that the number of elderly people unable to live on their own in their later years is on continuing rise in Japan. Nursing Care Insurance Law was enacted in December 1997 and came to effect in April 2000 to sustain the daily livelihoods of elderly people who require care due to physical or mental incapacities related to old age. Benefits are generally provided in kind in the form of care services.

Those ages 40 and above with residency in Japan are, regardless of nationality or the length of intended stay in Japan, required to participate in insurance by having their share of contribution withheld from salaries and bonuses together with contributions for Health Insurance. As of September 1, 2017, the contribution rate of Nursing Care Insurance is 1.65% of SMR and SBR. It is capped at JPY22,935 on SMR of JPY1,390,000 and at JPY94,545 on cumulative SBR of JPY 5,730,000 or more. Contributions are shared equally between employer and employee and the applicable rate does not vary across prefectures.

## Child Raising Contribution

Child Raising Contributions are pooled by the government to fund child raising grants to eligible households with children.

Child Raising Allowance Contribution is paid by employer only, and contribution rate is currently 0.23% of SMR and SBR. It is capped at JPY1,426 on SMR of JPY620,000 or more and at JPY3,450 on SBR of JPY1,500,000 or more.

## Welfare Pension Insurance

All residents of Japan aged 20 and above participate in public pension programs regardless of nationality and are issued a pension booklet which contains a basic pension number unique to each individual.

Corporate employees participate in Welfare Pension Insurance managed and operated by the Japanese government. Registration with Welfare Pension Insurance is administered by the employer, usually by their human resource department or outsourced service provider.

Oftentimes, however, employees on international assignment to Japan or their employers do not wish to register with Welfare Pension Insurance because they are covered under similar system in their home country. Certain bilateral social security agreements, such as those between Japan and the U.S., may, under such circumstance, offer exemptions from participating in Welfare Pension Insurance. It should, however, be noted that exemption is available only if employees on international assignment to Japan obtain a certificate of coverage from a competent authority in their home country prior to their assignment or secondment to Japan.

Employees already living and working in Japan and those coming on assignment or secondment to Japan from countries that do not have a bilateral social security agreement with Japan will be required to register with the Welfare Pension Insurance regardless of whether or not the individual is covered under an equivalent or similar program in their home country.

In the event employees on international assignment to Japan avoid participation in Welfare Pension Insurance not due to the application of bilateral social security agreement but due to the nature of their service performance in Japan and other specific facts and circumstances, they are required to participate in the National Pension managed and operated by the Japanese government. National Pension is a pension system for non-employees. Participants include workers in agriculture, forestry and fishery industries along with shop owners, self-employed workers and those unemployed and their dependent family members. Registration with National Pension requires the individual to file the necessary application forms at the Pension Office or at the national pension division within local municipal offices with jurisdiction over their registered address.

### Benefits

Welfare Pension Insurance provides old-age, disability and survivor's benefits to covered employees and their dependent family members.

#### Old-age benefits

In principle, a covered employee who has (a) contributed to Welfare Pension Insurance for 10 years or more (effective August 1, 2017), (b) reached 65 years of age and (c) is not employed is eligible to receive Old-Age Basic Pension (a fixed amount) and Income-Related Pension (a variable amount).

#### Disability benefits

Disability benefits are generally provided to employees who suffer non-work related injuries or sickness and who continue to suffer disability after 18 months. Sickness/illness allowance from Health Insurance is available during the 18 months if the employee is unable to work and unpaid.

#### Survivor's benefits

Survivor's benefits are provided to a dependent spouse or other qualified relatives in the case of death of the covered employee.

#### Lump-sum withdrawal payment

Employees on international assignment or secondment to Japan who participated in Welfare Pension Insurance may elect to claim a part of their cumulative contribution paid into the Welfare Pension Insurance through payroll deductions.

As of September 1, 2017, the contribution rate of Welfare Pension Insurance is 18.30% of SMR and SBR. It is capped at JPY 113,460 on SMR of JPY 620,000 or more and at JPY274,500 on SBR of JPY 1,500,000 or more.

## Workers' Accident Compensation Insurance

Workers' Accident Compensation Insurance provides benefits to employees who suffer injuries and sickness arising out of and in the course of employment including daily commuting to and from work. Employers with one or more employees are required to provide insurance coverage to employees under the Workers' Accident Compensation Insurance.

Contribution rates range from 0.25% to 8.8% of actual salaries and bonuses, depending on the industry in which employers operate and the type of work employees are engaged in. There are no upper limits on the contribution amounts.

Medical expenses related to injuries and sickness arising out of and in the course of employment including daily commuting to and from work are covered in full by the insurance. In the case of permanent disability, annual or lump-sum benefits are paid based on the severity of the injury.

## Employment Insurance

Employment Insurance provides unemployment benefits and job securing assistance to the unemployed. Employers with one or more employees are required to provide insurance coverage to employees under Employment Insurance.

Though at different rates, employers and employees both contribute to the system by paying insurance contributions. In most industries, contributions paid by employers is 0.60% of employees' salaries and bonuses, and contributions paid by employees is 0.30% of their salaries and bonuses. There is no upper limit on the contribution amount.

Employment Insurance provides unemployment benefits for a period of 90 to 360 days depending on the length of service with the previous employer and the reason or cause of leaving the previous employer.



# **International Social Security Agreements**

## Objectives

Since the early 2000's, Japan has established a network of bilateral Social Security agreements that coordinate the Japanese Social Insurance systems with the comparable systems of other countries. The topic should be of particular interest to multinational companies and to people who work abroad during their careers.

International Social Security agreements, often called "Totalization Agreements" have two main purposes: (1) elimination of dual Social Security taxation, the situation that occurs when a worker from one country works in another country and is required to pay Social Security taxes to both countries on the same earnings, and (2) filling gaps in benefit protection for workers who have divided their careers between Japan and another country.

Following is a list of agreements Japan has concluded and the effective dates of each as of 31 May, 2020. Some of these agreements were subsequently revised; the dates shown are the dates the original agreement entered into effect.

Germany	February 2000
United Kingdom	February 2001
Korea	April 2005
United States	October 2005
Belgium	January 2007
France	June 2007
Canada	March 2008
Australia	January 2009
Netherlands	March 2009
Czechoslovakia	June 2009 (Currently preparing for partial amendment)
Spain	December 2010
Ireland	December 2010
Brazil	March 2012
Switzerland	March 2012
Hungary	January 2014
India	October 2016
Luxemburg	August 2017
Italy	In preparation (signed February 2009)
Philippines	In preparation (signed November 2015)
Slovakia	In preparation (signed January 2017)

## Elimination of Dual Taxation

Without some means of coordinating Social Security coverage, people who work outside their country of origin may find themselves covered under the systems of two countries simultaneously for the same work. When this happens, both countries generally require the employer and employee to pay Social Security taxes.

Dual Social Security tax liability is a widespread problem for multinational companies and their employees because, for example, the U.S. Social Security program covers expatriate workers, both those coming to the United States and those going abroad. U.S. Social Security extends to U.S. citizens and U.S. resident aliens employed abroad by U.S. employers without regard to the duration of an employee's foreign assignment, and even if the employee has been hired abroad. This extraterritorial U.S. coverage frequently results in dual tax liability for the employer and employee since most countries, as a rule, impose Social Security contributions on anyone working in their territory.

Paying dual Social Security contributions is especially costly for companies that offer "tax equalization" (or "gross up") arrangements for their expatriate employees. A firm that sends an employee to work in another country often guarantees that the assignment will not result in a reduction of the employee's after-tax income. Employers with tax equalization programs, therefore, typically agree to pay both the employer and employee share of host country Social Security taxes on behalf of their transferred employees.

Under the tax laws of many countries, however, an employer's payment of an employee's share of a Social Security contribution is considered to be taxable compensation to the employee, thus increasing the employee's income tax liability. The tax equalization arrangement generally provides that the employer will also pay this additional income tax, which in turn serves to increase the employee's taxable income and tax liability even further. The employer again pays the additional tax, etc., etc. As one can readily see, the employee's foreign Social Security coverage results in a substantially greater tax burden for the employer than the nominal Social Security tax alone.

## Detached-worker Rule

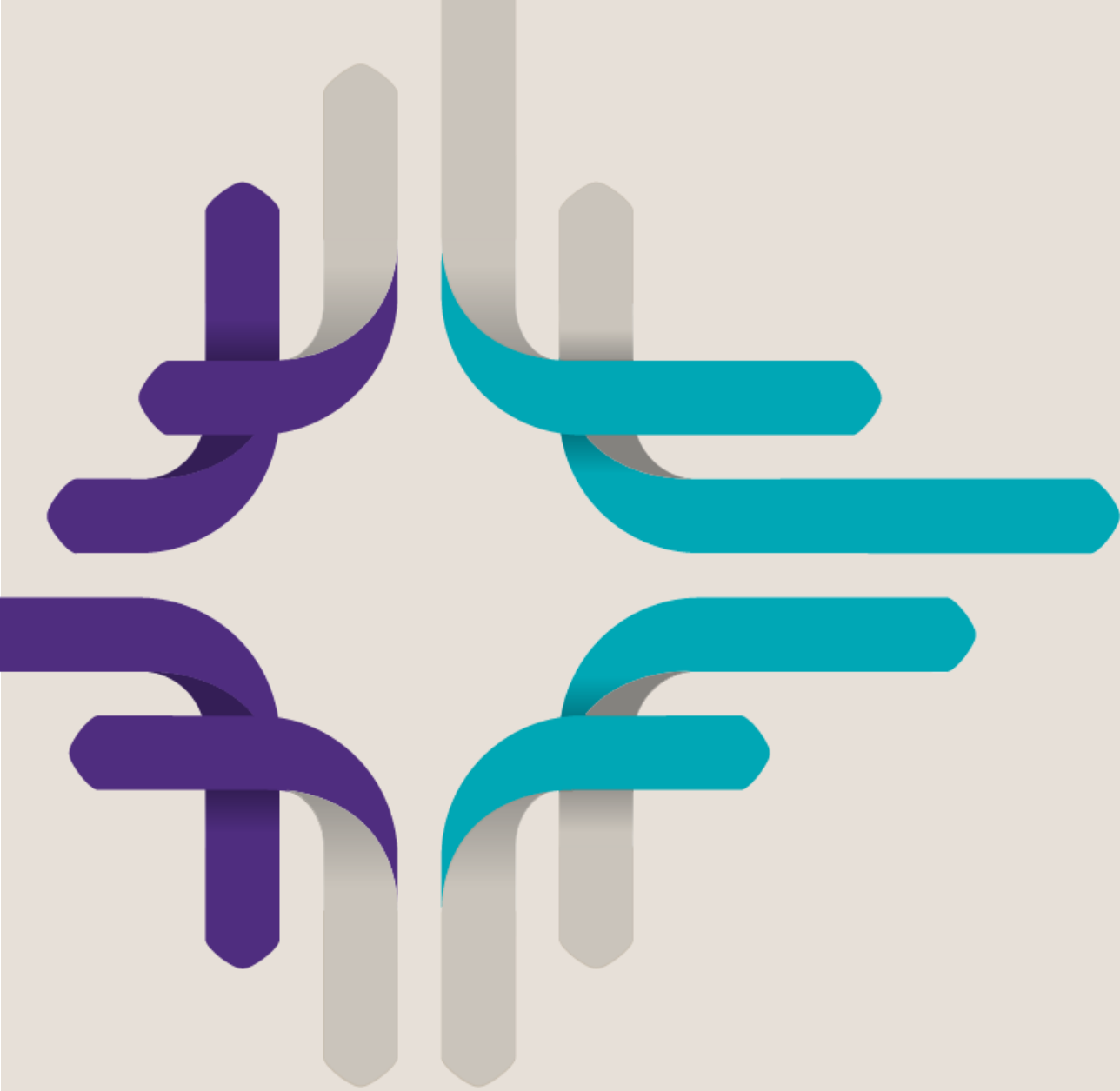
Most agreements include an exception to the territoriality rule, a rule whereby an employee who would otherwise be covered by both Japan and a foreign system remains subject exclusively to the coverage laws of the country in which he or she is working, designed to minimize disruptions in the coverage careers of workers whose employers send them abroad on temporary assignment. Under this "detached-worker" exception, a person who is temporarily transferred to work for the same employer in another country remains covered only by the country from which he or she has been sent.

For example, an individual temporarily transferred by the US employer to work in Japan continues to be covered under US social security and can be exempt from registering with Japanese social security. The individual and employer pay contributions only towards US social security.

The detached-worker rule in Japanese agreements generally applies to employees whose assignments in the host country are expected to last 5 years or less. The 5-year limit on exemptions for detached workers is substantially longer than the limit normally provided in the agreements of other countries.

## Totalization of Coverage Periods

Workers who have divided their careers between two countries sometimes fail to qualify for retirement, disability, or survivors' benefits from one or both countries because they do not have enough credits to be eligible. Under the totalization agreement, such workers may qualify for partial or full benefit based on combined, or "totalized", coverage credits from both countries.



# Inheritance Tax and Gift Tax

# Inheritance Tax and Gift Tax

## Background

Japan has one of the highest tax rates in the World for transfers of wealth, such as by inheritance or gift. Despite this, in recent years the government has sought to widen the scope of Inheritance Tax and Gift Tax as part of a drive to increase the tax levied on high net worth individuals. Following the business sentiment that the laws were a difficult obstacle to recruiting highly-skilled professionals from overseas, additional measures were introduced to bring Japan's inheritance and gift tax laws in line with several European countries and the U.S., which do not levy inheritance/estate tax on expats on temporary assignments with offshore assets.

The resulting tax reforms have resulted in a complicated set of rules to determine a taxpayer's obligation to file returns and pay tax.

## Outline

Japan operates an Inheritance Tax system supplemented by a Gift Tax system. Inheritance Tax is levied on the transfer of property from a decedent and the Gift Tax system applies to prevent the reduction of the Inheritance Tax base through transfers during a taxpayer's lifetime. The obligation to pay and the scope of both taxes are the same in most situations, but Gift Tax rates are higher than Inheritance Tax rates and the exempt amount is lower.



Obligation and scope

The obligation to pay Japanese Inheritance Tax and Gift Tax falls on the person inheriting or receiving assets. The chart below shows the scope of Japan IHT and Gift Tax

Decedent / donor \ Successor / donee		Domicile in Japan		No domicile in Japan		
			Temporarily domiciled *1	Japanese national		No Japanese nationality
				Domiciled in Japan within the past 10 years	No domicile in Japan within the past 10 years	
Domicile in Japan						
	Temporarily domiciled foreign national *1					
No domicile in Japan	Domiciled within the past 10 years					
	Exceptions *2					
	No domicile in Japan within the past 10 years					

Worldwide assets fall within the scope of Japan inheritance and gift tax.

Only assets located in Japan fall within the scope of Japan inheritance and gift tax.

Notes:

\*1 Temporarily domiciled

Visa status from Immigration Control and Refugee Recognition Act Appendix Table 1 (other than Permanent resident and Spouse of Japanese national), AND domiciled in Japan for fewer than 10 of previous 15 years

\*2 Exceptions

Scope of assets subject to tax differs depending on whether by inheritance or gift, as well as the nationality and domicile of the two parties.

# Inheritance Tax Calculation

## Basic exemption

Each estate benefits from a basic exemption and a deduction for each statutory heir. As a result, the tax basis of an estate for Inheritance Tax purposes is calculated as follows:

Taxable amount = Value of assets received

- JPY30 million (basic exemption)
- (JPY6 million x no. of statutory heirs)

## Tax rate

The liability is then calculated as:

$$\text{Tax liability} = (\text{Taxable amount} \times \text{tax rate}) - \text{deduction}$$

based on graduated tax rates as shown in the table below:

Total taxable amount after exemptions (JPY)	Inheritance Tax rate (%)	Deduction (JPY)
10 million or less	10	0
30 million or less	15	500,000
50 million or less	20	2 million
100 million or less	30	7 million
200 million or less	40	17 million
300 million or less	45	27 million
600 million or less	50	42 million
More than 600 million	55	72 million

# Gift Tax Calculation

Gift Tax is calculated based on the sum of gifts received by a taxpayer during a calendar year. The tax basis for Gift Tax purposes is calculated as follows:

Taxable gifts = Net value of assets received during a calendar year

- JPY1.1 million (annual exemption)

## Tax rate

The liability is then calculated as:

$$\text{Tax liability} = (\text{Taxable amount} \times \text{tax rate}) - \text{deduction}$$

Different rates and deductions apply depending on the nature of the relationship between the donor and the donee.

For gifts within a family to a donee who is at least 20 years old from a lineal ascendant the tax rates and deductions are as follows:

Taxable gift (JPY)	Gift Tax rate (%)	Deduction (JPY)
2 million or less	10	0
4 million or less	15	100,000
6 million or less	20	300,000
10 million or less	30	900,000
15 million or less	40	1.9 million
30 million or less	45	2.65 million
45 million or less	50	4.15 million
More than 45 million	55	6.4 million

For gifts other than the above, the rates and deductions are as follows:

Taxable gift (JPY)	Gift Tax rate (%)	Deduction (JPY)
2 million or less	10	0
3 million or less	15	100,000
4 million or less	20	250,000
6 million or less	30	650,000
10 million or less	40	1.25 million
15 million or less	45	1.75 million
30 million or less	50	2.5 million
More than 30 million	55	4 million

## Filing and payment obligations

Inheritance Tax returns must be filed within ten months of the date of the passing of the decedent. Gift Tax returns must be filed between 1 February and 15 March of the calendar year following the gift. Any Inheritance Tax or Gift Tax due should be paid by the same deadline as the tax return.

## Others

### Foreign Tax credit

A foreign tax credit is available for taxes similar to Inheritance Tax or Gift Tax which are paid in a foreign country on assets located outside of Japan. In the absence of an estate tax treaty with the country, the credit is limited to taxes paid in a single jurisdiction. Currently Japan has only entered into an estate tax treaty with the USA.

For Inheritance Tax purposes, the credit is capped at using the following formula:

$$\text{Foreign tax credit limit} = \text{Japan Inheritance tax due} \times \frac{\text{Property received located in the foreign country}}{\text{Total property received}}$$

For Gift Tax purposes, the credit is capped at using the following formula:

Foreign tax credit limit =

$$\text{Japan Gift tax due} \times \frac{\text{Gifts of property located in the foreign country during the year}}{\text{Total property received through gifts during the year}}$$



## Other Taxes

## Fixed Assets Tax (Depreciable Assets)

Depreciable assets are defined as the business assets excluding land/buildings where the amount of depreciation expense is included in losses or necessary expenses when calculating the income pursuant to the Corporation Tax Act or the Income Tax Act. These assets include the structures, machinery, equipment and fixtures, which the corporations or individuals who run a business can use for their business.

(1) Submitting your tax return

Those who possess depreciable assets as of January 1 in any given year shall report the depreciable assets concerned to the municipal office or the Tokyo Metropolitan Taxation Office in the ward (the 23 special wards) where the assets are located by January 31 of the year. The property price of depreciable assets is determined based on the information contained in the taxpayer's tax return and is registered into the depreciable assets tax register.

(2) Issue of Tax Notice

The tax amount is calculated in the following way, and a Tax Notice issued in early June.

$$\text{Tax amount} = \text{Standard taxable value} \times \text{Tax rate (1.4\%)}$$

Standard taxable value is the value that is decided based on the assessed value as of the base date for assessment (January 1) and is registered into the depreciable assets tax register. If the Standard taxable value calculated at assessment is less than JPY1,500,000 (tax exemption limit), no fixed assets tax is imposed, and therefore a tax notice is not issued.

(3) Payment due dates

Payment due dates are the each end of June, September, December and February. It is possible to pay the entire tax in June.

(4) When renting offices or other spaces (as tenants, etc.):

The tax is imposed on the depreciable fixed assets such as interior finishing, fixtures and building equipment installed by a tenant.

O = Taxable, X = Non-taxable

Acquisition value Depreciation method	Less than JPY100,000	JPY100,000 to less than JPY200,000	JPY200,000 to less than JPY300,000	JPY300,000 and above
Individual depreciation	O	O	O	O
Special provision for small business enterprises	O	O	O	
Inclusion into temporary deductible expense	X			
Three-year lump-sum depreciation	X	X		

### Special Tax Treatment regarding COVID-19

For certain SMEs affected by COVID-19, the tax rates applied to calculate fixed asset tax and city planning tax on depreciable assets and business-use houses will be reduced, depending on the following decrease in revenue:

Decrease in revenue for any 3 month period from February 2020 to October 2020 compared to the same period in the previous year	Reduced tax rate
30% or more decrease but less than 50%	50%
50% or more decrease	100%

These reduced rates will apply to the 2021 fiscal year only.

## Business Establishment Tax

Business establishment tax is a special purpose tax to be used for projects which to improve and maintain the urban environment. This is also municipal tax imposed only in the cities specified by the Local Tax Act.

The term “Business establishment” refers to offices and establishments regardless of whether they are owned or rented. Specifically, this includes offices, stores, factories and warehouses.

#### (1) Taxpayers and tax calculation

- Fixed assets rate

Corporations or individuals whose total floor space of offices in the specific cities is more than 1,000m<sup>2</sup> (tax exemption limit).

$$\text{Tax payable} = \text{Floor areas of offices (m2)} \times \text{JPY600}$$

- Employee rate

Corporations or individuals whose total number of employees in offices located in the specific cities is more than 100 (tax exemption limit).

$$\text{Tax payable} = \text{Total amount of employees' salary} \times 0.25\%$$

#### (2) Decision on tax exemption limit

The tax exemption limits are decided for the fixed assets rate and employee rate respectively in accordance with the actual status as of the final day of the business accounting year for corporations and as of December 31 for individuals.

#### (3) Due date and procedures for tax payment

The tax must be calculated by self-assessment and paid to the municipal office or the Tokyo Metropolitan Taxation Office in the ward (the 23 special wards), in which the principal place of business is located, within two months from the closing date of the business year in case of corporations, and for individuals by March 15 of the year following the year when the business was conducted. Different from enterprise tax and inhabitant tax on corporations, business establishment tax has no system for extending the due date of filing a tax return.

# Real Estate Acquisition Tax

Tax is imposed on those who acquired real estate through purchase, gift, or exchange of land/building or constructing (enlargement and remodelling) of a new residence/building, regardless of whether the property is registered or not. The tax, however, is not assessed for acquisition through inheritance.

## (1) Tax calculation

### Assessed value of acquired real estate (standard taxable value) x Tax rate

For residential land or evaluated residential land acquired on or before March 31, 2021, the standard taxable value is the acquisition price x 1/2. The tax rate is as follows:

Date of Acquisition	Land	Building (Residential)	Building (Non-Residential)
From April 1, 2008 to March 31, 2021		3/100	4/100

## (2) Due date and procedures for tax payment

A tax notice is sent from the municipal office or the Tokyo Metropolitan Taxation Office. The tax shall be paid by the end of tax period at the tax authority, at financial institutions such as banks, or post office.

## (3) Value of acquired real estate

The value of acquired real estate is assessed and determined based on the Standard Valuation Code of Fixed Assets, which was established by the Ministry for Internal Affairs and Communications. The assessed values are basically equivalent to the registered prices in the fixed assets tax register except for new or enlarged buildings. Therefore, the values refer to neither purchase prices of real estate nor construction work expenses.

## (4) Tax exemption limit

Real estate acquisition tax is not assessed when the standard taxable amount of the property is lower than shown in the table below:

Type		Value (JPY)
Land		100,000
Buildings	New/ expanded/renovated	230,000
	Others	120,000

## (5) Notification of the acquisition of real property

Notification must be submitted to the competent municipal office or Metropolitan Taxation Office having jurisdiction over the area where the land/buildings are located, within 30 days from the date of acquisition.

# Fixed assets tax (Land & Buildings)

Those who are registered in the fixed assets tax register as owners of land and/or buildings as of January 1 shall pay the fixed assets tax.

## (1) Taxpayer subsequent to transfer of assets

In the event that the transfer of ownership of assets is executed on or after January 2, the obligation for paying taxes on the assets is not transferred. Although there may be cases in which the burden of the fixed assets tax is shared between the parties based on the sales contract in proportion to the length of period of ownership, such an arrangement is not required under tax laws.



(2) Tax payment

**(Standard taxable value x 1.4%) - Deductions, etc.**

(3) Due date and procedures for tax payment

In principle, taxpayers shall pay the tax four times a year in June, September, December, and February based on the Tax Notice that is sent in the first tax due month in June.

(4) Assessed value of fixed assets

The value of fixed assets is the price that is determined by the prefectural governors or the mayors of city, town or village on the basis of the Standard Valuation Code of Fixed Assets, which was established the Ministry of Internal Affairs and Communications, and then registered in the fixed assets tax register.

(5) Tax exemption limit

Fixed assets tax is not imposed when the total standard taxable value of fixed assets owned by the same person in the same municipality is less than JPY300,000 for land and JPY200,000 for residential buildings.

## City planning tax

City planning tax is a special-purpose tax used to cover expenses for city development/maintenance and other costs. In principle, it is levied on individuals who own land or residential buildings in urbanization promotion areas designated under the City Planning Act.

(1) Taxpayers and tax payment

Those who were registered in the fixed assets tax register as owners of land and/or buildings as of January 1 pay the city planning tax.

**Standard taxable value x 0.3% - Deductions**

\*A tax reduction is applied for small-scale residential land.

(2) Due date and procedures for tax payment

In principle, taxpayers shall pay the tax four times a year in June, September, December, and February based on a Tax Notice that is sent in the first tax due month in June. City planning tax is levied in conjunction with fixed assets tax on land, houses and buildings. The Tax Notice shows both the city planning tax and the fixed assets tax due.

## Registration and license tax

Registration and license tax is 0.7% of share capital (minimum JPY150,000) at the time of incorporation of a limited stock company and 0.7% for registration of an increase in share capital (minimum tax amount JPY30,000). Registrations of ownership, leaseholds rights, real estate mortgages, industrial property and other rights, directors and statutory auditors of a company and business licenses of regulated businesses are also subject to registration and license tax.

Payment shall be made in cash, and the registration application form should be submitted together with the receipt of tax payment. When the tax amount is JPY30,000 or less, payment can be made with the stamp.

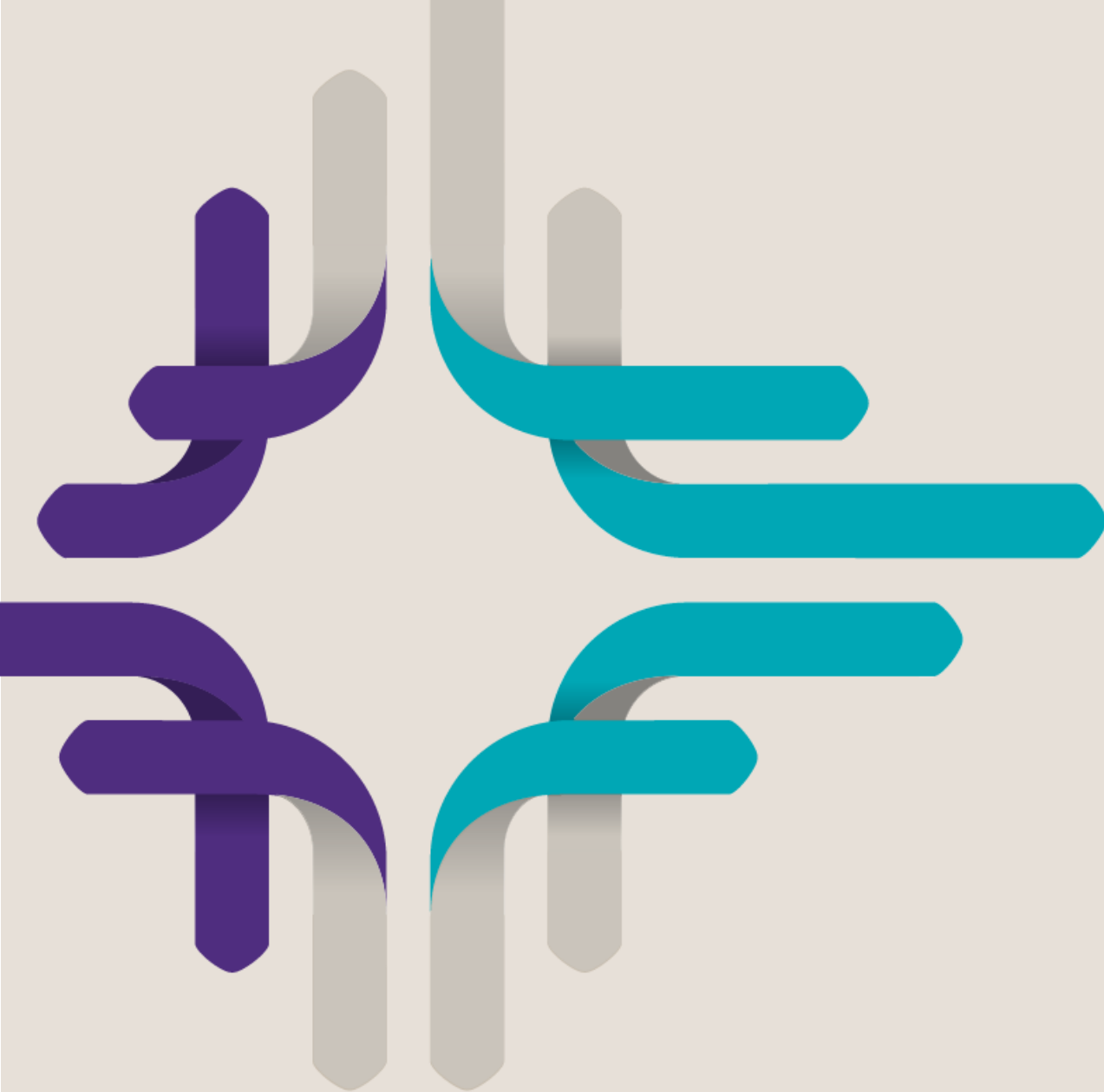
## Stamp tax

Stamp tax is levied on certain taxable documents, such as agreements, bills and receipts designated under the Stamp Tax Law. Those who create these documents should paste a revenue stamp based on the value of consideration shown in the document.

The creator of the document bears the responsibility for paying the tax and if this obligation is not met, penalty tax of 3 times the stamp amount is imposed (reduced to 1.1 times if the mistake is pointed out by the taxpayer).

### Special Tax Treatment regarding COVID-19

Stamp tax duty is exempted for special loan contracts that were provided by public and private financial institutions to companies affected by COVID-19. Refunds will be made retroactively to those who have already concluded a contract and paid stamp tax.



# Employment Regulations and Industrial Relations

## What kind of employment regulations exist?

Numerous laws regulate the employment environment in Japan. Among them, the Labour Standards Law stipulates the minimum employment conditions employers must observe including terms and conditions of labour contracts, wages, working hours, holidays, paid annual leave, safety, sanitation, women and minors, accident compensation, working regulations, etc.

Other examples of laws regulating the employment environment include the Labour Union Law which regulates the formation of labour unions, collective bargaining, labour agreements, etc. and the Labour Relations Adjustment Law which regulates restrictions and resolutions on strikes and other labour disputes.

## What are customary working hours and holidays?

Labour Standards Law stipulates that working hours must not be more than 8 hours a day and 40 hours a week. A working day from 9:00 a.m. to 5:00-6:00 p.m., with a one-hour lunch break, and a 5-day work week is common in Japan. The Labour Standards Law stipulates that an employer must give an employee at least 4 days' holiday in every 4-week period. Customary holidays are Sundays (and Saturdays in case of 5-day work week) and national holidays. In addition, annual paid holidays are given to employees based upon the company's internal working regulations or labour agreement. The minimum statutory requirement is 10 days following completion of the first six-months of service, with one day added for each of the following two years and two days added for each year thereafter of up to a total of 20 days.

## Is compensation payable for redundancy?

Labour Standards Law stipulates that when an employer discharges an employee, the employer must notify the employee 30 days in advance; otherwise the employer must pay the employee the equivalent of at least 30 days wages. Although not legally required, it is a common practice for Japanese companies to pay severance benefits when an employee leaves an employer. Amount of benefit is generally determined on the basis of number of years of service, current salary level and whether the termination is voluntary or involuntary.

It is important to note that due to the protective nature of the Labour Standards Law, terminating employees is very difficult and involves significant legal risk. Article 16 of the Labour Contract Law provides that "a dismissal shall, if it lacks objectively reasonable grounds and is not considered to be appropriate in general societal terms, be treated as an abuse of right and be invalid."

Further, numerous court cases have established rules on terminating employees due to business downsizing. The rules require that termination due to downsizing (1) was necessary from a business management perspective; (2) an effort was made by management to avoid business downsizing, (3) reasonable standards were set in place in selecting employees for termination; and (4) discussions were held with the selected employee. Courts have voided terminations lacking these factors and ordered monetary compensation to employees.

## What labour organisations exist?

Labour Standards Inspection Office supervises compliance with the Labour Standards Law and other employment related laws. An employer with 10 or more employees is required to prepare and file an Employers' Handbook or other internal policies with the Labour Standards Inspection Office, with the opinion of the labour union or other employee representative.

## Are working conditions controlled?

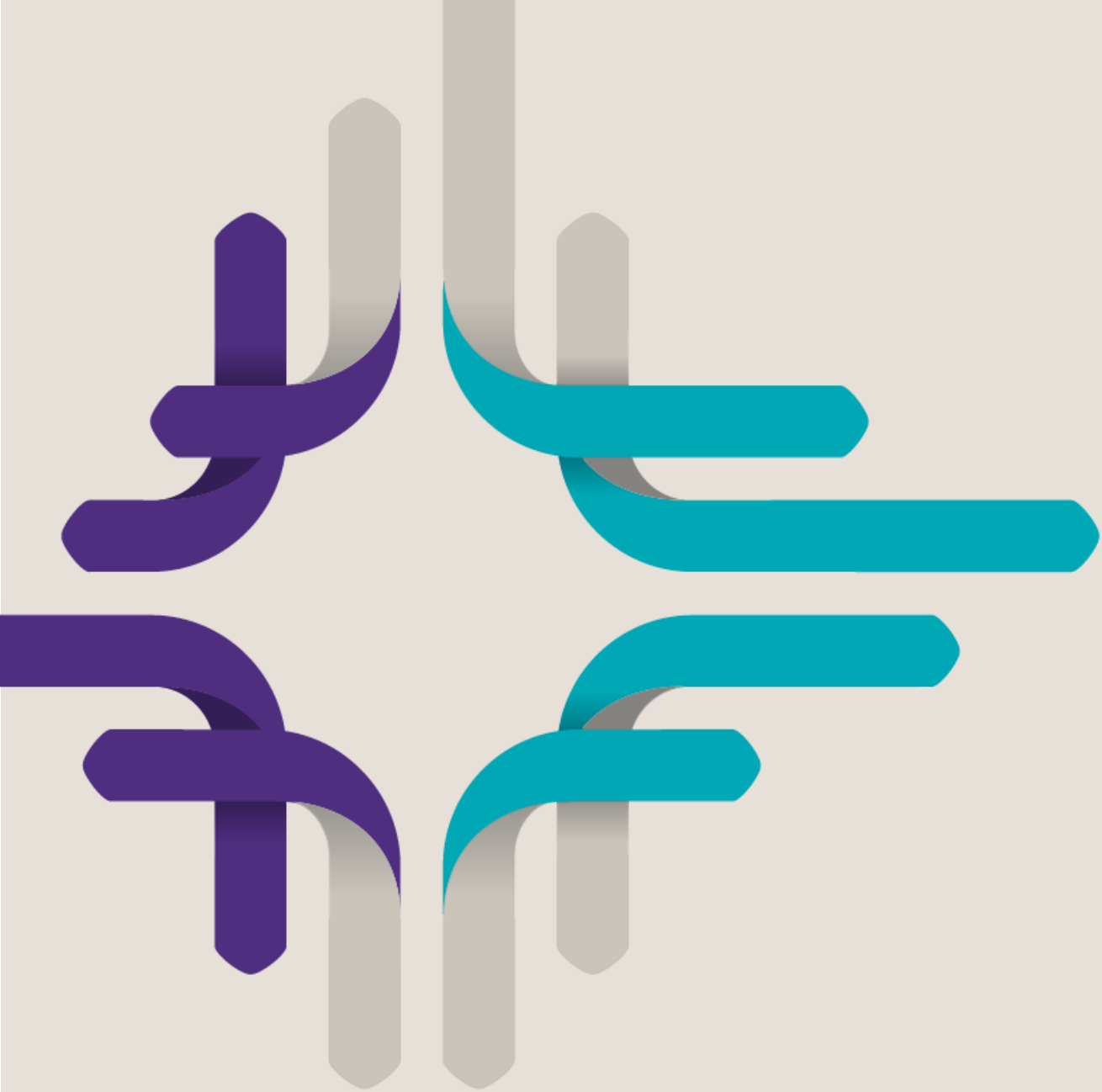
An inspector of the Labour Standards Inspection Office may order an employer to present its books and records or inspect them at the employer's premises and question the employer or employees to investigate compliance with labour and employment laws and regulations. An employee may ask for such an investigation. Penalties include imprisonment and fines for violation of respective laws and regulations.

## Are work permits required for foreign workers?

Yes. The Immigration-Control and Refugee-Recognition Law stipulates that only foreign persons who have obtained visas for (a) engaging in trade and other business or investment activities in Japan, (b) providing advanced or special technique or skills for invited organisations, (c) working as skilled labourers or (d) living permanently in Japan, may work in Japan.

## Are annual health check-ups required?

Yes. Industrial Safety and Health Law required employers to have their employees undergo annual medical examinations. The contents of the medical examination differ based on age and sex of employees. The cost of the medical examination is borne by the employer and time spent undergoing medical examination is considered as time worked.



# **Manufacturing and Other Trade Regulations**

## Are manufacturing licences required?

Manufacturing, selling and importing of pharmaceuticals products and oftentimes medical devices require licence from the Ministry of Health, Labour and Welfare. Manufacturing, selling and importing of other products may require specific government licenses.

## Are there any controls over prices and income?

While prices of certain basic products and services such as rice and other grains, petroleum, transportation fares, telephone and other utilities are controlled by the Japanese government, prices of other products and services are left to a supply and demand dynamics of economics.

## Is there any legislation over restrictive practices?

Anti-Trust laws prohibit private monopolies, unreasonable trading restrictions, unfair trading methods and any unreasonable restrictions on business activities by means of combination or agreement. The Fair Trade Commission supervises compliance with the law.

## What other restrictions may be imposed on a company's business?

Various laws, guidance by the regulatory Government departments and various agreements including labour agreements and loan agreements may impose restrictions on a company's business.

---

# Contact details

---

Grant Thornton International Business Centres in Japan can be located at the following addresses:

## International Business Center

Director: Isamu Takagi

Akasaka K tower 18F  
1-2-7 Motoakasaka, Minato-ku  
Tokyo, 107-0051  
Telephone: +81-36438-9395  
[www.grantthornton.jp](http://www.grantthornton.jp)

## Grant Thornton Taiyo LLC (Audit Services)

Tokyo

Akasaka K tower 22F  
1-2-7 Motoakasaka, Minato-ku  
Tokyo, 107-0051  
Telephone: +81-3-5474-0111

Osaka

Umeda Center Building 25F  
2-4-12 Nakazaki-Nishi, Kita-ku  
Osaka, 530-0015  
Telephone: +81-6-6373-3030

## Grant Thornton Taiyo Tax Corporation (Tax Services)

### Grant Thornton Taiyo Inc. (Consulting)

### Grant Thornton Taiyo Human Capital Corporation (Payroll solutions and Human Capital Services)

### Grant Thornton Taiyo Accounting Service Inc. (Accounting solutions and Treasury Services)

Tokyo

Aoyama Bldg.12F  
1-2-3 Kitaaoyama, Minato-ku,  
Tokyo, 107-0061  
Telephone: +81-3-5770-8822

Osaka

Umeda Center Building 13F  
2-4-12 Nakazaki-Nishi, Kita-ku  
Osaka, 530-0015  
Telephone: +81-6-6359-0002

## Grant Thornton Taiyo Advisors Co., Ltd. (Advisory Services)

Tokyo

Akasaka K tower 22F  
1-2-7 Motoakasaka, Minato-ku  
Tokyo, 107-0051  
Telephone: +81-3-6434-072



# Grant Thornton

An instinct for growth™

© 2020 Grant ThorntonTaiyo Tax Corporation. All rights reserved.

'Grant Thornton' refers to the brand under which the Grant Thornton member firms provide assurance, tax and advisory services to their clients and/or refers to one or more member firms, as the context requires. Grant Thornton International Ltd (GTIL) and the member firms are not a worldwide partnership. GTIL and each member firm is a separate legal entity. Services are delivered by the member firms. GTIL does not provide services to clients. GTIL and its member firms are not agents of, and do not obligate, one another and are not liable for one another's acts or omissions.