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Japan

Last Reviewed - 17 August 2019

Overview

Japan, a nation in East Asia, is an archipelago of 6,852 islands in the Pacific Ocean. It is a constitutional monarchy, with Tokyo as its capital. More than 99% of the population speaks Japanese. The economy of Japan is the third largest in the world after the United States and the People's Republic of China. Japan's currency is the yen (JPY).

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Corporate - Significant developments

Last Reviewed - 18 August 2019

2019 Tax Reform

On 27 March 2019, the 2019 Tax Reform Act was approved by the Diet, and, on 29 March 2019, the 2019 Tax Reform Act, the Enforcement Orders, and Regulations were promulgated, which are effective for corporate tax years ending on or after 1 April 2019, in principle. The 2019 Tax Reform Act provides for tax measures to promote investment in innovation and to encourage investment by small to medium size enterprises (SMEs) in improving business productivity.

In addition, the 2019 Tax Reform Act includes amendments consistent with the recommendations of the Organisation for Economic Co-operation and Development's (OECD's) Base Erosion and Profit Shifting (BEPS) Action Plan, with the stated purpose of supporting the global expansion of Japanese companies while limiting tax avoidance.

Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS (MLI) becomes effective for Japan

On 1 January 2019, the MLI entered into force for Japan. As of 1 July 2019, 15 jurisdictions, which are among the Japanese covered convention, deposited the instrument of ratification, acceptance, or approval of the Convention, and for 12 jurisdictions, the MLI entered into force.

Consumption tax

Due to a tax amendment, the consumption tax increase that was originally scheduled to rise to 10% on 1 April 2017 was delayed to 1 October 2019; however, concessions have been introduced with lower rates for selected goods to lessen the burden for the lower income tax brackets. To cope with the multiple consumption tax rates, an invoicing method will be introduced, although not until 1 April 2023, with transitional measures in place for the three-year and six months interim.

Corporate - Taxes on corporate income

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A domestic corporation in Japan is taxed on its worldwide income, including foreign branch income, while 95% of dividends received by a company from a foreign company in which it has held at least 25% (or could be lower under relevant tax treaties) of the outstanding shares for a continuous period of six months or more can be excluded from the company's taxable income. *See the description of Dividend income in the Income determination section for more information*.

A foreign corporation is taxed only on its Japan-source income. A foreign corporation with a permanent establishment (PE) in Japan is liable for corporate income taxes only on the income attributable to the PE.

Corporation tax

The corporation tax rates are provided in the table below (effective from fiscal years beginning on or after 1 April 2016 and 1 April 2018).

Company size and income	Corporation tax rate (%)	
	1 April 2016	1 April 2018
Paid-in capital of over 100 million Japanese yen (JPY)	23.4	23.2
Paid-in capital of JPY 100 million or less, except for a company wholly owned by a company that has paid-in capital of JPY 500 million or more:		
First JPY 8 million *per annum*	15.0	15.0
Over JPY 8 million *per annum*	23.4	23.2

National local corporate tax

Beginning from 1 October 2019, corporate taxpayers are required to file and pay the national local corporate tax at a fixed rate of 10.3% of their corporate tax liabilities. Currently, the national local corporate tax rate is 4.4%.

Standard enterprise tax (and local corporate special tax)

Enterprise tax is imposed on a corporation's income allocated to each prefecture. This allocation is generally made on the basis of the number of employees and number of offices in each location. The local corporate special tax, which is a rate multiplied by the income portion of enterprise tax, will be abolished from tax years beginning on or after 1 October 2019 and replaced by the special corporate business tax (including a size-based tax regime) by the 2019 Tax Reform.

Similar to the local corporate special tax, the special corporate business tax will be levied on the tax amount of the local business tax (income portion) and collected by the local government. However, under the local corporate special tax, the local corporate tax rate, for tax years beginning on or after 1 October 2019, will be decreased as follows.

The standard rates of enterprise tax, including local corporate special tax, are shown below.

	2015 Tax Reform	2019 Tax Reform

	2016 Tax Reform	2019 Tax Reform
	Fiscal year beginning 1 April 2016 thru 30 September 2019	Fiscal year beginning 1 October 2019
Enterprise tax *:		
First JPY 4 million	5.0% (3.4%)	3.5% (2.5%)
Next JPY 4 million	7.3% (5.1%)	5.7% (4.1%)
Over JPY 8 million	9.6% (6.7%)	7.0% (5.1%)
Local corporate special tax or special corporate business tax (the rate is multiplied by the income base of size-based enterprise tax), which is collected as national tax by filing corporate tax returns	43.2%	37.0%

* Tax rates shown in parentheses do not include local corporate special tax or special corporate business tax.

If the paid-in capital of a corporation is JPY 10 million or more and the corporation has place of business in more than two prefectures, the graduated rates above are not applicable.

For utilities and insurance companies, the standard tax rate is shown as follows:

	Fiscal year beginning prior to 30 September 2019	Fiscal year beginning 1 October 2019
Enterprise tax	0.9%	1.0%
Local corporate special tax or special corporate business tax	43.2%	30.0%

Size-based enterprise tax (and local corporate special tax)

Instead of the above general enterprise tax, a ‘size-based’ enterprise tax (*Gaikei Hyojun Kazei*) is applied to a company whose paid-in capital is more than JPY 100 million as of the year-end.

Factors such as the size of a corporation’s personnel costs and its capital (the amount of paid-in capital) will determine the additional amount of tax payable. The existing profit-based enterprise tax will also continue to apply at the tax rates indicated below. Therefore, a loss company in Japan may be required to pay tax based on value-added activities and the corporation’s paid-in capital.

The applicable standard rates are as follows:

Taxable base	Size-based enterprise tax (%)	
	2015 Tax Reform	2019 Tax Reform

Taxable base	Size-based enterprise tax (%)		
	2015 Tax Reform		2019 Tax Reform
	Fiscal year beginning prior to 31 March 2016	Fiscal year beginning 1 April 2016 thru 30 September 2019	Fiscal year beginning 1 October 2019
Value added base	0.72	1.2	1.2
Capital base	0.3	0.5	0.5
Income base *:			
First JPY 4 million	3.1 (1.6)	1.9 (0.3)	0.4 (0.11)
Next JPY 4 million	4.6 (2.3)	2.7 (0.5)	0.7 (0.19)
Over JPY 8 million	6.0 (3.1)	3.6 (0.7)	1.0 (0.27)
Local corporate special tax or special corporate business tax (the rate is multiplied by the income base of size-based enterprise tax), which is collected as national tax by filing corporate tax returns	93.5	414.2 **	260.0

* The rate shown for the income base is the total income-based tax including (i) the portion collected as part of the national tax return and (ii) the portion included as part of the enterprise tax return. The portion in parentheses of the income base column shows the amount collected as an enterprise local tax (the difference is collected as a national tax). The above rate changes for income base may not affect taxpayers who have elected consolidated taxation since consolidation is not applicable for local tax purposes. Tax rates shown in parentheses do not include local corporate special tax or special corporate business tax.

** The local corporate special tax will be abolished from 1 October 2019 and replaced with special corporate business tax.

Inhabitant's tax

Inhabitant's tax is imposed on a corporation's income allocated to each prefecture and city (municipal borough). The allocation is generally made on the basis of the number of employees, in the same way as enterprise tax.

The standard tax rate is 3.2% as prefectural tax and 9.7% as municipal tax. However, the tax rate is increased to 4.2% for prefectural tax and 12.1% for municipal tax, depending upon the determination of each local government. From fiscal years beginning on or after 1 October 2019, the rate is increased as follows:

Inhabitant's tax	Current		Expected from 1 October 2019	
	Standard rate (%)	Maximum rate (%)	Standard rate (%)	Maximum rate (%)
Prefectural tax portion	3.2	4.2	1.0	2.0
Municipal tax rate	9.7	12.1	6.0	8.4

Local corporate tax rate	4.4	10.3

In addition to the above, inhabitant's tax is imposed on a *per capita* basis, in the range from JPY 70,000 (in cases where the amount of paid-in capital is JPY 10 million or less and the number of employees in each prefecture and city is 50 or less) to JPY 3.8 million (in cases where the amount of paid-in capital is over JPY 5 billion and the number of employees in each prefecture and city is over 50). The inhabitant's tax amount is determined by the local government by the factors of paid-in capital and the number of employees.

Effective tax rate

The total corporate income tax burden (i.e. effective tax rate) varies depending upon the size of a company's paid-in capital. Since enterprise tax is deductible, the effective tax rate is less than the total of the statutory rates of corporation tax, inhabitant's tax, and enterprise tax.

The following is the summary of the effective applicable tax rates in the case of large corporations operating in Tokyo (taking no thought of an additional-value-based tax and capital-based tax out of the enterprise tax above):

	Effective tax rate (%)	
	Fiscal year beginning on or after 1 April 2018	**Fiscal year beginning on or after 1 October 2019**
Corporate tax	23.2	23.2
Local corporate tax	1.021 (23.2% x 4.4%)	2.390 (23.2% x 10.3%)
Enterprise tax	0.88	3.779 **
	Local corporate special tax or special corporate business tax	2.899 (0.7% x 414.2%)
Inhabitants' tax	3.782 (23.2% x 16.3%)	2.413% (23.2% x 10.3%)
Total	31.782	31.782 **
Effective tax rate *	30.62	30.62 **

* Effective tax rate is calculated after deducting the enterprise tax (including local corporate special tax or special corporate business tax).

** As of 1 July 2019, the applicable enterprise tax rate and special corporate business tax rate is not released by the Tokyo Metropolitan Government.

Corporate - Corporate residence

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Domestic and foreign corporation

A company that has its head office in Japan is a domestic corporation. The nationality of its shareholders or place of central management is not relevant.

A corporation other than a domestic corporation is regarded as a foreign corporation.

Permanent establishment (PE)

Under domestic tax law, the scope of Japan-source income in respect of which a foreign corporation is taxable depends upon the type of taxable presence that it has in Japan. Pursuant to the amendments of Article 5 of the OECD Model Tax Treaty (OECD MTC) in November 2017 and the signing of the MLI on 7 June 2017 by the Japanese government, articles related to the PE were revised by the 2018 Tax Reform. The articles of the Corporate Tax Law (CTL) and CTL Enforcement Ordinance (CTLEO) were revised to agree with the updated Article 5 of the OECD MTC. The revised definition of PE will apply to the tax years beginning on or after 1 January 2019. After the amendment, the types of taxable presence that a foreign corporation may have in Japan include the following:

- Branch, factory, other fixed places in which business is conducted in Japan, mine, quarry, building for rent, etc., but exclude a specified place used only for the purpose of storage, display, or delivery of goods or merchandise belonging to the enterprise and any other activity of a preparatory or auxiliary character (Direct PE).
- Construction, installation, assembly project, or supervisory services related thereto for a period of greater than one year, but exclude a specified place used only for the purpose of storage, display, or delivery of goods or merchandise belonging to the enterprise and any other activity of a preparatory or auxiliary character (Construction PE).
- A person other than an agent of an independent status (i.e. Agent PE) acting in a contracting state on behalf of an enterprise and has, and habitually exercises, in a contracting state, an authority to conclude contracts, in doing so, habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise, and these contracts are:
    - in the name of the enterprise
    - for the transfer of the ownership of, or for the granting of the right to use, property owned by that enterprise or that the enterprise has the right to use, or
    - for the provision of services by that enterprise.

In the above case, the enterprise shall be deemed to have a PE in that state in respect of any activities that person undertakes for the enterprise, unless the activities of such person are limited to preparatory or auxiliary character.

If a person acts exclusively or almost exclusively on behalf of one or more enterprises to which it is closely related, that person shall not be considered to be an independent agent.

As a matter of law, the articles of Japan's tax treaties have precedence over domestic tax law. By the amendments of the definition of PE under the domestic law, there may be some difference in the scope of PE from that of the existing tax treaties. Under the circumstances, the articles of the relevant tax treaties will override the above articles. Once a PE has been established for a foreign corporation under domestic law, all Japan-source income is taxable to the PE to the extent it is 'attributable to' the PE.

Corporate - Other taxes

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Consumption tax

Consumption tax (value-added tax or VAT) is levied when a business enterprise transfers goods, provides services, or imports goods into Japan. The applicable rate is 8%. As of 1 October 2019, the rate will increase to 10%. Exports and certain services to non-residents are taxed at a zero rate. Specified transactions, such as sales or lease of land, sales of securities, and provision of public services, are not subject to taxation.

Consumption tax paid by the business enterprise attributable to taxable revenue shall be creditable/refundable by filing the consumption tax return to the extent that such transaction is recorded in the accounting book and relevant invoices are kept.

In response to the increase in consumption tax rate to 10% from 1 October 2019, lower consumption tax rates on certain goods will be introduced. Also, in response to the multiple tax rates, an invoice system will be introduced from 1 April 2023. In the three-year and six months transitional period to the introduction of an invoice system, several measures will be implemented.

The lower consumption tax rate of 8% will still apply to food (excluding when purchased in restaurants) along with newspaper subscriptions where there is at least an issue twice per week. Until the invoice system is introduced, the credit for consumption taxes paid will follow the current method for tracking, where the lower tax rate on applicable items should be indicated in the invoice. With the increased administration cost of tracking the different rates, the simplified method of determining consumption taxes paid will be allowed.

After the new invoice system is introduced, qualified invoices issued by the registered businesses should be maintained for claiming credits of consumption taxes paid. Businesses (other than exempt entities) will need to file an application with their tax office to become qualified for issuing qualified invoices indicating details such as the business registration number, the applicable tax rate, etc.

Note that consumption tax is also imposed on the cross-border provision of digital services (e.g. e-books, music, and advertising) by foreign service providers. In this respect, a reverse-charge mechanism is applicable for business-to-business (B2B) transactions, and foreign service providers may need to register for consumption tax purposes with regard to business-to-consumer (B2C) transactions.

Also, Japanese sponsors are subject to a reverse-change system for sports or music/art attractions in Japan provided by foreign entertainment providers.

Customs duty

A customs duty is levied on imported goods based on the custom tariff table.

Excise taxes

Excise taxes are levied on gasoline, aviation fuel, tobacco, and liquor.

Fixed assets tax

The annual fixed assets tax is levied by the local tax authorities on real property and depreciable fixed assets used for business purposes. Real property is taxed at 1.7% (standard rate including city planning tax) of the value appraised by the local tax authorities. The depreciable fixed assets tax is assessed at 1.4% of cost after statutory depreciation.

Stamp duty

A stamp duty is levied on certain documents prepared in Japan. The tax amount is generally determined based on the amount stated in the document. The maximum amount of stamp duty is JPY 600,000.

Registration and licence tax

Registration and licence tax is levied where certain property is registered, at a rate from 0.1% to 2% of the taxable basis or at a fixed amount. The taxable basis depends upon the property being registered (e.g. the amount of paid-in capital registered by a company or the value of real estate as assessed by local tax authorities).

Payroll taxes

In general, the employer has an obligation to withhold payroll taxes monthly, and for annual year-end adjustment.

Labour and social insurance paid by employer

There are four types of insurance systems in Japan that enterprises employing workers that meet certain conditions must enrol in. Workers' accident compensation insurance is borne entirely by the employer. Employment insurance, health insurance/nursing care insurance, and employees' pension insurance is born by both the employer and employee.

The employer is generally liable to pay a share of the following contributions on salary or bonus, including fringe benefits, to be paid in Japan. The employer's share consists of the following contributions:

Contribution	Standard premiums on monthly salary	Standard premiums on bonus
Health insurance for the Metropolis of Tokyo (each prefecture has its own health insurance rate, and rates are slightly higher for individuals between the ages of 40 and 65)	5.815% (on a maximum of JPY 1,390,000 of wages per month)	5.815% (on an annual cap of JPY 5.73 million of irregular annual total payments)
Welfare pension, plus child allowance (1)	9.15% (on a maximum of JPY 620,000 of wages per month)	9.15% (on a maximum of JPY 1.5 million of irregular payments per month)
Employment insurance	0.6%	0.6%
Total (2)	15.565%	15.565%

Notes

1. The rate of 9.15% for welfare pension will be applied from April 2019. Premiums on child allowance will be imposed separately at 0.34%.
2. In addition, workers' accident compensation insurance will be imposed. The rate varies depending on the type of business.

Family corporation tax

If an individual shareholder together with family members own, either directly or indirectly, more than 50% of the total issued shares or voting rights of a Japanese corporation, the corporation is treated as a family corporation (with the exception of corporations with paid-in capital of JPY 100 million or less) and is subject to the family corporation tax in addition to corporation tax.

A family corporation is liable for an additional tax at the rates shown below on its undistributed current earnings in excess of specified limits.

Taxable undistributed current earnings	Family corporation tax rate (%)
First JPY 30 million *per annum*	10
Next JPY 70 million *per annum*	15
Over JPY 100 million *per annum*	20

Business premises tax

Business premises tax is levied and designated by each city in Japan, such as Tokyo, Osaka, Nagoya, Fukuoka, and other cities with a population of more than 300,000. A company that uses business premises in excess of 1,000 square metres and/or has more than 100 employees in a designated city is responsible to pay this tax based on the usage of the business (JPY 600 per square metre) and gross payroll (0.25% of gross payroll).

Corporate - Branch income

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Branch profits are taxed in the same manner as corporate profits. However, the family corporation tax does not apply to a branch of a foreign corporation. In addition, no withholding tax (WHT) is imposed on the repatriation of branch profits to the home office.

Corporate - Income determination

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The taxable income of a corporation is the aggregate income from all sources. There is no specific requirement to differentiate between the types of income. In principle, accounting for tax purposes follows Generally Accepted Accounting Principles (GAAP) in Japan, and income of a corporation is determined on an accrual basis.

Inventory valuation

Inventory cost should be determined by applying one of the following methods accepted for corporate tax purposes: actual individual cost, first in first out (FIFO), weighted average, moving average, most recent retail, selling price reduction, and lower of cost or market.

Capital gains

Capital gains and losses are classified as ordinary income and losses, respectively.

Under certain circumstances (e.g. qualified reinvestment, exchange property), taxes generally levied on capital gains may be deferred (i.e. provided rollover relief) as long as certain requirements are met. A special relief is available in the case of expropriation of real property by either the national or local government.

The recognition of capital gains or losses from the transfer of certain assets between group companies are to be deferred until the asset is transferred to another group company or a non-group company.

Dividend income

The threshold ownership percentage for corporate dividend exclusion is illustrated in the following table.

The holding period of six months or more until the fiscal year-end for which the dividend will be paid is required to apply the dividend income exclusion for the ownership of more than 1/3 to 100%. The dividend income exclusion for an 'other domestic corporation' and 'portfolio investment' is allowed by reference to the ownership percentage as of the fiscal year-end for which the dividend will be paid.

Type of investment	Ownership %	Exclusion %
Wholly owned domestic subsidiary	100%	100%
Affiliated domestic corporation	More than 1/3	100% less allocable interest (1)
Other domestic corporation	More than 5% but less than 1/3	50%
Portfolio investment	Less than 5%	20% (2)
Exchange trust fund (ETF)		20% (treated as a portfolio investment)
Other investment trusts		0%

Notes

1. Under certain simplified calculations to determine allocable interest, the 'base period' is the fiscal years beginning between 1 April 2015 and 31 March 2017.
2. For dividends from portfolio investments received by insurance companies, the exclusion percentage will be 40%.

95% of dividends received by a company from a foreign company in which it has held at least 25% of the outstanding shares for a continuous period of six months or more, ending on the date on which the dividend is declared, can be excluded from the company's taxable income.

If the foreign company is resident in a country with which Japan has concluded a tax treaty for the avoidance of double taxation, and such treaty provides for the allowance of an indirect foreign tax credit for taxes paid by the foreign company on the profits out of which the dividend is paid where the company holds a certain percentage of the foreign company's outstanding shares (e.g. 10% based on the tax treaty between the United States [US] and Japan), that percentage will apply for the purpose of determining the availability of the above exemption to the extent that it is lower than 25%.

The BEPS Action Plan 2 proposed that measures be taken to neutralise the tax effects of so-called 'hybrid mismatch' arrangements where, because of differences in the treatment of certain payments between jurisdictions, an item of income is not taxed in either the payer or the payee country because the payment is deductible in the payer country but not taxable in the recipient country. Thus, the recommendation in the BEPS Action Plan is to modify local tax law in order for the recipient country to tax the receipt.

Based upon the recommendation of the BEPS Action Plan 2, the 2015 Tax Reform Act excludes such types of dividends from the dividend exclusion regime. As a result, any dividends paid to Japanese corporate taxpayers under so-called 'mandatorily redeemable preferred shares' (MRPS) issued by Australian affiliates or by Brazilian affiliates where the dividends are paid in a manner similar to interest and deductible for Brazilian tax purposes will no longer be excluded from taxation in Japan.

To the extent any portion of the dividend is deductible for foreign tax purposes, the general principle is that all of the dividend should be taxable in Japan. However, if a portion of the dividend is not tax deductible in the foreign jurisdiction, dividend exclusion will be allowed only if the taxpayer discloses all of the appropriate information regarding the portion of the dividend that is not deductible in the foreign jurisdiction and backup details for the calculation in a timely filed tax return and maintains the relevant documents for inspection by the tax authorities.

Any foreign tax imposed on the taxable dividend in Japan will be eligible for foreign tax credit relief.

The new rules apply for any dividends received by a Japanese corporate taxpayer whose fiscal year began on or after 1 April 2016. However, if the Japanese corporate taxpayer owned the stock of the foreign affiliate as of 1 April 2016, dividends received for years beginning between 1 April 2016 and 31 March 2018 will be subject to the old rules (i.e. still eligible for exclusion).

The WHT for dividends is applicable at a rate of 15% national tax and 5% local tax or 20% (national tax) depending on the type of stock from which the dividends were received, and a tax credit may also be available for such WHT. The WHT (national tax) is subject to the income surtax of 2.1%, which is levied for the income earned for the period from 1 January 2013 through 31 December 2037.

Interest income

Interest received is included in taxable income. The WHT for interest is applicable at a rate of 15% national tax and 5% local tax, and a tax credit may be available for such WHT. As with dividend income, the WHT (national tax) is subject to the income surtax of 2.1%, which is levied for the income earned for the period from 1 January 2013 through 31 December 2037.

Royalty income

Royalty income is subject to the corporate taxation in the same manner as other income.

Foreign income

A Japanese corporation is subject to Japanese corporate income taxes on its worldwide income. However, to avoid double taxation of foreign-source income, Japanese corporations are allowed to claim a tax credit against corporation and

inhabitant's taxes for foreign income taxes paid directly. *See Foreign tax credit in the Tax credits and incentives section for more information*.

Undistributed profits of a foreign subsidiary (i.e. controlled foreign company [CFC]) to which an applicable tax rate is 30% (in case of a shell company) or 20% are included in the Japanese parent company's taxable income under certain conditions. *See Anti-tax haven (CFC) rules in the Group taxation section for more information*.

Corporate - Deductions

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Depreciation and amortisation

Depreciation is deductible in the calculation of taxable income for corporation tax purposes. Depreciable assets include tangible property (e.g. buildings, attachments to buildings, structures, machinery and equipment). Certain intangible assets are also eligible for amortisation (e.g. goodwill, patents, trademarks).

With regard to depreciation methods, a taxpayer may adopt one of the allowable methods for each of the type of depreciable property, except for buildings and structures and attachments to buildings. For selected structural improvements acquired on or after 1 April 2016, only the straight-line method will be permitted (i.e. the declining-balance accelerated depreciation method will no longer be allowed). Tangible property is generally depreciated using either the straight-line method or the declining-balance method. Intangible property is generally amortised under the straight-line method.

Useful lives for assets are set forth on the table in detail. For reference, the following is the brief table of useful lives for typical assets.

Types of assets	Useful lives (years)
Concrete buildings	21 to 50 (depending on uses)
Metal building	12 to 38 (depending on uses)
Electrical facilities and lighting	15
Heating and air conditioning	15
Motor vehicles	3 to 6 (depending on uses)
Personal computers	4
Digital telephone equipment	6
Machinery and equipment	3 to 22 (depending on uses)
Patents	8
Software	3 or 5 (depending on uses)

Start-up expenses

Start-up expenses, such as corporation organisation costs and opening costs (i.e. costs to begin business after the corporation is established), are treated as deferred assets and allowed to be amortised on a voluntary basis.

Interest expenses

Interest expenses on borrowing are deductible in the calculation of taxable income in principle. However, the interest payment to related parties in the corporate group may be disallowed to be deducted to some extent in certain cases. *See*

'Thin capitalisation' and 'Interest expense deduction limitation' in the Group taxation section.

Reserves

Reserves recorded in the books of accounts, except for reserves for doubtful receivables and return of goods not sold, are not deductible for corporate tax purposes.

Reserve for doubtful receivables

A reserve for doubtful receivables is available to SMEs, banks, insurance companies, and other similar financial corporations.

The deductibility of a reserve for doubtful receivables is limited by the following two components: (i) an estimate of irrecoverable amounts from a debtor and (ii) a calculation of the limit in the aggregate based on either the actual historical bad debt percentage or statutory percentage (reduced for large corporations), excluding the irrecoverable amount of receivable in (i) above.

Reserve for return of goods not sold

A deductible reserve for return of goods not sold is available to corporations such as publishers, wholesalers of books, and others, provided that the corporation sells the merchandise under an unconditional repurchase agreement.

Under the 2018 Tax Reform, the deductible reserve for return of goods not sold will be abolished with a transitional period (years beginning from 1 April 2021 thru 31 March 2030).

Charitable contributions

Except for certain designated donations, the tax deduction for charitable contributions is limited to certain amounts, as follows:

Donation	Deduction limit
General donation	((0.25% of capital plus capital surplus) + (2.5% of income)) x 1/4
Donation made to designated public purpose companies	((0.375% of capital plus capital surplus) + (6.25% of income)) x 1/2

Donations subject to this limitation include economic benefits considered to be given as a subsidy. Donations to foreign affiliates are not fully deductible.

In cases where a donation occurs between group companies (as defined), there will be no tax implications for either the donor or donee (i.e. no deduction for the donor and no taxation for the donee).

Directors' remuneration

The remuneration paid to directors is deductible only in the following four cases:

- Fixed monthly payments.
- Fixed payments (either cash amount or the number of shares or stock options) in accordance with an advance notice to the tax office.
- Performance bonuses, either in the form of cash, stocks, or stock options, paid in proportion to the company's performance (sales, earnings, stock value, etc.) to directors who engage in the operation of the company's business, to the extent that certain requirements are met.
- Retirement compensation (where the amount is calculated by the service period but not on a performance basis).

If the amount of remuneration is deemed unreasonable by the tax authority, only the reasonable amount is deductible for tax purposes.

Entertainment expenses

In principle, entertainment expenses are not deductible for tax purposes. However, an SME, defined as a company with paid-in capital of JPY 100 million or less (except for a company wholly owned by a company that has paid-in capital of JPY 500 million or more after the group taxation regime is effective) may take a tax deduction up to the smaller of the actual disbursement for the entertainment expense or JPY 8 million. With regard to expenses for eating and drinking, a company may deduct such expenses as far as the expense does not exceed JPY 5,000 per person (excluding expenditures for internal purposes) for tax purposes.

Corporations are able to deduct 50% of the entertainment expenses for food and drink (excluding entertainment for internal purposes).

The above treatment is applicable to the fiscal years beginning before 31 March 2020.

Fines and penalties

Fines and penalties are not deductible.

Taxes

Enterprise tax and business premises tax are deductible in the calculation of the taxable income for corporation tax purposes on a cash basis. However, corporation tax and inhabitant's tax are not deductible. Fixed assets tax and other taxes are deductible, when assessed. Foreign income taxes also may be deductible if the Japanese corporation does not elect to claim a foreign tax credit.

Net operating losses

For corporation tax and enterprise tax purposes (indirectly for inhabitant's tax purposes), a tax loss can be carried forward to offset future income in the case that a taxpayer files a 'blue form' tax return (*see Tax returns in the Tax administration section*) or if the tax loss is incurred as a result of certain disaster events.

Based on the 2016 Tax Reform Act, changes in the limitation for the net operating loss deduction will be implemented over three years. Thereafter, the limitation will be reduced to 50%, although the limitation carryover period will be extended from the current nine years to ten years for losses incurred on or after years beginning on or after 1 April 2018. SMEs are not subject to the loss deduction limitation.

	Fiscal year 2015 (1)	Fiscal year 2016	Fiscal year 2017	Fiscal year 2018
Limitation ratio for large corporations	65%	60%	55%	50% (2)
Carryover period for loss utilisation as well as assessment by tax authorities and request for downward adjustment by taxpayer (assuming loss period financial documentation is maintained)	9 years	9 years	9 years	10 years (2)

Notes

1. For fiscal years beginning on or after 1 April 2015 and before 1 April 2016 in which the taxpayer claims a net operating loss deduction.
2. Applicable to tax losses incurred in fiscal years beginning on or after 1 April 2018.

Certain newly established corporations and companies coming out of a rehabilitation process will not be subject to the loss limitation rules for a certain period.

Type of corporation applicable	Years in which full deduction is allowable	Years where regular limitation applies even if full deduction otherwise allowable

Type of corporation applicable	Years in which full deduction is allowable	Years where regular limitation applies even if full deduction otherwise allowable
Newly established corporations (1) and corporations coming out of the rehabilitation process (2)	Seven years from establishment of the corporation or seven years from the decision of the court to exit the rehabilitation process.	For years ending on or after (i) a company is listed on a stock exchange, or (ii) the company is deemed to be rehabilitated.

Notes

1. SMEs, 100% subsidiary of larger corporations, or 100% parent corporation after share transfer are excluded.
2. SMEs are excluded.

Where there is a change in ownership of a corporation followed by certain events, such as the cessation of business or a significant change in its business within a five-year period following a business acquisition, the utilisation of its tax loss is restricted.

Carryback of tax losses is generally available for one year for national corporation tax purposes. This carryback rule is suspended until the fiscal year ending 31 March 2020 (except in specified circumstances, e.g. year of liquidation).

No carryback of losses is allowed for enterprise tax and inhabitant's tax.

Payments to foreign affiliates

In order to support a deduction in Japan for expenses incurred by a foreign affiliate and charged to a Japanese corporation, in general, it should be demonstrated that the service arrangement between the foreign affiliate and the Japanese corporation satisfies arm's-length criteria for purposes of Japan's transfer pricing laws and regulations.

Generally, fees that are paid by a Japanese subsidiary to a foreign affiliate should be deductible for Japanese tax purposes if the following conditions are met:

- The services should have the same character as services that take place between non-related companies or such services are essential to Japan's activities.
- There is a written service agreement.
- The services were requested by the Japanese corporation.
- The rendering of services is documented with evidence (e.g. requests for services from the Japanese subsidiary, regular invoices sent by the foreign affiliate).
- The service charges are reasonable.

Corporate - Group taxation

Last Reviewed - 18 August 2019

Consolidated tax regime

Under the consolidated tax regime, a consolidated group can report and pay national corporate income tax on a consolidated basis. A consolidated group may be formed by a Japanese parent company and its 100% owned (directly or indirectly) Japanese subsidiaries. The taxpayer may file an application to elect a consolidated group filing for tax purposes, but the election must include all of the parent's eligible subsidiaries. Once the election is made, the consolidated filing, in principle, cannot be revoked unless there is a specific event, such as an ownership change, that causes the qualifying conditions of a consolidated filing to fail or an application to discontinue the consolidated group has been approved by the Commissioner of the National Tax Agency (NTA).

The taxable income of the consolidated group is computed on a consolidated basis by aggregating the taxable income or losses of each member of the consolidated group followed by the consolidation adjustments. Profits from intra-group transactions, except for transfer of certain assets as defined, should be included in the aggregate taxable income. Gains or losses from the intra-group transfer of certain assets are deferred.

Pre-consolidation tax losses of a subsidiary can be carried forward into a consolidated tax group if certain conditions are met, but may only be offset against taxable income of the subsidiary for the calculation of consolidation income.

The consolidated national corporate income tax liability is determined by applying the corporate income tax rate to the consolidated taxable income and adjusted for consolidated tax credits. The total tax liabilities are allocated back to each member company. The parent company files the consolidated return and pays the national corporate income tax for the group; however, each member company remains jointly and severally liable for the consolidated group's total national corporate income tax liability.

Local corporate income taxes levied on member companies are paid on a separate company basis, but the amount of local tax payable may be affected because of the consolidated filing.

Group taxation regime

A group taxation regime is applicable to domestic companies that are wholly owned by a domestic company, foreign company, or individual ('group companies'). Unlike the consolidated tax regime, the group taxation regime automatically applies to group companies.

The key points of this regime are summarised as follows:

- The recognition of capital gains or losses from the transfer of certain assets (including the transfer of assets as a result of a non-qualified or taxable merger) between group companies is deferred until the asset is transferred to another group company or a non-group company. The scope of assets is the same as that under the tax consolidation system (i.e. fixed assets, land, securities, monetary receivables, and deferred expenses [excluding securities for trading purposes and assets with a book value of less than JPY 10 million]).
- Where a donation occurs between group companies, there are no tax implications for either the donor or donee (i.e. no deduction for the donor and no taxation for the donee). Note that this treatment is not applied to a group company owned by an individual. This is consistent with the treatment of a donation between members of a consolidated tax group.
- A dividend received from a group company can be fully excluded from taxable income without any reduction for allocable interest expense. This is consistent with the treatment of dividends between members of a consolidated tax group.

A group company that would otherwise qualify as an SME on a stand-alone basis is not eligible for SME benefits (e.g. reduced corporate tax rate, preferable allowable ratios for deductible portion of bad debt provisions, partial deductibility of entertainment expenses, carryback of tax losses) if the SME is owned by a parent company or two or more parent companies of the group that has paid-in capital of JPY 500 million or more.

Where a corporation that is a member of a 100% group is in the process of liquidation and is expected to be dissolved, any loss from the impairment or devaluation of the shares of the liquidating corporation cannot be recognised by the parent company as a tax deductible expense.

Transfer pricing

If a corporation that is subject to corporation tax sells property to or buys property from a foreign-related person, or provides services or conducts other transactions with a foreign-related person, and consideration is received or paid by the corporation, the transaction is required to be carried out at an arm's-length price for corporation tax purposes.

A foreign-related person is a foreign corporation that maintains certain special relationships with the subject corporation, such as parent-subsidiary, brother-sister, or substantial control relationship.

The arm's-length price for the sale or purchase of inventory may be determined using one of the following methods:

- Comparable uncontrolled price method.

- Resale price method.
- Cost plus method.
- Berry Ratio method.
- Other method (i.e. profit split method and transactional net margin method [TNMM]).

The 'most appropriate method' should be applied in order to calculate the arm's-length price.

An advanced pricing agreement (APA) system is available to confirm the arm's-length pricing system proposed by a taxpayer. In general, corporations entering into an APA are advised to file a request for mutual agreement procedures (MAP) in order to obtain the agreement of the competent authorities of each country.

In October 2015, the OECD released the final BEPS reporting package with Action 13 relating to transfer pricing and related documentation. Taking into consideration the compliance costs for taxpayers along with increased transparency, the 2016 Japan Tax Reform requires the following documentation in order to adhere with the BEPS project:

Document	Required information	Submission deadline	Applicability
Country-by-Country (CbC) Report	Country revenue, pre-tax income, taxes payable, etc.	Must be e-filed within one year of the last fiscal day of the ultimate parent	Applicable for fiscal year of the ultimate parent entity beginning on or after 1 April 2016
		Master File	Group company structure, business outline, financial conditions, etc.
Local File	Transfer pricing documentation	By due date of tax return, to retain for seven years	Applicable for corporate tax in fiscal years beginning on or after 1 April 2017

Under the 2019 Tax Reform, the transfer pricing rules were revised to align with BEPS Action 8 and the revised OECD transfer pricing guidelines, including:

- Clarification of the definition of intangibles subject to transfer pricing legislation and introduction of measures for adjusting the transfer pricing of hard to value intangibles (HDVI).
- Introduction of the discounted cash flow (DCF) method as an approved transfer pricing methodology.
- Extension of the current statute of limitations for transfer pricing assessments from six years to seven years.

The above amendments will be applied to tax years beginning on or after 1 April 2020.

Thin capitalisation

Interest paid on debt to controlling foreign shareholders is disallowed to the extent the average balance of debt on which that interest is paid is more than three times the equity of controlling foreign shareholders.

Interest expense deduction limitation (earning stripping rule)

Under the 2019 Tax Reform, the earnings stripping rule was revised to align with BEPS Action 4, including:

- Expansion of the scope of non-deductible interest, which includes interest paid to third parties but excludes interest that is subject to Japanese income tax in the hands of the recipient.
- Lowering of the benchmark fixed ratio from 50% to 20%.
- Starting from taxable income, exempted dividend will no longer be added and WHT claimed as tax credit will be added.
- Lowering of the threshold for application of the new rules.

The above amendments will be applied to tax years beginning on or after 1 April 2020.

The deductible portion of a corporation's net interest expense to a related party as well as to the third party is restricted to 20% of the adjusted income. The net interest is calculated as interest expense less corresponding interest income. Interest expense does not include (i) interest expenses on specified bonds (issued to limited number of unrelated parties and not in public), (ii) interest payments subject to Japanese taxation or paid to qualifying public service corporations, and (iii) interest on back-to-back repos.

The adjusted income is defined as taxable income, adding back interest expense and depreciation expense, but excluding extraordinary income or loss.

Limitation (*de minimis* and group basis) on application is (i) net interest expense in a fiscal year is JPY 20 million or less, or (ii) the aggregated net interest expense on a Japanese corporate group basis (where there is more than a 50% capital relationship) is 20% or less of the aggregated adjusted income on the same group basis.

The non-deductible interest incurred in the past seven years will be deductible at up to 20% of the current adjusted taxable income.

Anti-tax haven (controlled foreign company or CFC) rules

Undistributed profits of a foreign subsidiary (i.e. CFC, which is defined as a foreign related corporation [FRC] by the (i) equity ownership test [owned more than 50% by Japanese corporations or residents] or (ii) *de fact* control test) to which an applicable tax rate is 30% (in case of a shell company) or 20% are included in the Japanese parent company's taxable income under certain conditions.

In the 2017 Tax Reform, major changes were made considering the BEPS recommendations to shift to a more of an income-based approach (although elements of the entity approach remain). After the amendments, income earned by a CFC is 'aggregated' (i.e. included within Japanese taxable income) in three different ways:

- Entity-based aggregation where all of the income of a CFC is taxable to a Japanese shareholder if (i) the main business of the foreign controlled subsidiary is not 'active' (as defined) and (ii) the foreign tax rate is lower than a 20% 'trigger' rate.
- Entity-based aggregation where all of the income of a CFC is taxable to a Japanese shareholder if (i) the CFC fails certain 'substance' and 'administration and control' tests and is thereby treated as a 'paper company' or 'cash box company' and (ii) the foreign tax rate is lower than a 30% 'trigger' rate.
- Income-based aggregation where even if the entity-based aggregation rules do not create income inclusion on an entity basis the relevant income of a CFC is taxable to a Japanese shareholder if (i) income of the CFC includes certain 'passive' categories of income and (ii) the foreign tax rate is lower than a 20% 'trigger' rate.

A Japanese corporation owning a 10% or more direct or indirect interest in a CFC is required to include its pro-rata share of the taxable retained earnings of the CFC in its gross income under certain circumstances.

A dividend paid by a CFC is not deductible when calculating its undistributed income.

The new rules apply for fiscal years of foreign subsidiaries starting on or after 1 April 2018.

Under the 2019 Tax Reform, the CFC regime was amended, including:

i. Narrowing of the definition of 'Paper Company' by excluding specified holding companies, real estate holding companies, and resource development project companies.
ii. Expansion of the definition of 'Cashbox Company'.
iii. Relaxation of the threshold for the unrelated entity test (a component of the CFC 'economic activity test') applicable to FRCs primarily engaged in the insurance industry.
iv. For FRCs under a consolidated tax return system or subject to pass through tax treatment, clarification of (a) the calculation of income for entity-based aggregation, (b) the calculation of the threshold effective tax rate, and (c) the use of foreign tax credits.
v. Revision of the scope of passive income aggregation.

Amendment (ii) above will be applied to CFCs with tax years beginning on or after 1 April 2019. The remaining amendments will be applied to CFCs with tax years beginning on or after 1 April 2018 for Japanese parent corporations'

aggregated taxable income for tax years ending on or after 1 April 2019.

Under the 2019 Tax Reform, the following three categories of FRCs are no longer treated as Paper Companies; (i) specified share holding companies (FRCs primarily engaged in the holding of shares of [specified] subsidiaries), (ii) specified real estate holding companies (FRCs primarily engaged in the holding of specified real estate), and (iii) resource development project companies (FRCs primarily engaged in the holding of shares of specified resource development project subsidiaries, providing funding raised from unrelated parties to such subsidiaries, or holding specified real estate related to such projects).

To qualify as one of the exempted FRCs described above (other than category (i), FRCs primarily engaged in the holding of shares of subsidiaries), the FRC should be managed and controlled by a management company and should perform functions essential to the carrying out of the management company's business.

In addition, the 2019 Tax Reform introduced specific tax treatment to the determination of aggregated income for FRCs applying consolidated tax return filing rules or covered by pass through provisions in the jurisdiction of their head office location. Under the amendments, the aggregated taxable income calculated under the tax law of the FRC, the threshold effective tax rate of the FRC, and the amount of foreign tax credits (applied by the Japanese parent company) are all calculated without applying any consolidated tax return filing rules or pass through provisions. The New Tax Circulars prescribe the use of the principle method or simplified method (*described below*) for the above calculation, as well as provide guidance regarding the application of optional income tax provisions and foreign tax credits.

	Applied provisions in the local statutes	**Aggregated income calculation**	
		Principle methods	**Simplified methods**
Consolidated tax filings	Corporate tax filing submitted on a consolidated basis (corporate tax payable is calculated based on the consolidated group's taxable income and filed by a single entity)	Calculated on a non-consolidated tax filing basis	Approved if the local provisions result in a reasonable calculation of income
	Pass through provisions	The FRC's corporate tax income is treated as income of the FRC's shareholder(s)	Calculated without application of the pass through provision (as if the FRC's income were not attributable to the FRC's shareholder(s))

Corporate - Tax credits and incentives

Last Reviewed - 18 August 2019

Foreign tax credit

A Japanese corporation is subject to Japanese corporate income taxes on its worldwide income. However, to avoid double taxation of foreign-source income, Japanese corporations are allowed to claim a tax credit against corporation and inhabitant's taxes for foreign income taxes paid directly.

Creditable foreign taxes are defined as taxes that (i) are incurred directly by the taxpayer; (ii) are levied by foreign governments and local authorities in accordance with local tax laws; (iii) are levied on corporate income; and (iv) have the

same characteristics as Japanese income tax, corporation tax, and local income-based taxes. A tax for which a refund can be claimed optionally by the taxpayer after the tax payment, or a tax whose payment grace period can be decided by the taxpayer, is not regarded as a foreign tax.

In order to prevent the credit from reducing corporation tax on Japan-source income, certain limitations are set on the amount of foreign taxes that can actually be credited. The ceiling is currently 35% for the foreign taxes paid.

A foreign tax credit is not applicable for enterprise tax purposes, although foreign branch income attributable to a business executed outside Japan is exempt from enterprise tax.

Generally speaking, the foreign tax credit system does not apply to the extent the dividend income from the foreign subsidiary is subject to the dividend exemption system.

Foreign corporations with a PE in Japan should note that when a foreign corporation's PE in Japan is subject to taxation in Japan as well as in jurisdictions other than its country of residence, double taxation may arise. To alleviate an unfair tax burden, a foreign tax credit regime is also applicable to PEs in Japan similar to that which applies to Japanese corporations. However, foreign tax (including WHT) paid in the enterprise's country of residency would not, in principle, be creditable under consequential changes to the foreign tax credit regime.

Under the 2019 Tax Reform, the amount of foreign tax that qualifies for foreign tax credits will be calculated without applying the tax consolidation or pass through provisions when the CFC is subject to the tax consolidation rule or pass through treatment in the jurisdiction of the CFC.

Tax credits and incentives for research and development (R&D) cost

Under the 2019 Tax Reform, R&D tax incentives (the R&D tax credit system) were revised to promote innovation by (i) increasing the tax credit ratio, (ii) increasing the limitation of tax credits for qualified venture corporations (i.e., from 25% to 40% of the corporate tax amount), and (iii) expanding the scope of open innovation R&D activities to include the cost of B2B outsourced R&D activities.

R&D tax credits (permanent measures)

The tax credit ratio formula was modified as shown in the following table:

Movement in R&D ratio (increase or decrease in ratio)	Tax credit ratio
8% <	9.9%＋(movement in R&D ratio - 8%) × 0.3 (upper limit of 10%)
8% ≧	9.9% - (8% - movement in R&D ratio) × 0.175 (lower limit is 6%)

The upper limit of the tax credit ratio of 10% is currently temporarily increased to 14% until 31 March 2019 (and is not applicable to tax years beginning on or after 1 April 2019). Under the 2019 Tax Reform, this applicable period was extended for a further two years.

In addition, the tax credit limitation for certain R&D venture corporations (i.e. corporations established in the past ten years or less with carryforward losses and that are not a subsidiary of a large corporation) was increased from the previous rate of 25% to 40% of the corporate tax liability.

R&D tax credits for corporations with higher R&D expenditure ratios

A preferential tax credit ratio and tax credit limitation is currently temporarily provided to taxpayers with higher R&D expenditure ratios (more than 10% of average gross sales). Under the 2019 Proposals, these preferential measures will be incorporated into the R&D tax credit system above, and the applicable period was extended for a further two years.

The formula of the preferential tax credit ratio for corporations with higher R&D expenditure ratios will be modified as shown in the following table:

Movement in R&D ratio (increase or decrease in	Tax credit ratio

ratio)	
8% <	9.9% ＋ (movement in R&D ratio - 8%) × 0.3 × α (upper limit is 10%)
8% ≧	9.9% - (8% - movement in R&D ratio) × 0.175 × α (lower limit is 6%)
	α = ratio of R&D expenditure to average gross sales

The preferential tax credit limitation (*see below*) remains the same, but the applicable period was extended for a further two years.

Tax credit limitation	Additional tax credit (no change to the current rule)
25% of corporate tax liabilities	(α - 10%) × 2 (upper limit is 10%)
	α = ratio of R&D expenditure to average gross sales

Open innovation R&D tax credits

The scope of R&D expenditure that qualifies as 'open innovation' was expanded to include B2B outsourced R&D activities (i.e. R&D conducted jointly with certain R&D focused venture corporations, or R&D expenditure arising from contracts with certain R&D focused venture corporations). In addition, 25% of the R&D tax credit ratio will be applied to R&D expenditures involving R&D focused corporations (i.e. joint R&D and contracted R&D); currently, the ratio is 20%.

The tax credit limitation for open innovation R&D expenditure was increased from the current rate of 5% to 10%.

R&D incentives for SMEs

The current special measures providing a preferential tax credit limitation (an upper limit of 35% of corporate tax liabilities) where the ratio of increased R&D expenditure exceeds 5% was modified (the threshold was increased from 5% to 8%), and the applicable period was extended for a further two years.

The previous special measures providing a preferential tax credit ratio for an increased R&D expenditure ratio (more than 10% of average gross sales) was modified in the same way as R&D tax credits for corporations with higher R&D expenditure ratios described above.

Salary increase tax credits

Under the 2018 Tax Act, the salary increase tax credit was amended for large corporations so that only those corporations increasing domestic investment would be eligible for the credits. The salary increase tax credit is available for corporations filing 'blue form' tax returns that meet the conditions described below. The revised salary increase tax credit rules will be applicable for fiscal years beginning on or after 1 April 2018 until 31 March 2021.

		Before the amendments	After the amendments
Conditions	(1)	Increased salary payment / (Salary payment to employees in base year) ≥ 5%	Abolished
	(2)	Salary payment in the current fiscal year ≥ salary payment in the preceding fiscal year	Salary payment in the current fiscal year ≥ salary payment in the preceding fiscal year
	(3)	((Average salary payment in the current fiscal year - average salary payment in the preceding fiscal year) ÷ average salary payment in the preceding fiscal year) ≥ 2%	((Average salary payment in the current fiscal year - average salary payment in the preceding fiscal year) ÷ average salary payment in the preceding fiscal year) ≥ 3%

	(4)	N/A	Domestic capital expenditure ≥ total depreciation
Tax credit		10% of the increased salary payment plus 2% of the salary payment made in the preceding year	15% of increased salary payment; 20% if training costs have increased by 20% or more
Limitation on tax credit		Up to 10% of the corporate tax liability	Up to 20% of the corporate tax liability

Internet of Things (IoT) investment tax incentive

A tax incentive (either accelerated depreciation or tax credit) for costs related to the development of certain data gathering and analytic information systems under the Special Measures Act for the Improvement of Productivity (Productivity Act) is available to companies that file blue form tax returns and have obtained approval of an 'innovative data utilisation plan'. Companies will be eligible for either accelerated depreciation (30%) or tax credit (3% or 5%) if they have acquired software as well as machinery or equipment worth JPY 50 million or more pursuant to the approved plan. The IoT investment tax incentive will be applicable from the effective date of the Productivity Act (6 June 2018) until 31 March 2021.

The amount of tax credit available will be higher for companies that satisfy a 'salary increase condition' (i.e. the average salary for employees of the company is increased for the year by more than 3%).

Special tax treatment for investment in certain equipment

SMEs filing 'blue form' tax returns may elect, under certain conditions, to claim accelerated depreciation of 100% of the base acquisition cost or a special tax credit equivalent to 10% of the base acquisition cost on designated equipment to the extent that it is acquired between 1 April 2014 and 31 March 2021. The maximum tax credit is limited to 20% of the taxpayers' corporate tax liability.

The 'Incentive for New Investment into Production Facilities' is applicable to any industry that invests in new production facilities (30% special depreciation or 3% tax credit on acquisition cost, up to 20% of corporate tax liability, etc., and subject to certain conditions). In addition, an investment incentive applies to SMEs that invest in equipment and furnishings pursuant to certain facility remodelling (30% special depreciation or 7% tax credit on acquisition cost, up to 20% of corporate tax liability [one-year carryforward of any excess], and subject to certain conditions). The SME tax incentive is granted to an SME engaged in the distribution, retailing, service, and/or agriculture business. This incentive is effective for tax years beginning on or after 1 April 2013 through 31 March 2021.

Incentives for the revitalisation of local 'hubs'

A taxpayer is eligible for certain tax incentives if it relates to or expands certain kinds of operations in local areas (generally other than Tokyo, Osaka, or Nagoya). Details as to the kinds of operations eligible are included in a future Revised Regional Revitalization Law.

Any qualifying investments have the following depreciation incentives with respect to investments in buildings:

Depreciation incentives	Investment pursuant to an approved relocation plan	Investment pursuant to expanding an existing operation
Type of depreciation (if plan is approved prior to 31 March 2020 and asset is acquired within two years of approval).	Additional first year depreciation of 25% of the acquisition cost (depreciation is accelerated).	Additional first year depreciation of 15% of the acquisition cost (depreciation is accelerated).

Alternatively, a taxpayer may choose to take a tax credit rather than accelerated depreciation, as follows:

Tax credits	Investment pursuant to an approved relocation plan	Investment pursuant to expanding an existing operation
Tax credits (if plan is approved prior to 31 March 2020 and asset is acquired within two years of approval)	Acquisition costs x 7%	Acquisition costs x 4%

Minimum investment is JPY 20 million for large corporations and JPY 10 million for SMEs.

Alternate to the investment incentive above, an employment-related tax credit is allowed for increased employment in a local hub if hired within two years of the plan approval. The credit shall be JPY 500,000 or JPY 600,000 times the number of increased employees at a maximum (if certain conditions are not met, the credit becomes JPY 200,000 per employee).

In either tax incentive, the amount of the above tax credits can only offset up to 20% of a corporation's tax liability.

Local government contributions

As part of the Regional Revitalization Act, 'blue form' corporate tax filers who make donations to approved regional donation plans up until 31 March 2020 will be able to claim a tax credit against corporate, enterprise, and inhabitant's taxes in addition to taking a deduction from the corporate tax. This is known as the corporate hometown tax, or *furusato nozei* system.

National strategic zones

For a 'blue form' filing corporation with an approved plan for qualified investment in a National Strategic Special Area up until 31 March 2020, a deduction of 20% of income is available for five years from the date of establishment.

Corporate - Withholding taxes

Last Reviewed - 18 August 2019

Tax treaty network

As of 1 July 2019, Japan has entered into 74 tax treaties with 130 countries and/or regions. In addition, on 1 January 2019, the MLI entered into force for Japan. As of 1 July 2019, 15 jurisdictions, which are among the Japanese covered convention, deposited the instrument of ratification, acceptance, or approval of the Convention, and for 12 jurisdictions (Australia, Finland, France, Ireland, Israel, Netherlands, New Zealand, Poland, Singapore, Slovakia, Sweden, United Kingdom), the MLI entered into force. The MLI for India, United Arab Emirates, and Luxembourg will enter into force by the end of 2019.

Note that since the Convention on Mutual Administrative Assistance in Tax Matters is a multilateral convention, and the tax conventions with the former Soviet Union and with the former Czechoslovakia were succeeded by more than one jurisdiction, the numbers of jurisdictions do not correspond to those of tax conventions, etc.

Companies making certain payments are required to withhold income taxes using the following rates:

Recipient	WHT (%)			
	Dividends		Interest	Royalties (2)
	Portfolio (3)	Substantial holdings (1)		
Japanese corporations	20	20	0/20 (4)	0
Resident individuals	20	20	0/20 (4)	0

Recipient	WHT (%)			
	Dividends		Interest	Royalties (2)
	Portfolio (3)	Substantial holdings (1)		
Foreign corporations, non-resident individuals:				
Non-treaty (5)	15/20 (3)	20 (3)	0/15/20 (4)	20
Treaty (6):				
Argentina (25)	15	10	0/12 (43)	3/5/10 (44)
Australia	10	0/5	10	5
Austria (26)	20	10	10	10
	10	0	0	0
Bahamas (7)	-	-	-	-
Bangladesh	15	10	10	10
Belgium (42)	15	10	10	10
	10	0	0/10 (27)	0
Bermuda (7)	-	-	-	-
Brazil	12.5	12.5	12.5	12.5/15/25 (8)
British Virgin Islands (7)	-	-	-	-
Brunei	10	5	10	10
Bulgaria	15	10	10	10
Canada	15	5	10	10
Cayman Islands (7)	-	-	-	-
Chile	15	5	4/10 (45)	2/10 (46)
China, People’s Republic of	10	10	10	10
Colombia (25)	10	5	0/10 (27)	2/10 (46)
Croatia (25)	5	0	0/5 (37)	5
Czechoslovakia (former) (9)	15	10	10	0/10 (9)
Denmark (26)	15	10	10	10

Recipient	WHT (%)			
	Dividends		Interest	Royalties (2)
	Portfolio (3)	Substantial holdings (1)		
	5/15 (28)	0	0	0
Ecuador (25)	-	-	-	-
Egypt	15	15	15/20	15/20 (10)
Estonia (26)	10	0	0/10 (29)	0
Finland	15	10	10	10
France	10	0/5 (30)	10	0
Germany	5/15 (31)	0 (31)	0	0
Guernsey (7)	-	-	-	-
Hong Kong	10	5	10	5
Hungary	10	10	10	0/10 (11)
Iceland (26)	5/15 (32)	0 (32)	0	0
India	10	10	10	10 (12)
Indonesia	15	10	10	10
Ireland, Republic of	15	10	10	10
Israel	15	5	10	10
Italy	15	10	10	10
Jersey (7)	-	-	-	-
Kazakhstan	15	5	10	5 (13)
Korea, Republic of	15	5	10	10
Kuwait	10	5	10	10
Latvia	0	0	0	0
Liechtenstein (7)	-	-	-	-
Lithuania (26)	0	0	0	0
Luxembourg	15	5	10	10
Macao (7)	-	-	-	-
Malaysia	15	5	10	10

Recipient	WHT (%)			
	Dividends		Interest	Royalties (2)
	Portfolio (3)	Substantial holdings (1)		
Man, Isle of (7)	-	-	-	-
Mexico	15	0/5 (14)	10/15 (14)	10
Netherlands	10	0/5 (15)	0/10 (15)	0
New Zealand	15	0	10	5
Norway	15	5	10	10
Oman	10	5	0/10 (33)	10
Pakistan	10	5/7.5 (16)	10	10
Panama (7)	-	-	-	-
Philippines	15	10	10	10/15 (17)
Poland	10	10	10	0/10 (11)
Portuguese Republic	10	5	0/5/10 (34)	5
Qatar	10	5	0/10 (35)	5
Romania	10	10	10	10/15 (18)
Samoa (7)	-	-	-	-
Saudi Arabia	10	5	0/10 (36)	5/10 (19)
Singapore	15	5	0/10 (36)	10
Slovenia	5	5	0/5 (37)	5
South Africa	15	5	10	10
Spain (25)	15	10	10	10
	5	0	0	0
Sri Lanka	20	20	0/15/20 (20)	0/10 (20)
Sweden	10	0 (21)	0	0
Switzerland	10	0/5	0/10 (35)	0
Taiwan	10	10	0/10 (38)	10
Thailand	15 (3)	15/20 (22)	10/25 (22)	15
Turkey	15	10	10/15 (23)	10

Recipient	WHT (%)			
	Dividends		Interest	Royalties (2)
	Portfolio (3)	Substantial holdings (1)		
USSR (former) (24, 26)	15	15	10	0/10 (24)
	10/15 (39)	5 (39)	0	0
United Arab Emirates	10	5	10	10
United Kingdom	10	0	0	0
United States (25)	10 (40)	0/5 (40)	0/10 (41)	0
	10 (47)	0/5 (47)	0	0
Vietnam	10	10	10	10
Zambia	0	0	10	10

Notes

1. The tax treaty rates apply only to corporate shareholders. The applicable treaty should be checked for conditions required to claim the reduced rate. Note that WHT may be subject to the income surtax of 2.1%, which is levied for the income earned for the period from 1 January 2013 through 31 December 2037.
2. The applicable treaty should be reviewed because certain tax treaties exclude film royalties and/or gain from copyright transfer from taxable income. Note that WHT may be subject to the income surtax of 2.1%, which is levied for the income earned for the period from 1 January 2013 through 31 December 2037.
3. 15% for publicly traded shares (for non-resident individual, only applicable to minority interest [less than 3% ownership]) and investment trusts. Note that WHT may be subject to the income surtax of 2.1%, which is levied for the income earned for the period from 1 January 2013 through 31 December 2037.
4. Interest on bank deposits and/or certain designated financial instruments is subject to a 15% national WHT and 5% local inhabitants WHT (20% combined). Taxation of such interest is fully realised by tax withholding, so resident individuals are not required to aggregate such interest income with other income. Interest on loans made by resident individuals is not subject to WHT; instead, it is taxed in the aggregate with other income. Such WHT is subject to the income surtax of 2.1%, which is levied for the income earned for the period from 1 January 2013 through 31 December 2037.
5. Dividends, interest, and royalties earned by non-resident individuals and/or foreign corporations are subject to a 20% national WHT under Japanese domestic tax laws in principle. An exceptional rate of 15% is applied to interest on bank deposits and certain designated financial instruments. Interest on loans, however, is taxed at a 20% rate. A special exemption from WHT applies to certain long-term corporate bonds issued to non-residents in foreign countries. Note that WHT may be subject to the income surtax of 2.1%, which is levied for the income earned for the period from 1 January 2013 through 31 December 2037.
6. Tax treaties with many countries provide reduced tax rates, as indicated. Some treaties, however, provide higher tax rates (e.g. Brazil, Thailand) or do not provide rates (e.g. Egypt, New Zealand). In these instances, rates specified under Japanese domestic tax laws apply. Each treaty should be consulted to see if a reduced rate for dividends (in the case of substantial holdings) is applicable.
7. The tax treaty was concluded mainly for the purpose of information exchange.
8. The tax treaty with Brazil provides a 25% tax rate for certain royalties (trademark). However, the WHT rate cannot exceed 20.42% (including the income surtax of 2.1%) on any royalties to be received by a

non-resident taxpayer of Japan under Japanese income tax law. Film royalties are taxed at 15%. Any other royalties are taxed at 12.5%.

9. The treaty with the former Czechoslovakia is applied to the Czech Republic and the Slovak Republic. It stipulates that cultural royalties are tax exempt.
10. Film royalties are taxed at 20%, and other royalties are taxed at 15%.
11. Cultural royalties are tax exempt.
12. The rate of 10% for royalties includes consideration for technical services.
13. The rate for royalties is reduced from 10% to 5% by Protocol.
14. Dividends received from subsidiaries, by parent companies that have met certain conditions, are exempt from WHT. Exempted for interest received by government and other specific entities; 10% for interest received by banks, financial institutions, or paid as a consequence of sale on credit of any equipment; 15% for others.
15. Dividends received from subsidiaries for which the parent company has over 50% shareholding are tax exempt. Interest received by government and other specific entities, or paid as a consequence of sale on credit of any equipment, merchandise, or service, is tax exempt.
16. A 5% rate is applied to a company that has over 50% shares with direct voting rights, and a rate of 7.5% is applied to a company that has over 25% shares with direct voting rights.
17. Film royalties are taxed at 15%. Any other royalties are taxed at 10%.
18. Cultural royalties are taxed at 10%.
19. Royalties paid for the use of certain equipment are taxed at 5%.
20. Interest paid to financial institutions is tax exempt, as well as film and copyright royalties. Patent royalties are subject to a 10% rate.
21. If certain conditions for beneficial owners are met, dividends are taxable only in the contracting state of which the beneficial owner is a resident.
22. Dividends paid by a corporation that is engaged in industrial undertakings are taxed at 15%. Interest paid to financial institutions is taxed at 10%.
23. Interest paid to financial institutions is taxed at 10%.
24. The treaty with the former USSR is applied to Armenia, Azerbaijan, Belarus, Georgia, Kyrgyzstan, Moldova, Tajikistan, Turkmenistan, Ukraine, and Uzbekistan. It stipulates that cultural royalties are tax exempt.
25. The new treaty was signed but has not yet become effective.
26. The treaty applies with respect to taxes levied on the basis of a taxable year for taxes for any taxable years beginning on or after 1 January 2019 and with respect to taxes not levied on the basis of a taxable year for taxes levied on or after 1 January 2019.
27. Exempted when paid and beneficially owned by enterprises, etc; 10% for others.
28. Exempted when paid by a company of Japan, holding at least 10% of voting power for six months, or beneficially owned by pension funds; 15% for others.
29. Exempted when received by governments, etc.; 10％ for others.
30. Exempted when paid by a company of Japan, holding at least 15% (direct or indirect) or 25% (direct) shares for six months; 5% for holding at least 10% (direct or indirect) shares for six months.
31. Exempted when holding at least 25% for 18 months; 5% when holding at least 10% for six months; 15% for others.
32. Exempted when holding at least 25% of voting shares for six months or beneficially owned by pension funds; 5% when holding at least 10% of voting shares for six months; 15% for others.
33. Exempted when received by governments, etc.; 10% for others.
34. Exempted when received by governments, etc.; 5% when received by banks; 10% for others.
35. Exempted when received by governments, financial institutions, etc.; 10% for others.
36. Exempted when received by governments or central bank; 10% for others.
37. Exempted when received by governments, etc.; 5% for others.
38. Exempted when received by governments, etc.; 10% for others.
39. Exempted when received by beneficially owned by pension funds; 5% when holding at least 15% of voting power for 365 days; 15% when shares deriving at least 50% of their value from immovable property; 10% for others.

40. Exempted when holding more than 50% of voting shares for 12 months or beneficially owned by pension funds; 5% when holding at least 10% of voting shares; 10% for others.
41. Exempted when received by governments or financial institutions; 10% for others.
42. The treaty entered into force on 19 January 2019 and will apply with respect to taxes levied on the basis of a taxable year for taxes for any taxable years beginning on or after 1 January 2020 and with respect to taxes not levied on the basis of a taxable year for taxes levied on or after 1 January 2020.
43. Exempted when received by the entity beneficially owned by governments; 12% for others.
44. Royalties on news are taxed at 3%, royalties on copyright are taxed at 5%, and other royalties are taxed at 10%.
45. Received by banks, etc, are taxed at 4% and 10% for others.
46. Royalties on equipment are taxed at 2%, and other royalties are taxed at 10%.
47. Exempted when holding more than 50% of voting shares for six months or beneficially owned by pension funds; 5% when holding at least 10% of voting shares; 10% for others.

Corporate - Tax administration

Last Reviewed - 18 August 2019

Taxable period

The tax year is the corporation's annual accounting period specified in its articles of incorporation. A Japan branch of a foreign corporation must use the same accounting period that is adopted by the corporation in its home country.

Tax returns

Corporate income tax returns (i.e. the national corporation tax return, enterprise tax return, and local inhabitants' tax return) are self-assessment tax returns.

If a corporation meets certain conditions, such as keeping certain accounting books, and makes an application for it in advance, it is allowed to file a 'blue form' tax return. A 'blue form' filing corporation may benefit from loss carryforward and other benefits, including incentive tax application.

A corporation (including a branch) is required to file the final tax return within two months after the end of its annual accounting period. If a corporation cannot file the final return because of specific reasons, the due date of the final return may be extended for one month (two months in case of consolidated tax filing) with the tax authority's approval. Further extension may be allowed by an advanced approval.

Payment of tax

Income taxes payable on the final corporate income tax return should be paid on or before the filing due date of the final tax returns (usually two months after the end of the corporation's accounting period). If an extension of time for filing is granted, the taxes may be paid on or before the extended due date with interest accrued at a rate of 1.6% (for the year 2019) *per annum* for the period from the day following the original due date (i.e. two months after the end of an accounting period) to the date of the actual payment.

Provisional tax payments are required for a corporation that has a fiscal period longer than six months. Provisional taxes generally are computed as one-half of the tax liabilities for the previous year, but they may be reduced by the filing of interim tax returns that reflect semi-annual results of the operations. The provisional tax payment is required to be made within two months after the end of the sixth month of the corporation's accounting period.

Penalties

If the tax return is filed late, a late filing penalty is imposed at 15% to 20% of the tax balance due. In the case that a corporation voluntarily files the tax return after the due date, this penalty may be reduced to 5%. The rate is increased to 10% to 15% once the tax audit notice is received.

An under-payment penalty is imposed at 10% to 15% of additional tax due. In the case that a corporation amends a tax return and tax liabilities voluntarily after the due date, this penalty may not be levied. The penalty is imposed at 5% to 10% once the tax audit notice is received.

In addition, interest for the late payment of tax is levied at 2.6% *per annum* for the first two months and increases to 8.9% *per annum* thereafter (for the year 2019).

Consolidated taxation

The parent company will file the consolidated tax return and pay national corporate income tax for the group. The consolidated tax return and payment due dates are the same as previously discussed; however, the due date of the final return may be extended for two months.

For local corporate income taxes, each member of the consolidated group must separately file the returns and pay the taxes.

Tax audit process

Generally speaking, corporate tax audit is performed in cycles of three to five years' duration. However, this period may be shortened in the case that some significant tax matters were pointed out in the prior audit and so on. If taxpayers request a downward correction, a tax audit will be performed to make sure of it.

With regard to tax audit procedures, tax laws have not clarified them thus far. Prior to conducting a tax audit, in principle, tax agents are required to notify taxpayers, and, upon completion of tax audits, tax agents are required to provide to taxpayers a brief written summary of their findings, etc.

Once an audit is complete, the basic principle is that a second audit is not allowed. However, if newly acquired information is obtained by the tax authorities that lead them to conclude that the reported taxable income should have been different, then the tax authorities can conduct another audit of the taxpayer. This limitation on the ability of the tax authorities to conduct a second audit only applies if the first audit was conducted on-site. If a 'desk audit' is only conducted, where the tax authorities do not conduct the audit on-site, no limitation applies.

Statute of limitations

The statute of limitations to request a downward correction of prior year tax liabilities is five years from when the original tax return was filed.

The statute of limitations with regard to upward corrections by the tax authorities is also five years.

Under the 2019 Tax Reform, the statute of limitation in relation to the transfer pricing tax liabilities was extended from six years to seven years. The extended statute of limitation will apply to the tax returns for the fiscal year beginning on or after 1 April 2020.

Topics of focus for tax authorities

Tax authorities are often focusing on cross-border, inter-company transactions (i.e. transfer pricing or donation issues), PE, and significant group restructuring, among other issues. Any developments in discussion on the G20/OECD BEPS project will also be of great interest for Japanese authorities.

In the G20 hosted by Japan in July 2019, the OECD tax report was submitted and approved by the G20. Additionally, the work programme on addressing the tax challenges arising from digitalisation was endorsed.

Corporate - Other issues

Last Reviewed - 18 August 2019

Requirement for banks to collect and remit information regarding bank accounts owned by non-residents

A tax reporting system is applicable under which individuals are required to report information to the relevant branch of the financial institution, which will, in turn, submit such information to the tax authorities in Japan.

The person who contracts with the financial institution for a deposit to a bank account in Japan on or after 1 January 2017 will be required to report the relevant information to the bank, including (i) name, (ii) address, (iii) date of birth, and (iv) resident country. If the resident country is outside Japan, the individual will be required to report the taxpayer identification number in the taxpayer's resident country. The financial institution will be required to report the individual information collected as well as details regarding the account (balances, transactions, etc.) as of 31 December by the following 30 April.

Corporate spin-offs

Corporate demerger

Before the 2017 Tax Reform, a corporate demerger by a corporation with many shareholders where the shares in the new company are given to the shareholders does not qualify as a tax qualified demerger. These rules are relaxed under the 2017 Tax Reform, whereby a spin-off of a specific business by a corporation without a controlling shareholder becomes tax qualified under certain conditions.

Distribution in kind

Before the 2017 Tax Reform, a distribution in kind by a corporation with many shareholders is not tax qualified. Under the 2017 Tax Reform, a spin-off conducted as a distribution in kind of shares in a 100% subsidiary becomes tax qualified under certain conditions.

Minority shareholder squeeze-outs

Under the 2017 Tax Reform, creating a 100% subsidiary through a squeeze-out process using shares with compulsory acquisition rights, share consolidation, and a request to sell back shares, is considered a type of corporate reorganisation. As part of bringing such squeeze-outs within the corporate reorganisation framework, special measures will be introduced, including mark-to-market rules and the special rules on consolidated taxation.

In a merger or share-for-share transfer, if the merging corporation or the 100% parent corporation owns 2/3 or more of the merged corporation or the 100% subsidiary, consideration other than shares can be provided to minority shareholders without disqualifying the corporate reorganisation.

Consideration in triangular mergers, corporate split-offs, and share-for-share exchanges

Before the 2019 Tax Reform, in a triangular merger, corporate split-off, or share-for-share exchange, shares of a 100% direct parent of an acquiring company are treated as tax qualified consideration. Under the 2019 Tax Reform, tax qualified consideration was expanded to include shares of an indirect 100% parent of the acquiring company.

Individual - Significant developments

Last Reviewed - 03 July 2019

2019 Tax Reform bills

On 27 March, the 2019 Tax Reform bills were approved in the Diet with the following changes to Japanese individual income tax, inheritance tax, and gift tax.

Extension of the income tax credit for housing loans for individuals who acquire a qualified residence that will be subject to the 10% consumption tax rate

Under the current rules, resident taxpayers who have home mortgages and are eligible for the home loan credit can enjoy up to 500,000 Japanese yen (JPY) of credit from their annual income tax for a period of ten years. In conjunction with the increase in consumption tax rate to 10% (from the current 8%) in October 2019, the credit will be extended for an additional three years on 2% of the building's price for those who enter into a new home purchase and move into the

residence between 1 October 2019 and 31 December 2020. The table below demonstrates the annual applicable credit for the period from the 11th year through the 13th year.

	General Type	**Qualified Long-Life Housing /** Qualified Low-Carbon Housing
A	Year-end loan balance (limited to JPY 40,000,000) x 1%	Year-end loan balance (limited to JPY 50,000,000) x 1%
B	Acquisition cost for the building excluding consumption tax (limited to JPY 40,000,000) x 2% ÷ 3	Acquisition cost for the building excluding consumption tax (limited to JPY 50,000,000) x 2% ÷ 3
Annual Credit	The lesser of A or B	The lesser of A or B

Reduction in the rates for annual automobile tax and repeal of one-time acquisition tax

In conjunction with the increase in consumption tax rate, the automobile acquisition tax will be abolished at the end of September 2019 and will be replaced by an automobile environment performance tax. The automobile environmental performance tax rate will range from 1% to 3%, depending on the automobile's fuel efficiency; however, a reduction of 1% in the tax rate will be allowed for the purchase from 1 October 2019 to 30 September 2020. In addition, the annual automobile tax imposed on car owners will be reduced by JPY 1,000 to JPY 4,500 per year.

Revision of the scope and applicable requirements for tax-exempt measures applied to dividend income or capital gains arising from Nippon Individual Savings Accounts (NISAs)

The scope and applicable requirements for tax-exempt measures applied to dividend income or capital gains arising from NISAs will be revised. The changes include the ability for the account holders to maintain the tax-exempt NISAs while they are temporarily out of Japan (up to five years). Currently, individuals leaving Japan need to move their financial products in a NISA to a taxable account, and such products cannot be moved back to the NISA once they return to Japan.

Revision of the scope and applicable requirements for tax qualified stock options

For qualifying businesses, the applicable person for tax qualified stock options (i.e. the treatment of deferred income arising from exercising the tax qualified stock options) will be expanded to include those other than directors or employees of the company issuing the stock options ('issuer'). The issuer must be a designated venture company pursuant to the revised Small and Medium Enterprises Management Reinforcement Law. If an individual who acquired the stocks by exercising the tax qualified stock options would depart from Japan, such individual would be subject to Japanese income tax as if the stocks were disposed of at a fair market price when the options were exercised.

Clarification of the income tax treatment of income from virtual currencies

For individual income tax purposes, income from virtual currencies is generally classified as miscellaneous income. In regards to sales and transfers of virtual currencies, the method of calculating the acquisition costs is clarified to be the moving average method or the gross average method. If an election was not made, the acquisition cost is calculated under the gross average method.

Introduction of stricter guidelines to municipalities participating in the hometown tax donation (furusato nozei) programme

Furusato nozei is a programme that allows people to donate to a municipal or prefectural government of their choice and, in return, receive tax deductions/credits (and gifts from such localities in most cases).

Under the new rules, the value of gifts provided by the municipalities must be limited to no more than 30% of the donation and must be produced within the municipality receiving the donation in order for the donation to be qualified for the full tax benefit. Those qualified municipalities must be designated by the Ministry of Internal Affairs and Communications.

The above changes are effective for donations made on or after 1 June 2019.

Step-up in cost basis for assets subject to a treaty country's exit tax

When a Japan resident taxpayer disposes of assets that were subject to an exit tax in a treaty country, and such treaty would include provisions to adjust double taxation for such dispositions, the cost basis will increase to the amount subject to such treaty country's exit tax.

Three-year extension on My Number notification to financial institutions for those who opened accounts by 31 December 2015

Taxpayers who opened their brokerage accounts before Japan's My Number (unified tax and social security number) system began on 1 January 2016 had a three-year grace period (until 31 December 2018) to provide their My Numbers to their brokers. The 2019 Tax Reforms grant another three-year grace period to the taxpayers.

A tax payment grace period (postponement) of inheritance or gift tax levied on assets acquired through business succession for individual business operators

The 2019 Tax Reforms have introduced a grace period for the payment of inheritance or gift tax in the event that a successor acquires certain business assets through inheritance or gifting and succeeds the respective business. The amount of tax deferred under the new rule is 100%. The qualified business assets include land, building, and certain depreciable assets. The new rule is similar to existing tax rules for corporate business succession, and, as in the case of a corporate business succession, a succession plan must be prepared and submitted to the designated district authorities.

The above changes are effective for business assets acquired between 1 January 2019 and 31 December 2028.

Extension of the period of tax-exempt lump-sum gifts for marriage, childcare, or education

Special gift tax exemptions that are available until April 2019 for cash gifts into a Japanese trust intended to cover costs associated with children's education, marriage and household expenses, and childcare will be revised and extended by another two years. While extending the eligible period, the 2019 Tax Reforms have also introduced a new income limit to the recipients of these gifts. If the donee's annual income for the year immediately preceding the year of gift exceeds JPY 10 million, the tax exemption will not apply. Also, educational costs other than those paid to schools (such as a tuition for after-school lessons) are generally not qualified for the exemption if the donee is 23 years old or older.

The above changes on the income threshold are effective for gifts paid into a qualified trust on or after 1 April 2019. The above changes on the qualified educational costs are effective for educational expenses paid on or after 1 July 2019.

Inheritance and gift tax law changes following amendments to the Civil Code to lower age of majority from 20 to 18 years old

Following the above change, inheritance and gift tax rules will be adjusted to reflect 18 years of age instead of 20. Two examples of these changes are as follows:

- The age of the child at which an heir is eligible for child credit on inheritance tax is adjusted from younger than 20 years to younger than 18 years.
- The requirements to qualify for the special system of 'settlement of taxes at the time of inheritance' where taxpayers can make irrevocable election to integrate inheritance and gift tax will be impacted with the change in age of lineal descendants from 20 to 18 years or older.

The changes will come into force for bequests and gifts made from 1 April 2022.

2018 Japan Tax Reforms

The 2018 Japan Tax Reforms include the following changes to Japanese individual income tax.

Decrease in the earned income deduction for employees by JPY 100,000 and the income level deduction cap reduced to JPY 1.95 million

Resident taxpayers are eligible for a deduction against earned income (which is a so-called ‘earned income deduction’) based on the percentage of their employment income. Currently, the earned income deduction has a minimum deduction amount of JPY 650,000, and it is capped at JPY 2.2 million.

Under the 2018 Tax Reforms, the earned income deduction for employees will be decreased by JPY 100,000, and the income level deduction cap will be reduced to JPY 1.95 million; however, the reduced deduction cap will not apply to taxpayers with dependent children under age 23 or those taking the special disability exemption.

The following changes, effective January 2020, will apply to the earned income deduction for a permanent resident and/or non-permanent resident employee:

Taxpayer’s annual salary	Earned income deduction
JPY 1,625,000 or below	JPY 550,000
Over JPY 1,625,000 and up to JPY 1,800,000	Gross income x 40% - JPY 100,000
Over JPY 1,800,000 and up to JPY 3,600,000	Gross income x 30% + JPY 80,000
Over JPY 3,600,000 and up to JPY 6,600,000	Gross income x 20% + JPY 440,000
Over JPY 6,600,000 and up to JPY 8,500,000	Gross income x 10% + JPY 1,100,000
Over JPY 8,500,000	JPY 1,950,000

For taxpayers with gross employment income over JPY 8.5 million with dependent children under age 23 or those taking the special disability exemption, the current rate (10%) will apply (up to gross employment income of JPY 10 million; the deduction is capped at JPY 2.1 million).

Increase in the personal exemption by JPY 100,000 but reduction of all personal exemptions at income levels between JPY 24 million and JPY 25 million and elimination of the personal exemptions for income levels over JPY 25 million

Resident taxpayers are entitled to a personal exemption for themselves (so-called ‘basic exemption’, which is currently JPY 380,000 for national tax and JPY 330,000 for local tax). Currently, there is no income threshold to be eligible for the basic exemption and all taxpayers can take the same level of exemption.

The following changes, effective January 2020, will apply to personal exemptions. For the first time, the basic exemption will be abolished for taxpayers with total annual income over JPY 25 million.

Taxpayer’s total annual income	‘Basic exemption’ for national tax	‘Basic exemption’ for local tax
Below JPY 24,000,000	JPY 480,000	JPY 430,000
Over JPY 24,000,000 and up to JPY 24,500,000	JPY 320,000	JPY 290,000
Over JPY 24,500,000 and up to JPY 25,000,000	JPY 160,000	JPY 150,000
Over JPY 25,000,000	None	None

Decrease in the public pension income deduction by JPY 100,000 and an introduction of a cap on the deduction at JPY 1,955,000 for seniors whose annual pension income exceeds JPY 10 million

Taxpayers are entitled to a deduction against qualified public pension income. Currently, this deduction is not limited by the taxpayer's income level.

Under the 2018 Tax Reforms, the public pension income deduction will be capped at JPY 1,955,000 when the gross public pension income reaches JPY 10 million. Furthermore, the public pension income deduction will be reduced for taxpayers with income other than public pension income of over JPY 10 million in two phases (for further details, please see the footnotes in the table below).

The following changes, effective January 2020, will apply to the public pension income deduction:

Recipient's age (years)	Amount of pension received (A)	Public pension income deduction
Under 65	Below JPY 1,300,000	JPY 600,000
	Over JPY 1,300,000 and up to JPY 4,100,000	(A) x 25% + JPY 275,000
65 and above	Below JPY 3,300,000	JPY 1,100,000
	Over JPY 3,300,000 and up to JPY 4,100,000	(A) x 25% + JPY 275,000
All ages	Over JPY 4,100,000 and up to JPY 7,700,000	(A) x 15% + JPY 685,000
	Over JPY 7,700,000 and up to JPY 10,000,000	(A) x 5% + JPY 1,455,000

For individuals who have income other than public pension income of over JPY 10 million and up to JPY 20 million, the pension deduction from the table above is reduced by JPY 100,000 (the maximum deduction of JPY 1,855,000).

For individuals who have income other than public pension income of over JPY 20 million, the pension deduction from the table above is reduced by JPY 200,000 (the maximum deduction of JPY 1,755,000).

Decrease in the 'blue form' tax return deduction by JPY 100,000 and increase in the 'blue form' deduction by JPY 100,000 for filing and maintaining tax returns and accounting documents electronically

Under the 2018 Tax Reforms, effective January 2020, the maximum 'blue form' deduction for taxpayers with business income will be reduced by JPY 100,000 from the current JPY 650,000. As an incentive for taxpayers to file 'blue form' tax returns electronically, taxpayers who do so or maintain accounting documents electronically will receive an additional JPY 100,000 'blue form' deduction (i.e. JPY 650,000 in total).

Japan non-permanent residents to be taxed on sale of personal property outside of Japan

Effective 1 January 2017, there is an increase in scope of taxation of non-permanent resident taxpayers of Japan. Income from the sale of personal property located outside of Japan will be taxable in Japan even if the proceeds are not remitted to Japan.

The 2017 Japan Tax Reform provided an exemption on the issue of capital gains taxation on certain foreign-listed securities sales for non-permanent residents, but the new rule on income from sale of other personal property will still apply.

Individual - Taxes on personal income

Last Reviewed - 03 July 2019

In Japan, permanent resident taxpayers are taxed on their worldwide income. Non-resident taxpayers are taxed only on their Japan-sourced income. Non-permanent resident taxpayers are taxed on their income other than foreign-source

income (in particular, potentially, on certain capital gains) that are not remitted into Japan plus potentially part of their foreign-sourced income that is paid in or remitted to Japan.

Personal income tax rates

The current national income tax rates are:

Taxable income (JPY)		Tax on column 1 (JPY)	Tax on excess (%)
Over (column 1)	Not over		
0	1,950,000		5
1,950,000	3,300,000	97,500	10
3,300,000	6,950,000	232,500	20
6,950,000	9,000,000	962,500	23
9,000,000	18,000,000	1,434,000	33
18,000,000	40,000,000	4,404,000	40
40,000,000		13,204,000	45

The tax liability is determined by multiplying the excess taxable income for each bracket by the percentage above and adding the cumulative tax figure (*see the Sample personal income tax calculation section for more information*).

Surtaxes

A surtax took effect 1 January 2013. The surtax is comprised of a 2.1% tax that is assessed on an individual's national income tax.

Local income taxes

Generally, in Japan, the local inhabitant's tax is imposed at a flat rate of 10%. Japanese local governments (prefectural and municipal governments) levy local inhabitant's tax on a taxpayer's prior year income. This applies where the taxpayer is a resident of Japan as of January 1 of the current year. For local inhabitant's tax purposes, an equalisation *per capita* tax is also assessed. The standard annual amount is JPY 5,000, while this may vary based on the prefecture/municipality in which the taxpayer resides. Local inhabitant's tax is not deductible.

Non-residents

A non-resident taxpayer's Japan-source compensation (employment income) is subject to a flat 20.42% national income tax on gross compensation with no deductions available. This rate includes 2.1% of the surtax described above (20% x 102.1% = 20.42%). A non-resident taxpayer may be subject to the local inhabitant's tax at a rate of 10% if they are registered as a resident as of 1 January of the current year.

Individual - Residence

Last Reviewed - 03 July 2019

A resident taxpayer is an individual taxpayer (i) who has a '*jusho*' (i.e. a residence) in Japan; or (ii) who has maintained a '*kyosho*' (i.e. a temporary place of abode) in Japan for a period of one year or more. A resident taxpayer who is not a Japanese national and who has an aggregate stay in Japan of five years or less within the preceding ten years (60 months within the preceding 120 months) would be classified as a non-permanent resident taxpayer. If a resident taxpayer is a Japanese national, or a foreign national with an aggregate stay in Japan of more than five years within the preceding ten years, the taxpayer is considered a permanent resident taxpayer.

Individual - Other taxes

Last Reviewed - 03 July 2019

Social security contributions

An employee whose salary or bonus, including fringe benefits, is paid in Japan by a local employer (including a Japanese branch of a foreign corporation) is generally liable to pay a share of social insurance premiums. The employee's share consists of the following contributions:

Contribution	Standard premiums on monthly salary	Standard premiums on bonus
Health insurance for the Metropolis of Tokyo (each prefecture has its own health insurance rate, and rates are slightly higher for individuals between the ages of 40 and 65)	4.95% (on a maximum of JPY 1,390,000 of wages per month)	4.95% (on an annual cap of JPY 5.73 million of irregular annual total payments)
Welfare pension (1)	9.15 % (on a maximum of JPY 620,000 of wages per month)	9.15% (on a maximum of JPY 1.5 million of irregular payments per month)
Unemployment insurance	0.3%	0.3%
Total	14.35%	14.35%

Note

1. The fixed rate of 9.15% for welfare pension will be applied from September 2017. Premiums on child allowance will be imposed separately at 0.34% from April 2019.

Japan social insurance paid by the employee is deductible for Japan income tax purposes.

Consumption taxes

A consumption tax is levied when a business enterprise transfers goods, provides services, or imports goods into Japan. As of 1 April 2014, the applicable rate is 8% (previously 5%). As of 1 October 2019, the rate will increase to 10% (for certain foods, drinks, and newspapers, the tax rate will remain as 8%). Exports and certain services to non-residents are taxed at a zero rate. Specified transactions, such as sales or lease of land, sales of securities, and provision of public services, are not subject to taxation. Consumption tax paid by the business enterprise attributable to taxable revenue shall be refundable by filing the consumption tax return to the extent that such transaction is recorded in the books of account and relevant invoices are kept.

Net wealth/worth taxes

There are currently no net wealth/worth taxes in Japan.

Inheritance, estate, and gift taxes

Inheritance tax is a national tax imposed on the recipients of an inheritance (including a devise).

Effective 1 April 2017, the transfer of overseas assets between foreign nationals who have a *jusho* in Japan for less than 10 years out of the last 15 years with a visa issued under Table 1 of the Visa Status Table of Immigration Control and Refugee Recognition Act ('temporary foreigners'), with other temporary foreigners or with foreigners outside of Japan, is

exempt from Japan gift and inheritance tax. Note, however, the transfer of overseas assets with Japanese nationals who currently have a *jusho* or had a *jusho* in Japan within the previous 10 years is not exempt.

To qualify for the above exemption, foreign nationals need to meet the definition of temporary foreigners. The foreign national has to (i) have a *jusho* in Japan for not more than 10 years out of the past 15 years looking back from the date of death/gift and (ii) hold a visa issued under Table 1. Foreign nationals who satisfy (i), but fail to satisfy (ii) (i.e. hold visa issued under Table 2), will not qualify as temporary foreigners and are therefore subject to worldwide taxation of Japan gift and inheritance tax while residing in Japan, regardless of whom the transfers are made with.

Note that a Table 1 visa under the Visa Status Table of Immigration Control and Refugee Recognition Act is essentially a work related visa and does not include the following visa types: permanent resident, spouse or child of Japanese national, spouse or child of permanent resident, and long-term resident.

The transfer of overseas assets to a Japanese national heir/donee who is not a resident of Japan but either the heir/donee or the decedent/donor had a *jusho* in Japan within the past 10 years of the gift or inheritance is subject to Japan gift and inheritance tax. Similarly, the transfer of overseas assets from a Japanese national decedent/donor who is not a resident of Japan but had a *jusho* in Japan within the past 10 years of the gift or inheritance is also subject to Japan gift and inheritance tax.

This is commonly referred to as ’10-year tail’ rule for Japanese nationals, as any transfers involving Japanese nationals could be subject to Japan gift and inheritance tax for up to 10 years after permanent departure from Japan. Note that there was no transition measure in the law that exempted Japanese nationals who have permanently departed Japan prior to 1 April 2017.

A similar ‘lookback’ rule, the ‘5-year tail’ rule, was introduced in 1 April 2017 for foreign nationals who had departed Japan but had a *jusho* in Japan for 10 years out of the last 15 years. Under this rule, the transfer of the foreign nationals’ worldwide assets continue to be subject to Japan gift and inheritance tax for up to 5 years after permanent departure from Japan if they resided in Japan for 10 years or more.

However, effective 1 April 2018, the ‘5-year tail’ rule for foreign nationals who had departed Japan but had a *jusho* in Japan for 10 years out of the last 15 years was repealed for gifts and inheritances occurring on or after 1 April 2018. This is provided that the donor does not return and re-establish *jusho* within 2 years of permanent Japan departure. Otherwise, the 10-out-of-15-year lookback rule will still apply. Effectively, any overseas assets gifted occurring within the 2 years between Japan departure and return could potentially be subject to Japan gift tax.

Note that any transfers of assets located in Japan is always subject to Japan gift and inheritance tax, regardless of whom or when the transfers take place with.

Assets subject to inheritance tax include tangible, intangible, real, or personal property, unless otherwise specifically exempt under the law. The asset is valued in accordance with the provisions of the Japanese tax rules. The same rules apply to the gift tax system.

The basic exemption is JPY 30 million plus JPY 6 million per statutory heir. If the gross estate is smaller than the total amount of the basic exemption, there is no filing requirement.

After the exemption(s) is applied, the total amount of inheritance tax is determined as follows. First, the assets are allocated to individuals (referred to as statutory heirs) in accordance with the statutory inheritance proportions. Then, the graduated inheritance tax rates are applied to each statutory heir’s portion. Each statutory heir’s portion is then added together to ascertain the total inheritance tax on the assets. Then, this tax is allocated based on the actual recipient(s) of the assets (this allocation is generally based on the deceased’s will). The actual recipient will be liable for the tax payment, and the tax credit (if any) will apply to the actual taxpayer’s liabilities. In summary, the will executed in the home country of the deceased will generally be respected; however, the total amount of tax is always calculated in accordance with the statutory heir inheritance proportions.

Gift tax is a national tax levied on the recipients of a gift. The scope of gift tax is similar to inheritance tax, i.e. a taxpayer’s visa type and the time they have resided inside and outside of Japan affects which gifts may be subject to gift tax. However, the gift tax regime is not unified with inheritance tax, with the exception of a gift that is made within three years from date of death of the donor.

The annual gift exemption per recipient is JPY 1.1 million. Any amount of gift(s) received above the exemption will potentially trigger Japan gift tax.

Additionally, there is a special system where the taxpayer can make an irrevocable election to integrate inheritance and gift tax when certain conditions are met.

Under the special system, referred to as 'settlement of taxes at the time of inheritance':

- Qualified transfers are those from lineal ascendants who are aged 60 years and older made to their lineal descendants who are aged 20 years or older.
- Gifts of up to a total of JPY 25 million will be exempt from gift tax. Several gifts can be made tax-free as long as the total gifts do not exceed the JPY 25 million threshold.
- Gifts are taxed at a rate of 20% on the amount exceeding the accumulated threshold of JPY 25 million. The amount of gift tax, if any, will be treated as a prepayment of tax against a future inheritance tax liability.
- Valuation of the gifted assets will freeze at the time of the gift for the inheritance tax calculation.
- Those who made this election will automatically be subject to the inheritance tax filing regardless of the situation at the time of inheritance.

Recently, special exemptions for gifts made for designated funds have been introduced. These programs are to promote the transfer of wealth from older generations to the younger generation and allow a certain amount of gifts that are free from tax. The exemption is applicable only if the funds are used for qualified expenses. A special account based on the custody agreement must be set up to take the tax benefit. This account is usually maintained by a financial institution that has custody of the funds. Any amounts not used for qualified purposes will be subject to gift tax. Currently, JPY 15 million of educational expenses, as well as JPY 10 million of expenses for marriage and childcare, are qualified for tax-exempt gifting per recipient (due to expire on 31 March 2019).

Inheritance tax rates

Taxable properties less exemption and various exclusions (JPY)		Tax table	
Over	Not over	Tax rate (%)	Deduction (JPY)
0	10,000,000	10	0
10,000,000	30,000,000	15	500,000
30,000,000	50,000,000	20	2,000,000
50,000,000	100,000,000	30	7,000,000
100,000,000	200,000,000	40	17,000,000
200,000,000	300,000,000	45	27,000,000
300,000,000	600,000,000	50	42,000,000
600,000,000	And above	55	72,000,000

Basic estate allowance for inheritance tax: JPY 30,000,000 + (JPY 6,000,000 X number of the legal heirs)

Gift tax rates

Taxable gifts less exemptions and other exclusions (JPY)		Tax table on gifts except for the column to the right		Tax table on gifts from lineal ascendants to their descendants who are at least 20 years old	
Over	Not over	Tax rate	Deduction	Tax rate (%)	Deduction (JPY)

		(%)	(JPY)		
0	2,000,000	10	0	10	0
2,000,000	3,000,000	15	100,000	15	100,000
		3,000,000	4,000,000	20	250,000
4,000,000	6,000,000	30	650,000	20	300,000
6,000,000	10,000,000	40	1,250,000	30	900,000
10,000,000	15,000,000	45	1,750,000	40	1,900,000
15,000,000	30,000,000	50	2,500,000	45	2,650,000
30,000,000	45,000,000	55	4,000,000	50	4,150,000
		45,000,000	And above	55	6,400,000

Annual basic exemption for gift tax *: JPY 1,100,000

* This basic exemption will not be applied to the irrevocable elective system mentioned above.

Property taxes

The annual fixed assets tax is levied by the local tax authorities on real property. Real property is taxed at 1.7% (standard rate including city planning tax) of the value appraised by the local tax authorities. The depreciable fixed assets tax is assessed at 1.4% of cost after statutory depreciation.

Registration and license tax is levied where certain property is registered, at a rate from 0.1% to 2% of the taxable basis. The taxable basis depends upon the property being registered.

Luxury and excise taxes

Excise taxes were abolished by introduction of the consumption tax.

Individual - Income determination

Last Reviewed - 03 July 2019

Gross income consists of all forms of taxable income (e.g. income from employment, investment, rental real estate).

Employment income

Salary, bonuses, stock or share-based income, foreign-service premiums, cost-of-living allowances, tax reimbursements, and other benefits in kind (except for certain tax-exempt items) are classified as taxable remuneration (employment income). Japan-source employment income is remuneration earned for services rendered in Japan, regardless of where or when the remuneration is paid.

Reasonable relocation expenses, including expenses for a spouse and children, that are borne by the employer do not constitute taxable income. A reasonable amount of airfare for home leave, including airfare for family members travelling together with the employee, is generally not taxable.

Where an employer provides housing, the amount of the taxable benefit is determined based on a formula, and, provided the housing arrangements are structured properly, generally, only a percentage of the rent paid is treated as taxable.

In the case of housing provided for a director (a board member) of a domestic or foreign company, the taxable value would generally be 50% (35% if it can be substantiated that the house is also used for business purposes by the

employer) of the actual rent. However, if the housing provided by the company is considered unnecessarily luxurious, the market rent may be deemed to be the taxable value.

Retirement or severance income is treated preferentially under the current Japan tax law. However, retirement payments that are approved by a company's shareholders and are to be made to a director of the company are only eligible for preferential tax treatment if the individual has served as a director for a period of more than five years. This five-year service period must have been with the same company.

Equity compensation

For directors and employees, income arising from the exercise of stock options is generally taxed at the date of exercise (fair market value at exercise - grant price) while income from restricted stock units is taxable at the point of vesting. Income arising from certain qualified stock options (qualified for Japan tax purposes) is not taxable at exercise but is taxed instead as a capital gain when the stocks received at exercise are sold, if certain conditions are met. The point of taxation of equity compensation will depend on the specifics of the plan.

In general, for residents, income derived from the exercise of an employee stock option issued by a non-Japanese company is treated as employment income and subject to Japanese national and local inhabitant's tax at the graduated income tax rates. In addition, gains from the sale of the equity acquired are subject to income tax at 15.315% national and 5% local tax (if the individual is a tax resident) unless certain other conditions are met.

Business income

If taxpayers engage in their own business, a business enterprise tax will be levied on their business income by the local prefectural government. Business enterprise tax is deductible for the calculation of business income. In general, business enterprise tax is assessed on business income in excess of JPY 2.9 million at a rate of 3%, 4%, or 5%, depending on the type of business.

Capital gains

Capital gains are, in principle, aggregated with other income after deductions for necessary expenses and after a statutory deduction of a maximum of JPY 500,000.

If the transferred assets were owned for more than five years, the gain is regarded as a long-term capital gain, and the taxable basis is reduced to 50% of the net capital gain.

Capital gains from sales of real property (land, building and structures) are taxed separately from other sources of income. Gains on property that were held for over five years as of 1 January of the year when the transfer was made are considered as long-term capital gains and are taxed separately from other sources of income at a flat rate of 20.315% (i.e. 15.315% national tax and 5% local inhabitant's tax). Gains on property that were held for five years or less are classified as short-term capital gains and are taxed at a flat rate of 39.63% (i.e. 30.63% national tax and 9% local inhabitant's tax).

Capital gains from sales of certain securities (including shares/equity interest in corporations, warrant bonds, etc.) are taxed separately from other sources of income at a flat rate of 20.315% (i.e. 15.315% national tax and 5% local inhabitant's tax).

Listed shares are shares listed on Japanese or foreign stock exchanges and government bonds, etc. Unlisted shares are shares other than listed shares indicated above.

From 1 January 2016, capital gains/losses arising from the sale of listed shares cannot be used to offset capital losses/gains arising from the sale of non-listed shares.

Dividend income

In principle, dividends are either taxed at (i) graduated rates after being aggregated with other sources of income or (ii) separately from other sources of income; however, certain capital losses may be used to absorb dividend income (*see Losses in the Deductions section for more information*). If paid onshore, dividends are subject to withholding tax (WHT). Dividends paid by corporations listed on an exchange are opt to be taxed at a flat rate of 20.315% (i.e. 15.315% national tax and 5% local inhabitant's tax).

Interest income

Interest on domestic bank deposits and/or certain designated financial instruments is taxed separately from other income and is subject to 20.315% WHT (i.e. 15.315% national tax and 5% local inhabitant's tax) if paid onshore. Interest paid by offshore financial institutions is taxed at graduated rates. Interest on bonds listed on an exchange is taxed at a flat rate of 20.315% (i.e. 15.315% national tax and 5% local inhabitant's tax).

Rental income

Rental income consists of gross rents received in connection with the letting of real estate to either an individual or commercial tenant. To arrive at the taxable amount, any allowable expenses and depreciation are deducted from the gross income. To the extent a taxpayer has a net rental loss, this loss can be used to offset other types of income. Note that mortgage interest payments allocable to the ownership of land can't be used to offset other types of non-rental income.

Non-resident's income

Assuming the non-resident does not have a permanent establishment (PE) in Japan, a non-resident's income from Japan-source interest, dividends, rental income, and royalties is generally subject to tax at a rate of 20.42% (15.315% in the case of interest on bank deposits and/or certain designated financial instruments) or lower treaty rates through WHT at source. A tax return is subsequently required to be filed to report rental income and determine the final tax liability.

Individual - Deductions

Last Reviewed - 03 July 2019

Employment expenses

A resident taxpayer who earns income from employment is eligible for an earned income deduction for purposes of both the national income and local inhabitant's tax. The amount of the deduction is based on the amount of the employment income and is determined by reference to a deduction table.

Personal deductions

Interest is not tax deductible. Japanese social security contributions are fully deductible. Medical expenses (irrespective of where they were paid) are tax deductible, with certain limitations.

Charitable contributions

Charitable contributions designated by the Ministry of Finance in Japan are tax deductible, with certain limitations. Qualified contributions or donations that total, in aggregate, over JPY 2,000 are deductible in computing the national tax. The total deduction is limited to 40% of income, less JPY 2,000. The definition of a qualified contribution is extremely restrictive (*see the Other tax credits and incentives section for more information*).

Life insurance premiums

Life insurance (or private pension) premiums paid to a Japanese agency in local currency are deductible to a limited extent in computing national and local inhabitants taxes.

Earthquake insurance premiums are also deductible for the purpose of both national and local inhabitant's tax to a limited extent.

Mortgage deductions

Mortgage interest is not tax deductible. However, a tax credit on housing loans may be available for up to ten years where certain conditions are met. The total amount of tax credit is determined by the year in which the taxpayer began to reside in the property as well as mortgage balance at the end of the tax year.

Standard deduction

Prior to the 2018 Japan Tax Reforms, a permanent and/or non-permanent resident employee can take an earned income deduction, computed by applying an appropriate rate to gross employment income as follows (the minimum standard deduction is JPY 650,000 or gross employment income, whichever is lower). The deduction is currently capped at JPY 2.2 million.

Taxable income (JPY)		Formula for exclusion amount calculation	Salary income exclusion - up to 2019 (JPY)
Over	Not over		
0	1,800,000	40% of income	650,000 minimum, up to 720,000
1,800,000	3,600,000	30% of income + 180,000	720,000 minimum, up to 1,260,000
3,600,000	6,600,000	20% of income + 540,000	1,260,000 minimum, up to 1,860,000
6,600,000	10,000,000	10% of income + 1,200,000	1,860,000 minimum, up to 2,200,000
10,000,000			2,200,000

Personal exemptions

Prior to the 2018 Japan Tax Reforms, resident taxpayers are entitled to a personal exemption (JPY 380,000 for national income tax purposes, JPY 330,000 for local inhabitant's tax purposes) for themselves and their dependent spouses.

In the case of a non-dependent spouse, a special spouse exemption (a maximum JPY 380,000 and JPY 330,000 for national income tax purposes and local inhabitant's tax purposes) can be taken, depending on the spouse's income, by taxpayers whose income amount does not exceed JPY 10 million.

Resident taxpayers are allowed a deduction for each dependant who is 16 years or older. A dependant is a relative, other than a spouse, who is supported by the taxpayer provided that the dependant's income does not exceed JPY 380,000 for the year. The dependant is not required to live with the taxpayer but should receive support from the taxpayer as part of the taxpayer's household. The amount of the deduction increases if the dependant is aged 70 or older at the end of the year or is at least 19 years old but less than 23 years of age. For each category of dependants, the deductions also increase if the dependant is a handicapped person.

In general, a non-resident taxpayer is not permitted to take any of these deductions.

Business deductions

Business expenses are tax deductible in some limited cases. An employer's reimbursements of business expenses, such as moving, travel, and entertainment expenses, do not constitute taxable income to the employee, provided the expenses are required for the employer's business.

A self-employed taxpayer is allowed to claim business expenses against income, provided it can be substantiated that the expenses are necessary.

Losses

Currently, capital losses derived from the sale of listed shares may be offset against dividends from listed shares for the same year up to the amount of the dividends, provided the taxpayer elects separate taxation by filing. With effect from 1 January 2016, interest income and capital losses derived from specified bonds was included in this offset arrangement; and, accordingly, capital losses arising from the sale of listed shares and specified bonds ('listed shares group') will be offset against dividends from listed shares and interest from specified bonds, provided separate taxation by filing is elected.

Under current tax law, capital losses within the listed shares group after offset against dividends and interest may be carried over for three years.

Individual - Foreign tax relief and tax treaties

Last Reviewed - 03 July 2019

Foreign tax relief

Resident taxpayers can credit foreign income taxes against their Japanese national tax and local inhabitant's tax liabilities (with certain limitations), where non-Japan-source income is taxed in Japan. Non-resident taxpayers are not entitled to take foreign tax credits on their Japan income tax returns unless one has a PE in Japan.

Tax treaties

Japan has tax treaties with the following countries:

Australia	Hungary	Panama
Austria	Iceland	Philippines
Bahamas	India	Poland
Bangladesh	Indonesia	Portuguese Republic
Belgium	Ireland, Republic of	Qatar
Bermuda	Isle of Man	Romania
Brazil	Israel	Samoa
British Virgin Islands	Italy	Saudi Arabia
Brunei	Jersey	Singapore
Bulgaria	Kazakhstan	Slovenia
Canada	Korea, Republic of	South Africa
Cayman Islands	Kuwait	Spain
Chile	Latvia	Sri Lanka
China	Liechtenstein	Sweden
Czechoslovakia (1)	Lithuania	Switzerland
Denmark	Luxembourg	Taiwan
Egypt	Macao	Thailand
Estonia	Malaysia	Turkey
Fiji	Mexico	USSR (2)
Finland	Netherlands	United Arab Emirates
France	New Zealand	United Kingdom
Germany	Norway	United States
Guernsey	Oman	Vietnam

Hong Kong	Pakistan	Zambia

Notes

1. The treaty with the former Czechoslovakia is applied to the Czech Republic and the Slovak Republic.
2. The treaty with the former USSR is applied to Armenia, Azerbaijan, Belarus, Georgia, Kyrgyzstan, Moldova, Russia, Tajikistan, Turkmenistan, Ukraine, and Uzbekistan.

Mutual Administrative Assistance

Japan has signed a Convention on Mutual Administrative Assistance in Tax Matters and it is effective.

Base Erosion and Profit Shifting (BEPS) Agreement

On 7 June 2017, Japan signed a Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS, which will not be effective until the instrument of ratification is submitted. It is effective with Australia, Finland, France, Ireland, Israel, Netherlands, New Zealand, Poland, Singapore, Slovakia, Sweden, and the United Kingdom.

Totalisation agreements

Designed to avoid overlaps in social security enrolment, Japan has entered into social security agreements with several countries. The agreements currently in effect are with Australia, Belgium, Brazil, Canada, the Czech Republic, France, Germany, Hungary, India, Ireland, Korea, Luxembourg, the Netherlands, Philippines, Slovak Republic, Spain, Switzerland, the United Kingdom, and the United States. Agreements with China, Italy, and Sweden have been signed and are in the process of implementation.

Individual - Other tax credits and incentives

Last Reviewed - 03 July 2019

For local tax purposes, contributions to the community chest, the Japan Red Cross, the prefecture and municipality, and groups approved by each prefecture/municipality under their regulations, qualify as creditable charitable contributions. Contributions over a standard JPY 2,000 base amount are deductible, subject to a cap.

Individual - Tax administration

Last Reviewed - 03 July 2019

Taxable period

The Japanese individual income tax year runs from 1 January to 31 December.

Tax returns

All income tax returns are filed on an individual basis in Japan; joint tax returns are not permitted. The tax year is the calendar year for all resident-status individuals, and a taxpayer is required to file a national tax return by 15 March of the following year.

If a taxpayer’s income consists only of employment income paid by one local employer (including a Japanese branch of a foreign corporation) that does not exceed JPY 20 million in a year, the payer of the income makes a so-called ‘year-end adjustment’ on the employment income, and if total income other than employment income is JPY 200,000 or less, the employee is not required to file an income tax return.

Overseas Assets Reporting

Permanent residents of Japan who own assets outside of Japan that exceed JPY 50 million in value as of 31 December of the year must disclose such assets by submitting an annual report by 15 March of the following year.

Assets and Liabilities Reporting

Asset and liability reporting is required for those who have total income on the tax return exceeding JPY 20 million and hold worldwide assets with a gross fair value of JPY 300 million or more, or securities of JPY 100 million or more as of 31 December. Individuals meeting the conditions will need to report, in detail, of their worldwide assets and liabilities. These reports are not a part of the income tax return and need to be filed separately with the tax office by 15 March of the following year.

Payment of tax

If salary is paid in Japan by a local employer, monthly withholding of national income tax is required. The national tax due on overseas payments of salary is payable when the tax return is filed, rather than through payroll withholding. Two provisional payments of national tax are required in July and November if the previous year's final tax liability (after the deduction of WHT) was JPY 150,000 or more.

Local inhabitant's tax is assessed on the prior year's income if a taxpayer is registered as a resident as of 1 January of the current year. The tax is paid on a four instalment basis (i.e. in June, August, October, and January of the following year) or withheld from monthly salary from June through May of the following year if the salary is paid in Japan.

Tax audit process

The tax authority of Japan is the National Tax Agency, and audits are conducted randomly.

Statute of limitations

The standard statute of limitations under audit is currently five years, though this can be extended in cases of tax evasion.

Topics of focus for tax authorities

The topics covered under tax audits can be wide ranging and varied and will largely depend on the individual taxpayer.

Individual - Sample personal income tax calculation

Last Reviewed - 03 July 2019

National tax	JPY
Gross taxable income	10,000,000
Earned income deduction	(2,200,000)
Income after earned income deduction	7,800,000
Total deductions	(380,000)
Taxable basis	**7,420,000**
Gross national tax liability	1,070,600
2.1% national surtax	22,482
Total gross national tax liability	1,093,082

National tax due	**1,093,000**
Local inhabitant's tax	**JPY**
Gross taxable income	10,000,000
Earned income deduction	(2,200,000)
Income after earned income deduction	7,800,000
Total deductions	(330,000)
Taxable basis	**7,470,000**
Prefectural tax due	299,300
Municipal tax due	450,200
Local inhabitant's tax due	**749,500**
Total tax due	**1,842,500**

Individual - Other issues

Content Not Available

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