

Japan Tax Bulletin

Preferential Tax treatments for Small or Medium sized Enterprise (“SME”)

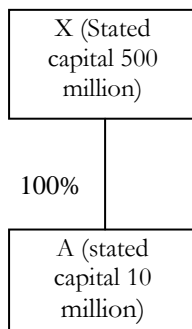
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SME is treated preferentially for various tax aspects. This issue summarizes preferential tax treatments of SME.

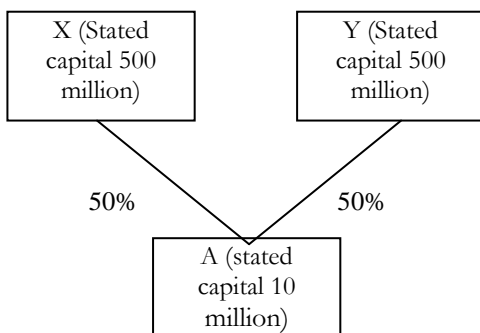
1. SME

There are a couple of definitions of SME depending preferential tax treatments applicable. Article 66 of the Corporation tax law defines SME as a corporation whose stated capital is JPY 100 million or less. Even where the stated capital is JPY 100 million or less, a corporation is not qualified for SME if 100% owned directly or indirectly by a corporation/corporations of which stated capital is JPY 500 million or more (“Large corporation”).

Corporation A below is not SME as it is wholly owned by a large corporation (X)



Corporation A below is SME unless X and Y are 100% owned by a common corporate parent.



2. Tax rate

2.1 Corporation tax

The tax rate of Corporation tax (national corporate income tax) is 23.9%. The tax rate for taxable income up to 8 million is 15%¹ where a taxpayer is SME.

2.2 Enterprise tax

Enterprise tax is one of local income tax. Where a taxpayer's stated capital is more than JPY 100 million, enterprise tax consists of the three components, income levy, added value levy and capital levy. Added value levy and capital levy are payable even where the taxpayer is making losses. This is called as business scale based taxation where large business scale corporations bear costs of government services even if in loss position. The business scale based taxation is not applied to SME. The tax base is income levy only.

Further, where SME's stated capital is less than JPY 10 million or it has offices less than 3 prefectures, the following reduced rates of 3.4% (for taxable income JPY 4 million or less) and 5.1% (for taxable income exceeding JPY 4 million to JPY 8 million) while the standard rate is 6.7%.

2.3 Inhabitant tax

Inhabitant tax is another local income tax levied by municipal governments. The tax rate is 12.9%. There is no preferential tax rate for SME.

3. Tax loss

Tax loss can be carried forward to succeeding 9 years and be deducted from current year's taxable income with restriction of 80% of the current year's

taxable income for a blue tax return filer².

80% is reduced to 65% for a year beginning during April 1, 2015 and March 31, 2017 and 50% for a year beginning after March 31, 2017.

SME can deduct fully tax loss carried forward from the current year's taxable income.

Tax loss can be carried back to previous 1 year. However, tax loss carry back is currently suspended except for SME or a corporation in liquidation.

4. Entertainment expenses³

Entertainment expenses are entirely disallowed except 50% of meal/drink expenses. For SME, the bigger of 50% of meal/drink expenses⁴ or JPY 8 million is allowed.

5. Depreciation of small sum assets

Small sum assets of which acquisition cost is less than JPY 100,000 can be expended when acquired, assets of which acquisition cost is less than JPY 200,000 can be equally depreciated in three years. For SME, assets of which acquisition cost is less than JPY 300,000 are entirely deductible when acquired with the cap of JPY 3 million.

6. Tax incentives

6.1 Investment Tax incentive

a. Investments in equipment that enhances productivity

Where SME acquires machinery/equipment that enhances productivity, SME is granted 100%

² A blue tax return filer is a taxpayer who has made an election as such and is required to maintain books and records to calculate taxable income correctly.

³ Entertainment expenses are the expenses of entertaining customers, suppliers, and other persons associated with the business of the corporation for purposes of furthering the corporation's business interests.

⁴ Meal/drink expenses not exceeding JPY 5,000 per person with persons other than employees or officers are not included in entertainment expenses.

¹ The tax rate is temporarily reduced from 19% to 15% for a business year beginning before April 1, 2017 (Article 42-3-2① of Special Taxation Measures law).



one off special depreciation or 10% (SME of which stated capital is JPY 30 million or less)/7% (SME of which stated capital is more than JPY 30 million and not exceeding JPY 100) tax credit.

b. Investments in other equipment than one that enhances productivity

Where SME acquires other machinery/equipment than one that enhances productivity, SME is granted 30% one off special depreciation or 7% (SME of which

stated capital is JPY 30 million or less).

For this purposes, a company of which stated capital is JPY 100 million or less is not qualified for SME where 1/2 or more is owned by a corporation of which stated capital is more than JPY 100 million or 2/3 or more is owned by two or more corporations of which stated capital is more than JPY 100 million.

6.2 R&D tax credit

A corporate taxpayer who files a blue tax return qualifies for a tax credit of 8% to 10% of qualifying R&D expenses capped at 20% of the corporation tax liability. For SME, 12% of qualifying R&D expenses are creditable against corporation tax with the cap of 30% of corporation tax liability.



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