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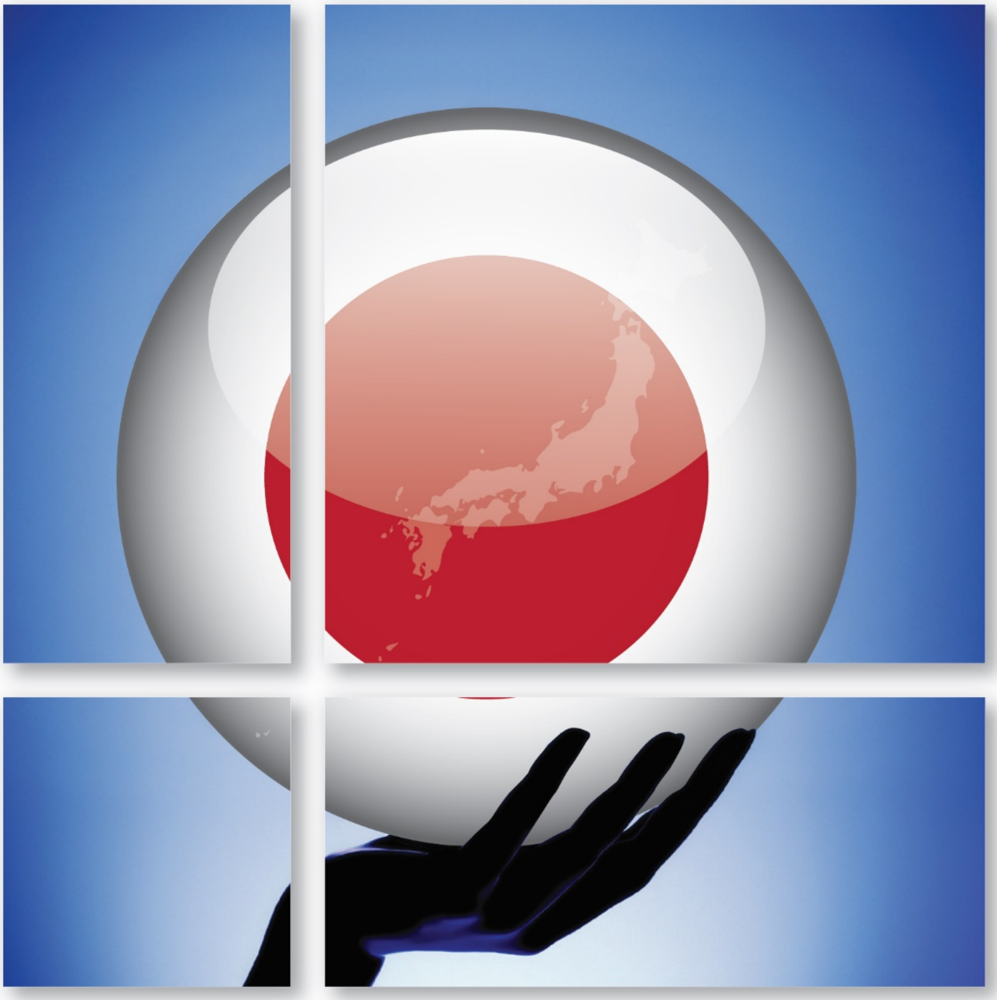

Japan

Tax Guide

2015/16

FOREWORD

A country's tax regime is always a key factor for any business considering moving into new markets. What is the corporate tax rate? Are there any incentives for overseas businesses? Are there double tax treaties in place? How will foreign source income be taxed?

Since 1994, the PKF network of independent member firms, administered by PKF International Limited, has produced the PKF Worldwide Tax Guide (WWTG) to provide international businesses with the answers to these key tax questions.

As you will appreciate, the production of the WWTG is a huge team effort and we would like to thank all tax experts within PKF member firms who gave up their time to contribute the vital information on their country's taxes that forms the heart of this publication.

The PKF Worldwide Tax Guide 2015/16 (WWTG) is an annual publication that provides an overview of the taxation and business regulation regimes of the world's most significant trading countries. In compiling this publication, member firms of the PKF network have based their summaries on information current on 1 January 2015, while also noting imminent changes where necessary.

On a country-by-country basis, each summary such as this one, addresses the major taxes applicable to business; how taxable income is determined; sundry other related taxation and business issues; and the country's personal tax regime. The final section of each country summary sets out the Double Tax Treaty and Non-Treaty rates of tax withholding relating to the payment of dividends, interest, royalties and other related payments.

While the WWTG should not to be regarded as offering a complete explanation of the taxation issues in each country, we hope readers will use the publication as their first point of reference and then use the services of their local PKF member firm to provide specific information and advice.

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- Assurance & Advisory;
- Financial Planning / Wealth Management;
- Corporate Finance;
- Management Consultancy;
- IT Consultancy;
- Insolvency - Corporate and Personal;
- Taxation;
- Forensic Accounting; and,
- Hotel Consultancy.

In addition to the printed version of the WWTG, individual country taxation guides such as this are available in PDF format which can be downloaded from the PKF website at www.pkf.com

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PKF INTERNATIONAL LIMITED
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BASIC FACTS

Full name:	Japan
Capital:	Tokyo
Main language:	Japanese
Population:	126.43 million (2014 estimate)
Major religion:	Shintoism, Buddhism
Monetary unit:	Yen (JPY)
Internet domain:	.jp
Int. dialling code:	+81

KEY TAX POINTS

- Domestic corporations, whose head or main office is located in Japan are subject to tax on their worldwide income.
- Foreign corporations are subject to either corporation tax or final withholding tax on Japanese source income (including income relating to the exploration for oil in the continental shelf) depending on the type of income and the extent of the foreign corporation's activities in Japan.
- Vendors are liable for a consumption tax (value added tax) of 6.3% of sales, including imports of goods and services.
- Relief is available for foreign taxes on foreign source income and capital gains whether or not Japan has concluded a tax treaty with the foreign country.
- Under the consolidated tax regime, an affiliated group of companies (a 'Consolidated Group') can report and pay national corporate income tax as one unit.
- All transactions between related companies are required to be conducted on an arm's length basis within the meaning of an 'arm's length price' depending upon the transaction.
- Domestic corporations are subject to withholding tax on dividends, interest and certain other income. Foreign corporations are subject to withholding tax on dividends, interest, royalties, income from immovable property, rentals from industrial or commercial equipment, and certain other income. No tax credit for income tax withheld on dividends is allowed in the case of foreign corporations.
- Non-resident taxpayers are taxed only on their Japanese source income. Non-permanent resident taxpayers are taxed on Japanese source income plus that part of non-Japanese source

income that is paid in and/or remitted to Japan. A permanent resident taxpayer is taxed on his worldwide income.

- Japan's annual tax reforms has steadily lowered corporation tax rates as part of a continuing effort to revitalise the economy. In response to the need for additional funds to deal with the aftermath of the earthquake in 2011, a surcharge of 10% of the national corporation tax liability has been added to the national corporation tax rate for three years from April 2012.

A. TAXES PAYABLE

COMPANY TAX

Domestic corporations are those whose head or main office is located in Japan. Companies incorporated in Japan under the Corporate Law or under other special laws are required to locate their head office in Japan. Such domestic corporations are subject to tax on their worldwide income.

Foreign corporations are all corporations which are not domestic corporations. A corporation having its head or main office outside Japan is a foreign corporation even if its business operations are in Japan. Foreign corporations are subject to corporation tax on Japanese source income, including income relating to the exploration for oil in the continental shelf. Foreign corporations are subject to either corporation tax or final withholding tax on Japanese source income, depending on the type of income and the extent of the foreign corporation's activities in Japan. Foreign corporations are not subject to tax on liquidation income.

The rate of national tax for Japanese corporations is 25.5% unless the paid-in capital of the corporation is JPY 100 million or less, in which case the first JPY 8 million of income is only taxed at 15%. In response to the need for additional funds to deal with the aftermath of the earthquake in 2011, a surcharge of 10% of the national corporation tax liability has been added to the national corporation tax rate for three years from April 2012. This surtax was planned to be levied for three years from April 2012, however, an early repeal by one year was finalized on 12 December, 2014. From 1 October, 2014, a part of inhabitant tax (local tax) has been moved to the national tax regime as ‘local corporate tax’ of 4.4%.

Tax is imposed on a current year basis. The tax year adopted is generally that specified in a company's constituent documents with the standard year being a calendar year. However, it should be noted that other periods are also allowed, including periods of 12 months or less. Japanese branches of foreign corporations are required to adopt the accounting period used by their foreign head office. Final tax is payable when lodging the final corporation tax return, usually required within two months of the end of the accounting period. Extensions of time to lodge can be sought although interest at 7.3% or less is payable where such an extension is obtained.

Interim tax returns and payments are required if a corporation has a fiscal period longer than six months. Ordinarily, provisional taxes are computed as one half of the tax liability of the previous year but a reduction is available where the interim tax returns are filed to reflect bi-annual results of operations for the current year.

BLUE RETURN FILERS

Preferential tax treatment is given to companies who file ‘Blue Returns’. A company which undertakes to maintain specified bookkeeping records and documentation and gains approval from the Director of the District Tax Office can file a Blue Return, the associated benefits of which are as follows.

- Tax losses may be carried forward for nine years (however for large scale companies, the use of the losses is restricted to 80% of taxable income for each year) or carried back to the previous year (temporarily suspended except for companies with paid-in capital of JPY 100 million or less (except for a subsidiary of a large scale company).

- The revenue authorities cannot seek to adjust taxable income without a physical review of the books and records of the company and must state the reason for such an adjustment.

- Allowance of reserves, special depreciation and tax credits as stipulated in the Special Taxation Measures Law.

Importantly, a new company must seek registration for Blue Form returns within the earlier of three months from incorporation or the end of the initial accounting period.

VALUE ADDED TAX (VAT)

Vendors are liable for a consumption tax (VAT) of 6.3% (7.8% from 1 April 2017) of sales, including imports of goods and services. Only a limited number of goods and services are zero rated.

Exemptions apply to leases of land, education and medical treatment. Exports and certain specific services invoiced to non-residents are zero rated. In addition, a new local consumption tax is also collected at the rate of 1.7% (2.2% from 1 April 2017). The net result will be a 8% (10% from 1 April 2017) rate of consumption tax.

LOCAL TAXES
INHABITANT TAX

Inhabitants Taxes are local prefectural and municipal taxes. These taxes are computed as a percentage of the corporation tax before tax credits. From 1 October, 2014, a part of inhabitant tax has been moved to national tax regime as ‘local corporate tax’.

Each prefecture and municipality may elect an Inhabitants Tax rate within the range shown below:

Details	Rates
Prefecture	3.2% to 4.2%
Municipality	9.7% to 12.1%
Tokyo Metropolitan (combined)	12.9% to 16.3%

In addition to the above, local governments charge a per capita levy on inhabitants with standard rates that vary from JPY 70,000 to JPY 3,800,000 depending upon the amount of the paid-in capital and the number of employees.

ENTERPRISE TAX

Prefectures can elect to levy an Enterprise Tax. The tax base is business income and liquidation income as computed for corporation tax purposes, with certain adjustments such as the exclusion of income from a business carried on in a foreign country. Enterprise Tax is deductible in computing taxable income for corporation and Enterprise Tax purposes.

Size-based taxation has been newly introduced and this taxation is applied only to large corporations with paid-in capital of more than JPY 100 million and for the business years beginning on or after 1 April 2004. For such large corporations, Enterprise Tax consists of the traditional Enterprise Tax levied based on the taxable income and the newly introduced Enterprise Tax levied based on the capital etc. (i.e. paid-in capital and capital surplus) and value added (i.e. wages, interest and rental expenses).

Tax rates vary depending on whether or not the corporation is a large corporation with paid-in capital of more than JPY 100 million and depending on the prefecture:

Taxable periods beginning after 1 October 2014:

			Standard (%)	Maximum (%)	Local Corporate Special Tax
(1)	**Company whose paid-in capital is JPY100 million or less**				
	Taxable Income:				
		First JPY 4,000,000 per annum	3.4	3.65	(Taxable Income*Tax rate)*43.2%
		Next JPY 4,000,000 to JPY 8,000,000 per annum	5.1	5.465	
		Above JPY 8,000,000 per annum	6.7	7.18	
(2)	**Company whose paid-in capital is more than JPY 100 million**				
	(a)	Income base (taxable income):			
		First JPY 4,000,000 per annum	2.2	2.39	(Taxable Income*Tax rate)*67.4%
		Next JPY 4,000,000 to JPY 8,000,000 per annum	3.2	3.475	
		Above JPY 8, 000,000 per annum	4.3	4.66	
	(b)	Added value base:			
		The sum of wages, net interest expense and net rental expense	0.48	0.504	0.504
	(c)	Capital base:			
		The sum of paid-in capital and capital surplus	0.2	0.21	0.21

OTHER TAXES
FAMILY HOLDING COMPANY SURTAX

Family holding companies are liable for surtax on earnings not distributed in excess of specified limits at the following rates:

Excess Income	Rates
First JPY 30,000,000 per annum	10%
Next JPY 70,000,000 per annum	15%
Over JPY 100,000,000 per annum	20%

A Japanese company in which more than 50% of the shares are held by the first shareholders' group is a family holding company and is subject to the surtax.

A family holding company with paid-in capital of JPY 100 million or less (when its 100% parent company's stated capital is JPY 500 million or more, 'Intra-group transaction taxation' in the year of 2010 tax reform takes away this benefit) whose net equity is 50% or less of its total assets is not subject to this special corporate surtax for accounting periods which begin on or after 1 April 2003 but before 1 April 2006.

BUSINESS OFFICE TAX

Companies whose business premises exceed 1,000 square meters and / or employ in excess of 100 employees in designated cities are subject to a tax on business activity based on space or gross payroll respectively. It is within the discretion of the city authorities whether or not to charge the tax. Additions can be made to the list of designated cities for the purpose of this tax but the city must have a population of at least 300,000. The tax is imposed on:

(a) Construction or extension of business premises (a one-time payment due from the owner of the building);

(b) Ongoing businesses.

The rate of tax is JPY 600 per square meter of floor space in business use plus 0.25% of the total remuneration paid to employees.

FIXED ASSETS TAX

Real property and tangible depreciable fixed assets are subject to a fixed assets tax at the standard rate of 1.4% with an upper limit of 2.1% (1.7% for real property in specified large cities).

LANDHOLDING TAX

Landholding tax is also levied at the national and municipal level.

TOTAL EFFECTIVE TAX RATE

By way of example of how the major taxes interrelate and accumulate, set out below is a sample effective tax rate calculation for a Japanese or foreign corporation having paid-in capital of JPY 100 million or less.

	Rate (%) (until March, 2014)	Rate (%) (from April, 2014)
Effective tax rate	38.01	35.64

Note: Enterprise Tax is deductible for corporation tax purposes for the period in which it is paid.

B. DETERMINATION OF TAXABLE INCOME

Income is ordinarily determined in accordance with generally accepted accounting principles, with certain adjustments made to comply with the tax law. Income and expenses are recorded on an accruals basis, with deductions from gross income for all reasonable expenses, costs and losses.

Restrictions apply to the deduction of entertainment expenses.

DEPRECIATION

Depreciation is allowed in respect of all tangible assets, other than land and specified intangible assets. Depreciation on tangible assets is calculated using the straight-line or declining-balance method at the option of the taxpayer. However, for buildings, only straight-line method may be used. Intangible assets are generally amortised on a straight-line basis.

The legislation specifies the period over which assets are to be depreciated and the rates for both the straight-line and declining-balance methods. Minor assets that cost JPY 100,000 or less are deductible as an expense. In addition to ordinary depreciation, special depreciation in the form of increased initial depreciation and accelerated depreciation is available in certain cases.

STOCK / INVENTORY

Inventory valuation methods acceptable for tax include an item's individual cost, FIFO, moving or straight average, most recent purchase, retail and lower of cost or market. Importantly, the tax treatment must replicate that adopted for the statutory accounts.

LOSSES

Corporations filing a ‘Blue Return’ are eligible for loss carry-over treatment. In general, losses may be carried forward seven years (nine years from April 2012; however for large scale companies, use of the losses is restricted to 80% of taxable income for each year) or carried back one year.

The carry-back provisions have been suspended for accounting periods ending after 1 April 1992. However, a Blue Return status corporation with paid-up capital of JPY 100 million or less (except for a subsidiary of a large scale company) can carry back a net loss incurred in a business year to the previous year.

The loss is limited to the loss incurred for each business year within the five years after the initial business year.

FOREIGN SOURCE INCOME

Japanese corporations are taxable on their worldwide income when earned. However, corporations are generally entitled to claim tax credits against corporation and Inhabitants Tax for foreign income taxes paid (direct credit).

For subsidiaries in low or nil tax countries or jurisdictions whose profits are not distributed, such profits are taxed in the hands of the Japanese parent on an accruals basis, with any associated foreign tax credits being available.

OVERSEAS INVESTMENT

Japanese corporations investing in certain companies involved with developing countries or in prospecting for or developing natural resources may be able to establish a tax deductible reserve of 30% or 90% of the amount invested.

After the reserve has been maintained for five successive years, the amount of reserve multiplied by the number of months of the business year, divided by 60, must be restored to taxable income in succeeding years following the year of reserve accrual.

TAX CREDIT INCENTIVES – CAPITAL INVESTMENT

Corporate tax credits of 7% of the acquisition cost are available on designated energy efficient machinery and equipment acquired by small to medium sized corporations. The total credit available, however, is limited to 20% of the corporate tax.

The credit was only applied to qualifying capital equipment acquired by 31 March 2016.

C. FOREIGN TAX RELIEF

Relief is available for foreign taxes on foreign source income and capital gains whether or not Japan has concluded a tax treaty with the foreign country. Where a tax treaty exists it will specify the method of relief. In the absence of a treaty, the domestic Japanese tax legislation allows a tax credit or deduction from taxable income.

Under Japanese domestic law, foreign taxes not eligible for foreign tax credits are deductible. Treaties following the OECD model normally provide relief in the form of either a credit or exemption from tax.

D. CORPORATE GROUPS

The Japanese consolidated tax regime (a part of the corporate tax reform act for the year 2002) was enacted on 1 August 2002. The revised Corporate Tax Law and the Corporate Tax Law Enforcement Order are applicable to consolidated years ending on or after 31 March 2003, with transitional rules in respect of consolidated years beginning between 1 April 2002 and 30 June 2003, and ending on or after 31 March 2003.

Under the consolidated tax regime, an affiliated group of companies (a 'Consolidated Group') can report and pay national corporate income tax as one unit. For these purposes, a Consolidated Group means a Japanese parent company and its 100% directly or indirectly owned Japanese subsidiaries. An application for consolidated filing is at the tax payers' choice but, if made, must include all of the parent's eligible subsidiaries. Once started, consolidated filing should in principle continue indefinitely, unless a specific event (such as change of ownership) causes the qualifying conditions for consolidated filing to be failed, or an application to discontinue is approved by the Commissioner of National Tax Administrative Agency.

The group's national corporate income tax liability will be computed on a consolidated basis by aggregating the separate taxable income or loss of the member companies, and then making various consolidation adjustments. The consolidated national corporate income tax liability will then be determined by applying the normal corporate income tax rate to the consolidated taxable income, adjusted for consolidated tax credits. The total liabilities will then be allocated among the members. The parent company will file the consolidated return and pay the national corporate income tax on behalf of the group, although the member companies remain jointly and severally liable for the Consolidated Group's national corporate income tax liability. Local corporate income taxes levied on member companies will continue to be paid on an individual basis although the amount payable will be affected by the existence of the consolidation.

The consolidation tax regime provides for certain benefits such as the deduction of losses of individual member companies from the total income of the Consolidated Group (for national corporate income tax purposes only); deferral of gains on intra-group transfers of certain assets; and non-taxability of the dividends received from other member companies (regardless of the interest expense attributable to the dividend income). On the other hand, some features of the consolidated tax regime may result in an unpredictable tax burden on the introduction of tax consolidation or when a company joins the Consolidated Group in the future, thus putting some restrictions on future M&A (mergers and acquisitions) activity by the group. Therefore, understanding these issues will become very important for tax professionals and taxpayers when considering an application for consolidation.

A company with registered capital of JPY 100 million or less can take various preferential tax treatments (for example, reduced tax rate for first JPY 8 million of income, one year loss carry back), however, ‘Intra-group transaction taxation’ in the year 2010 tax reform takes away such tax benefits when its 100% parent company’s stated capital is JPY 500 million or more.

E. RELATED PARTY TRANSACTIONS

All transactions between related companies are required to be conducted on an arm's length basis with the meaning of ‘arm's length price’ depending upon the transaction. Any difference arising between the price of the actual transaction and that regarded as the arm's length price is taxable or not deductible as applicable. The transactions covered by the provisions include the purchase and sale of inventory, the provision of services and financial facilities such as the making of loans and guarantee facilities.

F. WITHHOLDING TAXES

Domestic corporations are subject to 20% withholding tax on dividends and interest and certain other income. Foreign corporations are subject to withholding tax (generally at the rate of 20%) on dividends, interest, royalties, income from immovable property, rentals from industrial or commercial equipment and certain other income.

This tax may generally be taken as a credit against the ultimate tax liability of the recipient. It should be noted that where the foreign corporation has a permanent establishment in Japan, certain types of income (for example, rent and royalties) are exempt from withholding tax if taxed together with income from Japanese business income.

As indicated, the tax may generally be taken as a credit against the ultimate tax liability of the recipient. However, no tax credit is allowed for income tax withheld on dividends in the case of foreign corporations.

G. PERSONAL TAX

While similarities between the taxation of companies and individuals do exist in Japan, the above refers largely to companies. Accordingly, outlined below are the basic rules and rates applicable to individuals. Given the complexity of this area, it is necessary to stress the need to seek professional advice.

Non-resident taxpayers are taxed only on their Japanese source income. Non-permanent resident taxpayers are taxed on both Japanese source income plus that part of non-Japanese source income that is paid in and/or remitted to Japan. A permanent resident taxpayer is taxed on his worldwide income.

Individuals are generally classified on the following basis:

Period of Residence	Classification
Up to 12 months	Non-resident
12 months to 60 months	Non-permanent resident
More than 60 months	Permanent resident

National individual tax:

Taxable income (JPY)	Rate	Deduction (JPY)
0–1,950,000	5%	---
1,950,000–3,300,000	10%	97,500
3,300,000–6,950,000	20%	427,500
6,950,000–9,000,000	23%	636,000
9,000,000–18,000,000	33%	1,536,000
18,000,000-40,000,000	40%	2,796,000
Above 40,000,000	45%	4,796,000

Calculation: Taxable income × tax rate –deduction = national tax.

In response to the need for additional funds to deal with the aftermath of the earthquake in 2011, a surcharge of 2.1% of the national personal tax liability has been added to the national personal tax rate for 25 years from January 2013.

Retirement income, interest and timber income are each taxed separately from other income.

H. TREATY WITHHOLDING TAX RATES

	Dividends[1] (%)	Interest (%)	Royalties (%)
Treaty countries:			
Armenia	15/0	10	0/10
Australia	10/5/0	10	5
Austria	20/10	10	10
Azerbaijan	15/0	10	0/10
Bahamas	–[2]	–[2]	–[2]
Bangladesh	15/10	10	10
Belarus	15/0	10	0/10
Belgium	15/10	10	10
Bermuda	–[2]	–[2]	–[2]
Brazil	12.5/0	12.5	12.5/15/25
Brunei	10/5	10	10
Bulgaria	15/10	10	10
Canada	15/5	10	10
Cayman	–[2]	–[2]	–[2]
China	10/0	10	10

	Dividends[1] (%)	Interest (%)	Royalties (%)
Czech Republic	15/10	10	0/10
Denmark	15/10	10	10
Egypt	15	–[2]	15
Fiji	–[2]	–[2]	10
Finland	15/10	10	10
France	10/5/0	10	0
Georgia	15/0	10	0/10
Germany	15/10	10	10
Guernsey	–[2]	–[2]	–[2]
Hong Kong	10/5	10	5
Hungary	10/0	10	0/10
India	10/0	10	10
Indonesia	15/10	10	10
Ireland	15/10	10	10
Isle of Mann	–[2]	–[2]	–[2]
Israel	15/5	10	10
Italy	15/10	10	10
Jersey	–[2]	–[2]	–[2]
Kazakhstan	15/5	10	5
Korea, Republic of	15/5	10	10
Kuwait	10/5	10/0	10
kyrgyzstan	15/0	10	0/10
Liechtenstein	–[2]	–[2]	–[2]
Luxembourg	15/5	10	10
Macau	–[2]	–[2]	–[2]
Malaysia	15/5	10	10
Mexico	15/0/5	10/15	10
Moldova	15/0	10	0/10
Netherlands	10/5/0	10	0
New Zealand	15/0	10/0	5
Norway	15/5	10	10
Oman	10/5	10	10
Pakistan	5/7.5/10	10	10
Philippines	15/10	10	15/10
Poland	10/0	10	0/10
Portuguese	10/5	10/5/0	5
Romania	10/0	10	10/15
Russia	15/0	10	0/10
Samoa	–[2]	–[2]	–[2]
Saudi Arabia	10/5	10/0	5/10

	Dividends[1] (%)	Interest (%)	Royalties (%)
Singapore	15/5	10	10
Slovak Republic	15/10	10	0/10
South Africa	15/5	10	10
Spain	15/10	10	10
Sri Lanka	20/0	-	0/7.5
Sweden	10/0	10/0	0
Switzerland	10/5/0	10	0
Tajikistan	15/0	10	0/10
Thailand	20/15	10/25	15
Turkey	15/10	10/15	10
Turkmenistan	15/0	10	0/10
UAE	10/5	10	10
Ukraine	15/0	10	0/10
United Kingdom	10/0/5	10	0
United States	10/0/5	0/10	0
Uzbekistan	15/0	10	0/10
Vietnam	10/0	10	10
Virgin Island	–[2]	–[2]	–[2]
Zambia	0	10	10

NOTES

1. The lower rate applies to dividends paid to foreign corporations that own a particular percentage of share capital or voting power in the Japanese company paying the dividend. Please refer to the relevant treaty to determine the exact conditions required for the lower rate to apply.

2. The domestic rate applies – there is no rate specified in the treaty.

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